

**I SEMESTER BBA STUDY MATERIAL**  
**1.3 FUNDAMENTALS OF ACCOUNTING**

## **CHAPTER - I**

### **INTRODUCTION TO ACCOUNTING**

#### **INTRODUCTION**

In all activities (whether business activities or non-business activities) and in all organizations (whether business 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.

#### **MEANING AND DEFINITION OF BOOK- KEEPING**

##### **Meaning**

Book- keeping includes recording of journal, posting in ledgers and balancing of accounts. All the records before the preparation of trail balance is the whole subject matter of book-keeping. It is important to note that only those transactions related to business and which can be expressed in terms of money are recorded.

##### **Definition**

“Book- keeping is the art of recording business transactions in a systematic manner”.

A.H.Rosenkamph.

“Book- keeping is the science and art of correctly recording in books of account all those business transactions that result in the transfer of money or money’s worth”. R.N.Carter

#### **ACCOUNTING**

##### **Meaning of Accounting**

Accounting, as an information system is the process of identifying, measuring and communicating the economic information of an organization to its users who need the information for decision making. It identifies transactions and events of a specific entity. An entity means an economic unit that performs economic activities. Business transaction is a transaction in which money or money’s worth is involved.

##### **Definition of Accounting**

American Institute of Certified Public Accountants (AICPA) which defines accounting as “an art of recording, classifying and summarizing in a significant manner and in terms of money, transactions and events, which are, in part at least, of a financial character and interpreting the results thereof”.

##### **Objective 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.

**i) To keeping 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.

**ii) To ascertain whether the business operations have been profitable or not:** Accounting helps in ascertaining result i.e., profit earned or loss suffered in business during a particular period.

For this purpose, a business entity prepares either a Trading and Profit and Loss account or an Income and Expenditure account which shows the profit or loss of the business by matching the items of revenue and expenditure of the same period.

**iii) 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 barometers of health of a business entity.

**iv) 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.

**v) To protect business properties:** Accounting provides upto 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.

#### **Users of Accounting Information:**

**i) Owners:** The owners provide funds or capital for the organization. They possess curiosity in knowing whether the business is being conducted on sound lines or not and whether the capital is being employed properly or not

**ii) Management:** The management of the business is greatly interested in knowing the position of the firm. The accounts are the basis, the management can study the merits and demerits of the business activity. Thus, the management is interested in financial accounting to find whether the business carried on is profitable or not.

**iii) Creditors:** Creditors are the persons who supply goods on credit, or bankers or lenders of money. It is usual that these groups are interested to know the financial soundness before granting credit.

**iv) Employees:** Employees are interested in the financial position of the concern particularly when payment of bonus depends upon the size of the profits earned.

**v) Investors:** The prospective investors, who want to invest their money in a firm, of course wish to see the progress and prosperity of the firm, before investing their amount, by going through the financial statements of the firm.

**vi) Government:** Government keeps a close watch on the firms which yield good amount of profits. The state and central Governments are interested in the financial statements to know the earnings for the purpose of taxation.

**vii) Research Scholars:** Accounting information, being a mirror of the financial performance of a business organization, is of immense value to the research scholar who wants to make a study into the financial operations of a particular firm.

## Functions of Accounting

**1. Record Keeping Function:** The primary function of accounting relates to recording, classification and summary of financial transactions-journalisation, posting, and preparation of final statements. These facilitate to know operating results and financial positions. The purpose of this function is to report regularly to the interested parties by means of financial statements.

**ii) Managerial Function:** Decision making programme is greatly assisted by accounting. The managerial function and decision making programmes, without accounting, may mislead.

**iii) Legal Requirement function:** Auditing is compulsory in case of registered firms. Auditing is not possible without accounting. Thus accounting becomes compulsory to comply with legal requirements. Accounting is a base and with its help various returns, documents, statements etc., are prepared.

**iv) Language of Business:** Accounting is the language of business. Various transactions are communicated through accounting.

## Advantages of Accounting

The following are the advantages of accounting to a business:

- i) It helps in having complete record of business transactions.
- ii) It gives information about the profit or loss made by the business at the close of a year and its financial conditions.
- iii) It provides useful information for making economic decisions,
- iv) It facilitates comparative study of current year's profit, sales, expenses etc., with those of the previous years.
- v) It supplies information to judge the management's ability to utilise enterprise resources effectively in achieving primary enterprise goals.
- vi) It provides users information about transactions and other events which are useful for predicting, comparing and evaluating the enterprise's earning power.
- vii) Errors & Frauds can be minimized.

## Limitations of Accounting

1. Records only monetary transactions .
2. Effect of price level changes are not considered.
3. No Realistic information.
4. Personal bias of Accountant affects the accounting statements.
5. Permits alternative treatments.
6. No real test of managerial performance.
7. Accounting statements do not show the impact of inflation.

## Methods of Accounting

Business transactions are recorded in two different ways.

Single Entry System

Double Entry System

**Single Entry System:** It is incomplete system of recording business transactions. The business organization maintains only cash book and personal accounts of debtors and creditors. So the complete recording of transactions cannot be made and trail balance cannot

be prepared.

**Double Entry System:** In this system every business transaction is having a two fold effect of benefits giving and benefit receiving aspects. The recording is made on the basis of both these aspects. Double Entry is an accounting system that records the effects of transactions and other events in at least two accounts with equal debits and credits.

### **Steps involved in Double entry system**

(a) **Preparation of Journal:** Journal is called the book of original entry. It records the effect of all transactions for the first time. Here the job of recording takes place.

(b) **Preparation of Ledger:** Ledger is the collection of all accounts used by a business. Here the grouping of accounts is performed. Journal is posted to ledger.

(c) **Trial Balance preparation:** Summarizing. It is a summary of ledger balances prepared in the form of a list.

(d) **Preparation of Final Account:** At the end of the accounting period to know the achievements of the organization and its financial state of affairs, the final accounts are prepared.

### **Advantages of Double Entry System**

i) **Scientific system:** This system is the only scientific system of recording business transactions in a set of accounting records. It helps to attain the objectives of accounting.

ii) **Complete record of transactions:** This system maintains a complete record of all business transactions.

iii) **A check on the accuracy of accounts:** By use of this system the accuracy of accounting book can be established through the device called a Trial balance.

iv) **Ascertainment of profit or loss:** The profit earned or loss suffered during a period can be ascertained together with details by the preparation of Profit and Loss Account.

v) **Knowledge of the financial position of the business:** The financial position of the firm can be ascertained at the end of each period, through the preparation of balance sheet.

vi) **Comparative study is possible:** Results of one year may be compared with those of the previous year and reasons for the change may be ascertained.

vii) **Helps management in decision making:** The management may be also to obtain good information for its work, specially for making decisions.

viii) **No scope for fraud:** The firm is saved from frauds and misappropriations since full information about all assets and liabilities will be available.

## **BRANCHES OF ACCOUNTING**

The changing business scenario over the centuries gave rise to specialized branches of accounting which could cater to the changing requirements. The branches of accounting are;

- i) Financial accounting;
- ii) Cost accounting; and
- iii) Management accounting.

### **Financial Accounting**

The accounting system concerned only with the financial state of affairs and financial results of operations is known as Financial Accounting. It is the original form of accounting. It is mainly concerned with the preparation of financial statements

### **Cost Accounting**

In view of the limitations of financial accounting in respect of information relating to the cost of individual products, cost accounting was developed. It is that branch of accounting which is concerned with the cost ascertainment and cost control. Cost accounting seeks to ascertain the cost of unit produced and sold or the services rendered by the business unit with a view to exercising control over these costs to assess profitability and efficiency of the enterprise. It generally relates to the future and involves an estimation of future costs to be incurred.

### **Management Accounting**

It is an accounting for the management i.e., accounting which provides necessary information to the management for discharging its functions. According to the Anglo-American Council on productivity, "Management accounting is the presentation of accounting information in such a way as to assist management in the creation of policy and the day-to-day operation of an undertaking."

## PRINCIPLES OF ACCOUNTING

### ACCOUNTING CONCEPTS AND CONVENTIONS

#### Accounting concepts:

The term 'concept' is used to denote accounting postulates, i.e., basic assumptions or conditions upon which the accounting super-structure is based. The following are the common accounting concepts adopted by many business concerns.

1. Business Entity Concept
2. Money Measurement Concept
3. Going Concern Concept
4. Dual Aspect Concept
5. Accounting Period Concept
6. Cost Concept
7. Matching Concept
8. Realisation Concept
9. Accrual Concept
10. Objective Evidence Concept

**i) Business Entity Concept:** A business unit is an organization of persons established to accomplish an economic goal. Business entity concept implies that the business unit is separate and distinct from the persons who provide the required capital to it. This concept can be expressed through an accounting equation, viz,

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

**ii) Money Measurement Concept:** In accounting all events and transactions are recorded in terms of money. Money is considered as a common denominator, by means of which various facts, events and transactions are recorded. Those transactions which can be measured in terms of money will be recorded in the books of accounts.

**iii) Going Concern Concept:** Under this concept, the transactions are recorded assuming that the business will exist for a longer period of time, i.e., a business unit is considered to be a going concern and not a liquidated one. Keeping this in view, the suppliers and other companies enter into business transactions with the business unit. This assumption supports the concept of valuing the assets at historical cost or replacement cost. This concept also supports the treatment of prepaid expenses as assets, although they may be practically unsaleable.

**iv) Dual Aspect Concept:** According to this basic concept of accounting, every transaction has a two-fold aspect, viz., 1. giving certain benefits and 2. Receiving certain benefits. The basic principle of double entry system is that every debit has a corresponding and equal amount of credit. This is the underlying assumption of this concept. The accounting equation viz.,  $\text{Assets} = \text{Capital} + \text{Liabilities}$  or  $\text{Capital} = \text{Assets} - \text{Liabilities}$ , will further clarify this concept, i.e., at any point of time the total assets of the business unit are equal to its total liabilities. Liabilities here relate both to the outsiders and the owners. Liabilities to the owners are considered as capital.

**v) Accounting Period Concept:** Under this concept, the life of the business is segmented into different periods and accordingly the result of each period is ascertained. Though the business is assumed to be continuing in future (as per going concern concept), the measurement of income and studying the financial position of the business for a shorter and definite period will help in taking corrective steps at the appropriate time. Each segmented

period is called “accounting period” and the same is normally a year. At the end of an accounting period, an Income Statement is prepared to ascertain the profit or loss made during that accounting period and Balance Sheet is prepared which depicts the financial position of the business as on the last day of that period.

**vi) Cost Concept:** According to this concept, the transactions are recorded in the books of account with the respective amounts involved. For example, if an asset is purchased it is entered in the accounting record at the price paid to acquire the same and that cost is considered to be the base for all future accounting.

**vii) Matching Concept:** The essence of the matching concept lies in the view that all costs which are associated to a particular period should be compared with the revenues associated to the same period to obtain the net income of the business. Under this concept, the accounting period concept is relevant and it is this concept (matching concept) which necessitated the provisions of different adjustments for recording outstanding expenses, prepaid expenses, outstanding incomes, incomes received in advance, etc., during the course of preparing the financial statements at the end of the accounting period.

**viii) Realisation Concept:** This concept assumes or recognizes revenue when a sale is made. Sale is considered to be complete when the ownership and property are transferred from the seller to the buyer and the consideration is paid in full. However, there are two exceptions to this concept, viz., 1. Hire purchase system where the ownership is transferred to the buyer when the last instalment is paid and 2. Contract accounts, in which the contractor is liable to pay only when the whole contract is completed, the profit is calculated on the basis of work certified each year.

**ix) Accrual Concept:** According to this concept the revenue is recognized on its realization and not on its actual receipt. Similarly the costs are recognized when they are incurred and not when payment is made. This assumption makes it necessary to give certain adjustments in the preparation of income statement regarding revenues and costs. But under cash accounting system, the revenues and costs are recognized only when they are actually received or paid. Hence, the combination of both cash and accrual system is preferable to get rid of the limitations of each system.

**x) Objective Evidence Concept:** This concept ensures that all accounting must be based on objective evidence, i.e., every transaction recorded in the books of account must have a verifiable document in support of its existence. Only then, the transactions can be verified by the auditors and declared as true or otherwise. The verifiable evidence for the transactions should be free from the personal bias, i.e., it should be objective in nature and not subjective.

### **Accounting Conventions**

The following conventions are to be followed to have a clear and meaningful information and data in accounting:

**i) Consistency:** The convention of consistency refers to the state of accounting rules, concepts, principles, practices and conventions being observed and applied constantly, i.e., from one year to another there should not be any change. If consistency is there, the results and performance of one period can be compared easily and meaningfully with the other. It

also prevents personal bias as the persons involved have to follow the consistent rules, principles, concepts and conventions. This convention, however, does not completely ignore changes. It admits changes wherever indispensable and

adds to the improved and modern techniques of accounting.

**ii) Disclosure:** The convention of disclosure stresses the importance of providing accurate, full and reliable information and data in the financial statements which is of material interest to the users and readers of such statements. This convention is given due legal emphasis by the Companies Act, 1956 by prescribing formats for the preparation of financial statements. However, the term disclosure does not mean all information that one desires to get should be included in accounting statements. It is enough if sufficient information, which is of material interest to the users, is included.

**iii) Conservatism:** In the prevailing present day uncertainties, the convention of conservatism has its own importance. This convention follows the policy of caution or playing safe. It takes into account all possible losses but not the possible profits or gains. A view opposed to this convention is that there is the possibility of creation of secret reserves when conservatism is excessively applied, which is directly opposed to the convention of full disclosure. Thus, the convention of conservatism should be applied very cautiously

**iv) Materiality:** It means that in accounting a detailed record is made only of those transactions which are material (important). No detailed record is made of those transactions, which are insignificant as the work of recording the minute details of such transactions will be very high. Materiality depends on the amount involved in the transaction. For example, minor expenditure of Rs.50 for the purchase of a dust bin may be treated as an expense of the period rather than an asset.

### **BASES OF ACCOUNTING**

There are three bases of accounting in common usage. Any one of the following bases may be used to finalise accounts.

1. Cash basis
2. Accrual or Mercantile basis
3. Mixed or Hybrid basis.

### **Accounting on 'Cash basis**

Under cash basis accounting, entries are recorded only when cash is received or paid. No entry is passed when a payment or receipt becomes due. Income under cash basis of accounting, therefore, represents excess of receipts over payments during an accounting period. Government system of accounting is mostly on cash basis.

### **Accrual Basis of Accounting or Mercantile System**

Under accrual basis of accounting, accounting entries are made on the basis of amounts having become due for payment or receipt. Incomes are credited to the period in which they are earned whether cash is received or not. Similarly, expenses and losses are debited to the period in which, they are incurred, whether cash is paid or not. The profit or loss of any accounting period is the difference between incomes earned and expenses incurred, irrespective of cash payment or receipt. All outstanding expenses and prepaid expenses, accrued incomes and incomes received in advance are adjusted while finalising the accounts.

Under the Companies Act 1956, all companies are required to maintain the books of accounts according to accrual basis of accounting.

### **Mixed or Hybrid Basis of Accounting**

When certain items of revenue or expenditure are recorded in the books of account on cash basis and certain items on mercantile basis, the basis of accounting so employed is called 'hybrid basis of accounting'. For example, a company may follow mercantile system of accounting in respect of its export business. However, government subsidies and duty drawbacks on exports to be received from government are recorded only when they are actually received i.e., on cash basis.

### **ACCOUNTING EQUATION**

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

$$\text{Assets} = \text{Equities}$$

The equation is based on the principle that accounting deals with property and rights to property and the sum of the properties owned is equal to the sum of the rights to the properties. The properties owned by a business are called assets and the rights to properties are known as liabilities or equities of the business. Equities can be subdivided into equity of the owners which is known as capital and equity of creditors who represent the debts of the business known as liabilities.

These equities may also be called internal equity and external equity. Internal equity represents the owner's equity in the assets and external represents the outsider's interest in the asset. Based on the bifurcation of equity, the accounting equation can be restated as follows:

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

(Or)

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

(Or)

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

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

#### **1 Rules for accounting equation:**

Following rules help in making the accounting equation:

**Assets:** If there is increase in assets, this increase is debited in assets account. If there is decrease in assets, this decrease credited in assets account.

**Liabilities:** When liabilities are increase, outsider's equities are credited and when liabilities

are decreased, outsider's equities are debited.

**Capital:** When capital is increased, it is credited and when capital is withdrawn, it is debited.

**Expenses:** Owner's equity is decreased by the amount of revenue expenses.

**Income or profits:** Owner's equity is increased by the amount of revenue income.

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## LESSON JOURNAL AND LEDGER

### INTRODUCTION

Journal is a book of original entry where in transactions are first recorded. All transactions are recorded in the journal in the order in which they take place. Thus journal is a simple book of accounts in which all the business transactions are originally recorded in chronological order and from which they are posted to the ledger accounts at any convenient time. Journaling refers to the act of recording each transaction in the journal. The form, in which it is recorded, is known as a journal entry.

### **ADVANTAGES OF JOURNAL**

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

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

#### **Compound Journal Entry**

When two or more transactions of the same nature take place on the same date , a compound or combined journal entry may be passed for the same instead of passing separate entry for each transaction. Compound journal entry is one where two or more accounts are debited or two or more accounts are credited.

### LEDGER

Ledger is a main book of account in which various accounts of personal, real and nominal nature, are opened and maintained. It is a summary statement of all transactions relating to a person ,assets, expenses or incomes which have taken place during a particular period of time. when transactions take place, they are first entered in the journal and subsequently posted to the concerned accounts in the ledger. Posting refers to the process of entering in the ledger the information given in the journal.

#### **Distinction between journal and ledger**

- 1.Journal is a book of prime entry, whereas ledger is a book of final entry.
- 2.Transactions are recorded daily in the journal, whereas posting in the ledger is made periodically.
- 3.In the journal, information about a particular account is not found at one place, whereas in the ledger information about a particular account is found at one place only.
- 4.Recording of transactions in the journal is called journalising and recording of transactions in the ledger is called posting.
- 5.A journal entry shows both the aspects debit as well as credit but each entry in the ledger shows only one aspect.
- 6.Narration is written after each entry in the journal but no narration is given in the ledger.
- 7.Vouchers, receipts, debit notes, credit notes etc., from the basic documents form journal

entry, whereas journal constitutes basic record for ledger entries.

## ILLUSTRATIONS

**Journalise the following transactions in the books of Imran:  
2012**

**Jan 1** Commenced business with cash Rs.5,00,000

3 Purchased furniture for cash Rs.20,000

5 Deposited with Bank Rs.30,000

6 Goods worth Rs.2000 given as charity.

10 Sold goods to Ramakrishnan on credit Rs.10,000

15 Bought from Raman & Co. goods worth Rs.50,000 at 10% trade discount

18 Received a first and final dividend of 70 paise in the rupee from the official receiver  
Of Mr.Rakesh

Who owed in Rs.10,000

20. Received Rs.9750 from Ramakrishnan in full settlement of his account for  
Rs.10,000

21. Goods worth Rs.3,000 were used by the proprietor for personal use.

25. Supplied goods costing Rs.2,000 to Madan issued invoice at 20% above cost less 5%  
trade discount

28. Stationery purchased for Rs.50

31. paid salaries Rs.3000

### Journal Entries in the books of Imran

Date	Particulars	LF	Debit	Credit
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1.1.12	Cash Account Dr To Imran's Capital A/c ( Being Capital introduced )	5,00,000	5,00,000
3.1.12	Furniture A/c Dr To Cash (Being Furniture purchased)	20,000	20,000
5.1.12	Bank Account Dr To Cash (Being cash deposited in the bank)	30,000	30,000
6.1.12	Charity Account Dr To Purchases ( Being goods donated)	2,000	2,000
10.1.12	Ramakrishnan Account Dr To Sales ( Being credit sales made)	10,000	10,000
15.1.12	Purchases Account Dr To Raman & Co ( Being credit purchases made)	45,000	45,000
18.1.12	Cash Account Dr Bad Debts Account Dr To Rakesh ( Being received 70 paise per rupee from the official receiver of Rakesh)	7,000 3,000	10,000
20.1.12	Cash Account Dr Discount Account Dr	9,750 250	10,000
21.1.12	To Ramakrishnan Drawings Account Dr To Purchases ( Being goods withdrawn by the proprietor for personal use)	3,000	3,000
23.1.12	Madan Account Dr	2,280	2,280
28.1.12		500	500
31.1.12		3,000	3,000

	<p><b>To Sales</b>  <b>( Being sold goods costing Rs2,000</b>  <b>@20% above cost and 5% trade</b>  <b>discount to Madan)</b></p> <p><b>Stationery A/c</b>  <b>Dr</b>  <b>To Cash</b>  <b>( Being stationery purchased)</b></p> <p><b>Salaries A/c</b>  <b>Dr</b>  <b>To Cash</b>  <b>( Being salaries paid</b></p>			
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## SUBSIDIARY BOOKS

### INTRODUCTION

Transactions are first recorded in the Journal as and when they take place. From the journal they are posted to the ledger. To save time and labour, journal is usually sub divided in such a fashion that transactions of a similar nature are entered in separate journals.

Division of journal into various books which will enable recording of transactions of similar nature is called subsidiary books. Where subsidiary books are maintained instead of one journal there will be several special journals.

### Features of subsidiary books

1. Subordinate to the main books of accounts.
2. Books of original entry.
3. Transactions are not journalized.
4. Special journals as each subsidiary book is maintained to record a particular type of transactions.
5. Entered daily in the subsidiary book

### KINDS OF SUBSIDIARY BOOKS

There are different types of subsidiary books which are commonly used in any big business concern. They are

- |                           |                       |
|---------------------------|-----------------------|
| 1 Purchases Book          | 2 Sales Book          |
| 3 Purchases Returns Books | 4 Sales Returns Books |
| 5 Bills Receivable Books  | 6 Bills Payable Books |
| 7 Cash Book               | 8 Journal Proper      |

### **Purchases Book**

This book is used to record all credit purchases made by the business concern from its suppliers. This book is also known as 'Purchases Books', 'Purchases Journal' or 'Invoice Book'. It contains five columns, viz., Date, Particulars, Ledger Folio, Inward Invoice Number and Amount. Whenever any credit purchase is made, the date on which the transaction has taken place is entered in the 'Date Column', the name of the party from whom the purchase has been made the particulars column, the inward invoice number with which the purchase has been made in the 'inward Invoice Number Column' and the money value of the purchase in the 'Amount Column'. The 'L.F. Column' is to record the ledger folio number while posting is made.

### **INVOICE**

An invoice is a statement describing the goods dispatched to the buyer and showing the total amount payable by him on account of the transaction.

Invoice is a statement describing in

**Posting:** The total of purchases book for a specified period is debited to the purchases

account in the Ledger. The personal accounts are posted by crediting the individual accounts.

### **Sales books**

This book is used to record all credit sales effected by the business to its customers. This book is also called as 'Sales Book', 'sales Journal' or 'Sold Book'. It contains five columns, viz., Date, Particulars, L.F., Outward Invoice Number and Amount. When any credit sales is effected, the date is entered in the 'Date Column', the name of the party to whom the sale is made in the 'Particulars Column', the invoice number with which the sales have been effected in the 'Out-ward Invoice Number Column' and the money value of the sales in the 'Amount Column', The LF column is entered while posting is effected.

**Posting:** The total of the Sales Book for a specified period is credited to the Sales Account in the Ledger. The personal account is posted by debiting the individual accounts.

### **Purchases Returns Books**

This book is used to record all transactions relating to the goods returned to suppliers. This book is also known as 'Purchases Returns journal' or 'Returns Outward Book',

The columns in this book are similar to those of Purchases Book except the Debit Note Column in which the debit note number is recorded. The Purchaser who returns the goods prepares a Debit Note. While posting, all the personal accounts are debited in the Ledger and the total of Purchases Returns Book is credited to Purchases Returns Account.

### **Debit Note**

A Statement prepared by the purchaser of goods and given to the seller or supplier of goods informing the supplier that his account has been debited. It is a note prepared at the time of returning the goods.

### **Sales Returns Books**

This book is used to record all transactions relating to goods returned by customers. This book is also known as 'Sales Return Journal' or 'Returns Inwards Book' the columns in this book are similar to those of Sales Book except the Credit Note Column in which the credit note number is recorded.

### **Credit Note**

A Statement sent by the seller to the purchaser for the goods returned by the latter to the former. It is called a credit note because the party's account is credited with the amount written in it.

### **Bills Receivable Book:**

When goods are sold on credit the seller may expect a written promise from the purchaser that he will pay the amount due on a certain date. The seller orders the purchaser to pay the amount due to him or his order. This order is called a Bills of Exchange. The seller calls this Bill Receivable because he has to receive payment on such bills. When there are many bills receivable separate subsidiary book called Bills receivable book is maintained.

### **Bills Payable Book:**

This book is used to record all the bills accepted by the business drawn by its creditors. It contains details regarding the name of the drawer, payee and date of acceptance, due date, place of payment, term and amount of the bill While posting the individual drawer or payee

account is debited and the Bills payable Account is credited with the total in the Bills Payable Book.

### **Journal Proper**

This book is used to record all the residual transactions which cannot find place in any of the subsidiary books. While recording, the entries are made in the journal covering both the aspects of the transaction. The following are some of the examples of transactions which are entered in this book.

1. Opening entries and closing entries.
2. Adjusting entries
3. Transfer entries from one account to another account.
4. Rectification entries.
5. Bills of Exchange Entries
6. Credit Purchase/sale of an asset other than goods.

### **Cash Book**

Cash Book is a sub-division of Journal recording transactions pertaining to cash receipts and payments. Firstly, all cash transactions are recorded in the Cash Book wherefrom they are posted subsequently to the respective ledger accounts. The Cash Book is maintained in the form of a ledger with the required explanation called as narration and hence, it plays a dual role of a journal as well as ledger. All cash receipts are recorded on the debit side and all cash payments are recorded on the credit side. All cash transactions are recorded chronologically in the Cash Book. The Cash Book will always show a debit balance since payments cannot exceed the receipts at any time.

**Kinds of Cash Book:** From the above it can be observed that the Cash Book serves as a subsidiary book as well as ledger. Depending upon the nature of business and the type of cash transactions, various types of Cash books are used. They are:

- a) Single Column Cash Book
- b) Two Column Cash Book or Cash Book with cash and discount columns.
- c) Three Columnar Cash Book or Cash Book with cash, bank and discount columns.
- d) Petty Cash Book.

**Single or Simple Column Cash Book :** This is the simplest form of Cash Book and is used when payments and receipts are mostly in the form of cash and where usually no cash discount is allowed or received. But, when transactions involving discounts are effected, it is recorded in a separate ledger account. Single Column Cash Book is just like a ledger account. When cash is received, it is recorded on the debit side, i.e., 'Receipts Side' of the Cash Book. Similarly when payment of cash is made, it is recorded on the credit side, i.e., "Payments Side" of the Cash Book

**Positing:** Once the Cash Book is entered with all the cash transactions, posting of the entries is made to the respective ledger accounts subsequently. For posting, from the debit side of the Cash Book, the concerned accounts are credited and from the credit side, the concerned accounts are debited.

### **Two Column Cash Book or Cash Book with Cash and Discount Columns:**

This type of Cash Book is used when cash transactions involving discount allowed or

received are effected. Usually, discount is allowed when payments are promptly made by the customers and discount is enjoyed when payments are promptly made by the business. In this two column Cash Book, instead of only one column for cash as in a Single Column Cash Book, one additional column is introduced, viz., 'Discount Column'. The discounts allowed by the business are entered on the debit side and discounts received are entered on the credit side of the Cash Book.

### **Three Columnar Cash Book or Cash Book with Cash, Bank and Discount Columns:**

Nowadays, every businessman invariably has a bank account to reap the advantages of safety, convenience, credit facilities and less clerical work. Thus, when a business is maintaining a bank account, the transactions can be made through cheques. Instead of maintaining the bank account in the ledger, it is found more convenient if it is included in the Cash Book as Cash Column. Thus, the three column Cash Book is the resultant effect where in addition to cash and discount columns, bank column is also included. The ruling of a three columnar cash book is as follows:

All cash receipts are entered on the debit side in the cash column and all cash payments on the credit side in the cash column of the Cash Book. Amounts paid into the bank or deposited are recorded on the debit side in the bank column and all payments made by cheques are recorded on the credit side in the bank column.

e) **Petty Cash Book:** The word 'petty' has its origin from the French word 'petit' which means small. The petty cash book is used to record items like carriage, cartage, entertainment expenses, office expenses, postage and telegrams, stationery, etc. The person who maintains this book is called the 'petty cashier'. The petty cash book is used by many business concerns to save the much valuable time of the senior official, who usually writes up the main cash book, to prevent over burdening of the main cash book with so many petty items and to find out readily and easily information about the more important transactions.

The amount required to meet out various petty items is estimated and given to the petty cashier at the beginning of the stipulated period say a fortnight or a month. When the petty cashier finds shortage of money, he has to submit the petty cash book, after making all the entries, to the chief cashier for necessary verifications. The chief cashier in turn, verifies all the entries with supporting vouchers and disburses cash or issues cheque for the exact amount spent.

### **Columnar Petty Cash Book or analytical Petty Cash Book**

In this cash book various items of petty cash payments are analysed and separate analytical columns are provided for recording each and every item. The amount of cash received from the chief cashier for meeting out the petty expenses is recorded on the debit side and the actual cash payments towards various petty items are recorded on the credit side in the total as well as analytical columns.

The analytical column is provided for each usual head of expense like postage & telegrams, printing & stationery, carriage & cartage, traveling expenses, entertainment expenses, office expenses, sundry expenses, etc. Subsequently, the totals of these analytical columns are posted

to the respective ledger accounts which save labour used in posting each item of payment

separately in the ledger. The balancing of petty cash book is done in the total payments column. Where the debit side (Receipts) exceeds that of the credit side (in the totals column-Payments), it represents the unspent balance of cash remaining with the petty cashier.

### **Cash Receipts and Vouchers:**

These are the vouchers and receipts for cash received and paid. Entries in cash book are made on the strength of the vouchers and receipts. They are also useful for auditing purpose.

### **Contra Entries**

For any single transaction the same account cannot be debited and credited. But since cash and bank accounts are maintained in the cash book, the debit and credit may be found in the two different accounts in the Cash Book. They are transactions which affect both the sides of the Cash Book. For instance, when cash is deposited into the bank, bank account should be debited and cash account should be credited. Hence, on

the debit side of the Cash Book, 'To Cash' is written in the particulars column and the amount is entered in the bank column. Similarly, on the credit side of the Cash Book, 'By Bank' is written in the particulars column and the amount is entered in the cash column.

When cash is withdrawn from the bank, on the debit side of the Cash Book, 'To Bank' is written in the particulars column and the amount is written in the cash column. Likewise, on the credit side of the Cash Book, 'By Cash' is written in the particulars column and amount is entered in the bank column. Therefore, **those entries which appear on both the sides of the Cash Book are called Contra Entries and they are identified and denoted in the Cash Book itself by writing the letter 'C' in the Ledger Folio Columns on either side.** For these transactions, as double entry procedure is completed in the cash book itself, no further posting is made in the ledger. In a three columnar Cash Book, cash and bank columns are balanced as any other ledger account and discount columns are simply totaled. To know the balance of the discount columns, a separate account, viz., discount account is opened in the ledger. While the cash column will always show a debit balance, the bank column may show a credit balance at times. The credit balance in the bank column represents nothing but bank overdraft.

## **ADVANTAGE OF SUBSIDIARY BOOKS**

The advantages of maintaining special journals can be summarized as under:

### **Division of work**

The division of journal resulting in division of work ensures more clerks working independently in recording original entries in day books.

### **Facilitate posting**

Because the transactions of one nature are recorded at one place, the posting of real account is highly facilitated.

### **Time Saving**

Due to division of work, it is possible to perform various accounting processes simultaneously. Thus, lesser time is required to complete accounting records.

### **Minimum frauds and errors**

Systematic recording of business transactions in special journals reduces the possibility of frauds and errors. It also helps in location of errors, if any.

### **Better information**

A lot of useful data like credit sales, credit purchases, returns etc., is made available which is not possible in journal system.

### **DISCOUNTS**

#### **Trade discount**

When a customer buys goods regularly or buys large quantity or buys for a large amount, the seller is usually inclined to allow a concession in price. He will calculate the total price according to the list of catalogue. But after the total is arrived at, he will make a deduction 5% or 10% depending upon his business policy. This deduction is known as Trade discount.

#### **Cash Discount**

An amount which is allowed for the prompt settlement of debt arising out of a sale within a specified time and calculated on a percentage basis is known as cash discount, i.e., it is always associated with actual payment.

#### **Difference Between Trade Discount and Cash Discount**

<b>Trade Discount</b>	<b>Cash Discount</b>
It is given by the manufacturer or wholesaler to a retailer and not to others	It may be allowed by seller to any debtor
It is allowed on a certain quantity being purchased	It is allowed on payment being made before a certain date
It is a reduction in the catalogue price of an article	It is a reduction in the amount due by a debtor
It is not usually accounted for in the books since the net amount is shown.	This discount must have to be accounted for in the books since it is deducted from the gross selling price.

### **Illustration 3**

**Enter the following transactions in the proper subsidiary books of Ram:  
2013 January**

1. Sold goods to Ramesh 5,250
2. Bought of Hari Ram Rs.7,800
2. Ramesh returned goods Rs.750
2. Purchased goods from Mangal Rs.7,000
4. Returned goods to Mangal Rs.1,000
4. Bought of Devi Dayal 3,250
4. Sold to Zakir Hussian 3,500
5. Zakir Hussian returned goods 450
6. Sold to Ram Prasad 5,000
  
6. Sold to Ghanshyam 3,000
7. Ram Prasad returned goods 500
7. Bought of Devi Dayal 7,000
8. Returned goods to Devi Dayal 750

9. Purchased goods from Raghunath subject to a trade discount of 10% 10,000  
 10. Sold to Raja Ram goods subject to a trade discount of 5% 5,000

**PURCHASE BOOK**

Date	Particulars	Invoice No.	LF	Details	Amount
1-1-13	Hari Ram				7,800
2-1-13	Mangal				7,000
4-1-13	Devi Dayal				3,250
7-1-13	Devi Dayal				7,000
9-1-13	Raghu Nath			10,000	
	Less Trade Discount 10%			<u>1,000</u>	<u>9,000</u>
	Purchase Account Dr.				<u>34,050</u>

**SALES BOOK**

Date	Particulars	Invoice No.	LF	Details	Amount
1-1-13	Ramesh				5,250
2-1-13	Dina Nath				5,500
4-1-13	Zakir Hussian				3,500
6-1-13	Ram Saran				5,000
6-1-13	Ghanshyam				3,000
10-1-13	Raja Ram			5,000	
	Less Trade Discount			<u>250</u>	
	Sales A/C Cr.				<u>4,750</u>
					<u>27,000</u>

**PURCHASE RETURNS BOOK**

Date	Particulars	Debit Note	LF	Details	Amount
4-1-13	Mangal				1000
8-1-13	Devi Dayal				<u>750</u>
	Purchase Returns A/C				<u>1,750</u>

**SALES RETURNS BOOK**

Date	Particulars	Credit Note	LF	Details	Amount
2-1-13	Ramesh				750
5-1-13	Zakir Hussian				450

7-1-13	Ram Saran Sales Returns A/c Dr.				<u>500</u> 1,700
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#### **Illustration 4**

From the following particulars prepare the Bills Receivable Book and Bills Payable Book:

2013 March

- 1 Acceptance received from Roy payable three months after date for Rs.6,500
- 5 Accepted Subhash's draft for Rs.4,000 for two months
- 12 Drew a bill on Yusuf for Rs.2,500 for 3 months
- 20 Give Rajesh our acceptance for Rs.5,000 payable 4 months after date
- 22 Roy's acceptance for Rs.6,500 was retired under a rebate of Rs.100
- 25 Received a bill from Naresh for Rs.1,000 for 1 month.
- 28 Accepted bill of Patel for Rs.4,500 for 2 months
- 30 Accepted Subash's Draft for Rs.2,000 for 1 month
- 30 Drew a bill on Yusuf for Rs. 2,000 for 2 months and accepted by him payable at Bank of India, Chandigarh

#### **BILLS RECEIVABLE BOOK**

Serial No.	Date of Receipt	From whom Received	Name of Acceptor	Where Payable	Date Of Bill	Term	When Due	Amount	Remarks
1.	1.3.13	Roy	Self		1.3.13	3 months	4.6.13	6,500	Retired
2.	12.3.13	Yusuf	Self		12.3.13	3 months	15.6.13	2,500	
3.	25.3.13	Naresh	Self		25.6.13	1 month	28.4.13	1,000	
4.	30.3.13	Yusuf	Self	B of Ind	30.3.13	2 months	2.6.13	<u>2,000</u> <u>12,000</u>	

**BILLS PAYABLE BOOK**

Serial No.	Date of Bill	Name of Drawer	Name of Payee	Term	When Due	LF	Amount	How met	Remarks
1.	5.3.13	Subash	Subash	2months	8.5.13		4,000		
2.	20.3.13	Rajesh	Rajesh	4 months	23.7.13		5,000		
3.	28.3.13	Patel	Patel	2 months	31.5.13		4,500		
4.	30.3.13	Subash	Subash	1 month	3.5.13		<u>2,000</u> <u>15,500</u>		

## Simple Cash Book

### Example 1

Enter the following transactions in Simple Cash Book:

2013 June 1. Balance of cash in hand Rs.15,000

8. Purchased goods for cash from Xavier Rs.3,200

15. Sold goods for cash Rs.4,800 to Y.

20. Received commission Rs.650 and paid commission Rs.550

28. Paid to Satish on account Rs.7,150

31. Paid salary to the office clerk Rs.1,000 and office rent Rs.600

### Solution

#### SIMPLE CASH BOOK

Date	Particulars	R.N	LF	Amount	Date	Particulars	Vr.N	LF	Amount
1.6.13	To Balance			15,000	8.1.13	By Purchase			3,200
15.6.13	b/d			4,800	20.1.13	By			550
20.6.13	To Sales			650	28.1.13	Commission			7,150
	To				31.1.13	By Satish			1,000
	Commission				31.1.13	By Salary			600
					31.1.13	By Rent			<u>7,950</u>
				<u>20,450</u>		By Balance			<u>20,450</u>
1.7.13				7,950		c/d			
	To Balance								
	b/d								

### Example 2:

Enter the following transactions in a Two Column Cash Book

2013 June:

1 Balance of cash in hand Rs.6,000

1 Received cash from Sohan Rs.1,000

3 Paid into Bank Rs.1,800

9 Paid to Mehta & Sons for goods purchased Rs. 2,000

- 10 Received Rs.1,800 from cash sales
- 11 Paid for cash purchases, Rs. 1,920 and received Rs.80 as discount
- 13 Withdrew for personal use Rs.1,000
- 19 Received Rs.1,160 from Kapoor and allowed Rs.40 as discount
- 20 Drew from bank for office use Rs.800
- 25 Paid cash for electricity charges Rs.120
- 26 Paid rent for March Rs.320
- 29 Cash Sales Rs.1,400
- 30 Deposited in Bank Rs.1,000
- 30 Paid cash for advertisement Rs.80
- 30 Paid salaries in cash Rs.140

### Solution

### CASH BOOK

Date	Particulars	LF	Dis - count	Cash	Date	Particulars	LF	Dis— count	Cash
<b>2013</b>					<b>2013</b>				
June 1	To			6,000	June 3	By Bank			1,800
June 1	Balance b/d			1,000	June 9	By Mehta & Sons			2,000
June 10	To Sohan			1,800	June 11	By Purchases	80		1,920
June 19	To Sales		40	1,160	June 13	By Drawings			1,000
June 20	To Kapoor			800	June 25	By Electricity			120
June 29	To Bank			1,400	June 26	charges			320
	To Sales				June 30	By Rent			1,000
					June 30	By Bank			80
					June 30	By Advertisement			140
					June 30	By Salaries			<u>3,780</u>
					June 30	By Balance c/d	80		<u>12,160</u>
July 1	To		<u>40</u>	<u>12,160</u>					
	Balance			3,780					
	b/d								

Prepare a Three Columnar Cash Book from the following transactions:

2013 January 1 Cash in hand Rs.15,000 and at bank Rs.4,000

4 Bought furniture for Rs.2,000 and issued a cheque

6 Deposited Rs.6,000 into Bank

8 Bought goods for cash Rs.2,500

- 10 Paid Vikram 850 in full settlement of Rs.900  
 14 Received Rs.1,250 from Tarun and allowed him a discount of Rs.40  
 18 Sent a Demand Draft to Satish for 1,750  
 20 Paid LIC premium Rs.355  
 25 Withdrew Rs.800 by cheque for personal use

### CASH BOOK

Date	Receipts	R No.	Discount	Cash	Bank	Date	Payments	V No.	Discount	Cash	Bank
						2013					
						Rs.					
Jan 1	To Balance b/d			15,000	4,000	Jan 4	By Furniture				2,000
Jan 6	To Cash (C)		40	1,250	6,000	Jan 6	By Bank (C)			2,500	
Jan 14	To Tarun					Jan 8	By Purchases		50	850	
						Jan 10	By Vikram			355	
						Jan 18	By Satish				800
						Jan 18	By Drawings			6,545	5,450
			40	<u>16,250</u>	<u>10,000</u>	Jan 20	By Drawing		50	<u>16,250</u>	<u>10,000</u>
Feb 1	To Balance b/d			6,545	5,450	Jan 25	By Balance c/d				
						Jan 31					

### Petty Cash Book

It is maintained by the Petty Cashier to record all the small payments like carriage, cartage, postage etc. It is a subsidiary book and is part of the cash book.

### Types of Petty Cash Book

- 1. Simple petty cash book:** It is a petty cash book which contains only one amount column for all classes of petty expenses.

Enter the following transactions in the simple petty cash book.

2013. January:

1. Received a cheque for Rs.1,000 to open the book
5. Bought postage stamp Rs.50
- 8 Paid for stationary Rs.80
- 10 Sent a Telegram Rs.70
- 12 Paid for cartage Rs.50
- 14 Paid tiffin charges for customers Rs.130
- 20 Balance due to Binder paid Rs.60
- 25 Paid auto charges of the salesman Rs.70
- 28 Paid coolie Rs.90
- 29 Purchased paper clips Rs.40
- 31 Paid electric charges Rs.80

#### SIMPLE PETTY CASH BOOK

Amount Received	Cash Folio	Date	Particulars	Voucher Number	Amount
		<b>2013</b>			
<b>1,000</b>		Jan. 1	To Bank A/c		--
		Jan. 5	By Postage		50
		Jan. 8	By Stationary		80
		Jan. 10	By Telegram		70
		Jan. 12	By Cartage		50
		Jan. 14	By Tiffin charges		130
		Jan. 20	By Binder's A/c		60
		Jan. 25	By Auto charges		70
		Jan. 28	By Coolie		90
		Jan. 29	By Paper clips		40
		Jan. 31	By Electric charges		80
		Jan. 31	By Balance c/d		<u>280</u>
<b><u>1,000</u></b>					<u>1,000</u>
<b>280</b>		February	To Balance b/d		

		1			
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## 2. Analytical Petty Cash Book

It is a method of recording petty cash payments in a columnar form. In such a petty cash book a separate column for each usual head of expenditure and for the total small cash payments is provided. It is known as Analytical petty cash book because the various small cash payments get automatically analysed when they are entered in their respective columns.

### Example:

#### 2013: July

- 1 Received from cashier Rs.800
- 2 Paid for postage Rs.8
- 5 Purchased stationary Rs.20
- 7 Sent telegram Rs.18
- 9 Paid for carriage Rs.24
- 12 Paid to Kulkarni Rs.100
- 14 Auto charges paid Rs.40
- 18 Paid for office cleaning Rs.24
- 22 Bought Postal stamps Rs.30
- 28 Paid for Journal and Magazines Rs.120
- 30 Floor cleaning charges Rs.24

### ANALYTICAL PETTY CASH BOOK

Amt received	Date	Particulars	V N	Total Payment	Printing & Station	Postage & Tele	Carriage	Traveling exp	Office Exp	Ledger
Rs.	2013			Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
	July 1	To Cash								
800	July 3	By Postage	1	08		08				
	July 5	By	2	20	20					
	July 7	Stationery	3	18		18				
	July 9	By	4	24			24			
	July 12	Telegram	5	10						100
	July 14	By Carriage	6	40				40		
	July 18	By Kulkarni	7	24					24	

	July22	By Auto	8	30		30				
	July28	char	9	120					120	
	July30	By Off	1	24					24	
		clean	0							
		By Postage		408	20	56	24	40	168	100
		By Journals		<u>392</u>						
		By Cleaning		<u>800</u>						
	Aug 1									
<u>800</u>		By Balanc								
392		c/d								
		To								
		Balancb/d								

### 3. Imprest System of Cash Book

Under this system , a round sum necessary for the possible needs of the business to meet petty cash expenses for the week or month is drawn by a cheque and handed over to the petty cashier. The actual amount spent by the petty cashier during the period will be given by a cheque , so that he may start the next period with the same amount as in the beginning of the last period. This system of maintaining the original amount of cash as such is known as Imprest system of maintaining petty cash book

Example:

Prepare Columnar Petty Cash Book on Imprest system from the following particulars

2013 June 1 Received for petty cash payments 1,000  
 ,, 2 Paid for postage 80  
 ,, 5 Paid for stationery 50  
 ,, 8 Paid for Advertisement 100  
 ,, 12 Paid for wages 40  
 ,, 16 Paid for carriage 30  
 ,, 20 Paid for conveyance 44  
 ,, 25 Paid for travelling expenses 160  
 ,, 27 Paid for Postage 100  
 ,, 28 Wages to office cleaner 20  
 ,, 30 Paid for telegrams 40  
 ; 30 Sent registered notice to landlord 6.

#### PETTY CASH BOOK

Cash Recei	Date	Particulars	L F	Total Payme	Postage & Tele	Carta- ge	Printin & advt	Trave- lling	Wages	Statio- nery	Sundr- ies
Rs.	2013			Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
1,000	June 1	To Cash									
	June 2	By Postage		80	80						

	June 5	By	50					50	
	June 8	Stationery	100			100			
	June 12	By Advt	40				40		
	June16	By Wages	30		30				
	June20	By Carriage	44						44
	June25	By	160				160		
	June27	Conveyance	100	100					
	June28	By Travll.	20				20		
	June30	Exp	40	40					
	June30	By Postage	6	6					
		By Wages	670	226	30	100	160	60	50
		By	<u>330</u>						44
<u>1,000</u>		Telegrams	<u>1000</u>						
		By							
330	July 1	Reg.notice							
670	July 1								
		By Balance							
		c/d							
		To Balance							
		b/d							
		To Cash A/c							

## **BANK RECONCILIATION STATEMENT**

### **Meaning**

Bank Reconciliation Statement is a statement prepared on a particular date to reconcile the balance as per Cash Book with the balance as per Pass Book and to know the exact balance with the bank.

BRS may be defined as “a statement prepared at periodical intervals, with a view to indicate the items which causes disagreement between the balance as per the bank column of the cash book and bank pass book on any given date.”

### **Causes for difference between balance as per cash book and pass book**

1. **Cheques issued but not yet presented for payment.** As soon as a **cheque** is issued, it is entered on the credit side of the Cash Book, but the Bank will make the entry only when the **cheque** is presented for payment. Thus there will be a gap of some days between the entry in the cash book and the pass book.
2. **Cheques paid into bank but not yet collected by the Bank.** As soon as **Cheques** are received they are entered on the debit side of the cash book, but the bank gives the credit only when it has been cleared. Thus there will be some gap between the date of depositing the cheque and the date of collection of the amount.
3. **Interest allowed by the Bank.** If the bank has allowed interest to the customer, the entry will be normally made in the Customer's account and later shown in the pass book. The customer usually gets to know the amount of interest from the pass book and only then he makes relevant entry in the Cash Book.
4. **Interest and Expenses charged by the Bank.** The entry for the Bank Charges will be normally made in the customer's account by the Bank. The customer makes the required entry only after he sees the Pass Book. Thus there will be some gap between the date of recording the Bank Charges in the Cash book & Pass book.
5. **Interest & Dividend collected by the Bank on behalf of the Customer.** When the bank collects interest and dividend for the customer it makes the entry in the customer's account. The customer makes the required entry only after he sees the pass book.
6. **Direct Payments by the Bank.** As per the standing instructions given to the Bank when the bank makes payment on behalf of the customer the entry will be made in the customer's account by the bank and the customer will make the entry in the cash book later when he sees the pass book. Thus the entries will be on different dates in both the cash book & pass book.

7. **Dishonour of a bill ( or cheque) discounted with the bank.** Cheques sent to the bank for collection or bills discounted with the bank but returned as dishonoured will have the same effect as cheques paid into the bank but not yet collected by it. Balance as per pass book will decrease as
8. compared to balance as per cash book because the fact of dishonor of cheque or bill has not yet been recorded in the cash book.
9. **Bills collected by the bank on behalf of the customer**
10. **Payment by customers direct into businessman's account with the banker**
11. **Wrong Debit or Credit given in the Pass Book or the Cash Book.**
12. **Errors in the Cash Book or the Pass Book.**

#### **Advantages of Reconciliation**

- i) It brings to notice the causes of difference between bank balance as per cash book and balance as per pass book.
- ii) Any undue delay in the clearance of cheques will be shown up.
- iii) A regular preparation of **BRS** would reduce the chance of fraud by the staff of the firm dealing in cash.
- iv) **BRS** is required to be prepared to ascertain the correct bank balance that can be shown in the Balance Sheet.

#### **Bank Reconciliation Statement as on ...**

<b>Particulars</b>	<b>Rs.</b>	<b>Rs.</b>
Balance as per Cash Book		xxx
Add:		
1. Cheques issued but not yet presented for payment	xxx	
2. Interest allowed by the bank	xxx	
3. Direct payment by a customer into bank	xxx	
4. Interest on investment credited by the bank	xxx	
5. Dividend on shares collected by the bank	xxx	
6. Rebate on bills retired under rebate through the bank but		

full amount entered in the cash book	xxx	
7. Any wrong entry on credit side of the pass book	<u>xxx</u>	<u>xxx</u>
Less:		xxx
1. Cheques deposited or paid into bank but not yet collected or credited	- xxx	
2. Bank Charges	xxx	
3. Insurance premium paid by the bank	xxx	
4. Interest on overdraft charged by the bank	xxx	
5. Dishonoured cheques or bills	xxx	
6. Drawings made by partners not entered in cash book	<u>xxx</u>	<u>xxx</u>
7. A wrong entry on debit side of the pass book		<u>xxx</u>
Balance as per pass book		

The following table will help to prepare the Bank Reconciliation statement

Items	Debit balance as per cash book	Credit balance as per pass book
I. Those items which affect the debit side of Cash Book:	---	+
i) Cheques deposited but not collected by the bank	---	+
ii) Cheques though entered in the cash book but omitted to be sent to the bank	+	---
II. Those items which affect the creditside of cash book:	+	---
Cheques issued but not presented for payment	+	---
III. Those items which affect the credit side of Pass Book:	+	---
i) Interest or Dividend credited by the bank		
ii) Amount deposited direct by a customer in to bank	---	+

A/c	---	+
iii) Cheques sent to the bank but omitted to be entered in the Cash book	---	+
IV. Those items which affect the debit side of Pass Book:		
i) Bank charges charged by the bank		
ii) Interest on overdraft		
iii) Payments made by the bank on standing instructions of the customer.		

**Example:**

From the following transactions prepare Bank Reconciliation Statement as on 31.08.2012

- a) Bank balance as per cash book Rs.8,000
- b) Cheques of Rs.1000, 2000 and 3000 issued on 8<sup>th</sup>, 10<sup>th</sup> and 13<sup>th</sup> of August. Of these a cheque issued on 10<sup>th</sup> only presented for payment till 31<sup>st</sup> August.
- c) Interest and dividend collected by the banker on 25<sup>th</sup> August and informed the customer on 1<sup>st</sup> September Rs.500.
- d) Cheques of Rs.3300 deposited into bank of which a cheque of Rs.2300 only collected in August.
- e) A cheque of Rs.2000 received and debited in cash book but not sent to bank till 31<sup>st</sup> August
- f) The following entries found in pass book only
  - a. Interest on bank balance Rs.250
  - b. Electricity bill paid Rs.400
  - c. Commission charged Rs.50

**Bank Reconciliation Statement as on 31.08.2012**

Particulars	Amount	Amount
Bank Balance as per Cash Book		<b>8,000</b>
Add: cheque issued but not presented for payment (1,000+3,000)	4,000	
Interest & Dividend collected and credited only in pass book	500	
Interest on bank balance credited only in pass book	<u>250</u>	<u>4,750</u>
		12,750

	1,000	
	2,000	
Less:		
Cheques deposited but not collected	400	
Cheques received but not sent to bank	<u>50</u>	<u>3,450</u>
Electricity bill paid and recorded only in pass book		<b><u>9,300</u></b>
Commission charged only in pass book		
Balance as per Pass Book		

## **TRIAL BALANCE**

### **INTRODUCTION**

According to the dual aspect concept, the total of debit balance must be equal to the credit balance. It is a must that the correctness of posting to the ledger accounts and their balances be verified. This is done by preparing a trail balance.

### **MEANING AND DEFINITION**

#### **Meaning**

Trial balance is a statement prepared with the balances or total of debits and credits of all the accounts in the ledger to test the arithmetical accuracy of the ledger accounts. As the name indicates it is prepared to check the ledger balances. If the total of the debit and credit amount columns of the trail balance are equal, it is assumed that the posting to the ledger in terms of debit and credit amounts is accurate. The agreement of a trail balance ensure arithmetical accuracy only, A concern can prepare trail balance at any time, but its preparation as on the closing date of an accounting year is compulsory.

#### **Definition**

According to M.S. Gosav “Trail balance is a statement containing the balances of all ledger accounts, as at any given date, arranged in the form of debit and credit columns placed side by side and prepared with the object of checking the arithmetical accuracy of ledger postings”.

### **OBJECTIVES OF PREPARING A TRAIL BALANCE**

- (i) It gives the balances of all the accounts of the ledger. The balance of any account can be found from a glance from the trail balance without going through the pages of the ledger.
- (ii) It is a check on the accuracy of posting. If the trail balance agrees, it proves:
  - (a) That both the aspects of each transaction are recorded and
  - (b) That the books are arithmetically accurate.
- (iii) It facilitates the preparation of profit and loss account and the balance sheet.

### **FEATURES OF TRAIL BALANCES**

The following are the important features of a trail balances:

- (i) A trail balance is prepared as on a specified date.
- (ii) It contains a list of all ledger account including cash account.
- (iii) It may be prepared with the balances or totals of Ledger accounts.
- (iv) Total of the debit and credit amount columns of the trail balance must tally.
- (v) If the debit and credit amounts are equal, we assume that ledger accounts are arithmetically accurate.

### **LIMITATIONS OF TRAIL BALANCE**

The following are the important limitations of trail balances:

- (i) The trail balance can be prepared only in those concerns where double entry system of book-keeping is adopted. This system is too costly.
- (ii) A trail balance is not a conclusive proof of the arithmetical accuracy of the books of account. On the other hand, some errors are not disclosed by the trail balance.
- (iii) If the trail balance is wrong, the subsequent preparation of Trading, P&L Account and Balance Sheet will not reflect the true picture of the concern.

### **METHODS OF PREPARING TRAIL BALANCE**

A trail balance refers to a list of the ledger balances as on a particular date. It can be prepared in the following manner:

#### **Total Method**

According to this method, debit total and credit total of each account of ledger are recorded in the trail balance.

#### **Balance Method**

According to this method, only balance of each account of ledger is recorded in trail balance. Some accounts may have debit balance and the other may have credit balance. All these debit and credit balances are recorded in it. This method is widely used.

**Note:** Accounts of all assets, expenses, losses and drawings are debit balances. Accounts of incomes, gains, liabilities and capital are credit balances.

Trial balance discloses some of the errors and does not disclose some other errors. This is given below.

#### **A) Trial Balance discloses the following Errors**

- i) Wrong totaling of subsidiary books
- ii) Posting of an amount on the wrong side
- iii) Omission to post an amount into ledger
- iv) Double posting or omission of posting
- v) Posting wrong amount
- vi) Error in balancing

#### **B) Trial Balance does not disclose the following Errors**

- i) Error of principle
- ii) Error of omission
- iii) Errors of Commission
- iv) Recording wrong amount in the books of original entry
- v) Compensating errors

#### **Illustration 4:**

From the following information prepare a Trial Balance as on 31<sup>st</sup> March 2013

Capital 12,500 ; Sales 15,450 ; Furniture & Fittings 640; Motor Car 6,250; Buildings 7,500; Total Debtors 3,800; Total Creditors 2,500; Bad Debts 125; Stock on( 1.4.12) 3,460;

Purchases 5,475; Bank (Cr. Balance) 2,850; Purchase Returns 125; Commission (Cr) 375; Sales Returns 200; Advertisement 250; Interest Account (Dr) 118; Cash Balance 650; Insurance & Tax 1,250; Salaries 4,082

### **TRIAL BALANCE AS ON 31.3.2013**

<b>Name of the Account</b>	<b>Debit</b>	<b>Credit</b>
Capital Account		12,500
Sales		15,450
Furniture & Fittings	640	
Motor Car	6,250	
Buildings	7,500	
Total Debtors	3,800	
Total Creditors		2,500
Bad Debts	125	
Stock on 1.4.12	3,460	
Purchases	5,475	
Bank Overdraft (Cr)		2,850
Purchase Returns		125
Commission (Cr)		375
Sales Returns	200	
Advertisement	250	
Interest A/c	118	
Cash Balance	650	
Insurance & Tax	1,250	
Salaries	4,082	
	<u>33,800</u>	<u>33,800</u>

### **FINAL ACCOUNTS OF PROPRIETARY CONCERNS**

#### **Introduction**

Final accounts or Financial Statements refers to statements prepared at the end of the accounting period to ascertain the profitability and the financial position of the business enterprise.

#### **Objectives**

- a. To ascertain the profit and profitability position of the business enterprise.
- b. To ascertain the financial position of the business enterprise

#### **Components of Financial Statements**

##### **a. Income Statement**

- (i) Trading Account

##### **b. Balance sheet**

(ii) **Profit & Loss Account**

**TRADING ACCOUNT**

**INTRODUCTION**

Trading account is prepared for an accounting period to find the trading results or gross margin of the business i.e., the amount of gross profit the concern has made from buying and selling during the accounting period. The difference between the

sales and cost of sales is gross profit. For the purpose of computing cost of sales, value of opening stock of finished goods, purchases, direct expenses on purchasing and manufacturing are added up and closing stock of finished goods is reduced. The balance of this account shows gross profit or loss which is transferred to the profit and loss account.

**PREPARATION OF TRADING ACCOUNT**

Trading account is a ledger account. It has to be prepared in conformity with double entry principles of debit and credit.

**Items shown in trading account:**

**(A) Debit side**

- (i) **Opening stock:** The stock at the beginning of an accounting period is called opening stock. This is the closing stock as per the last balance sheet. It includes stock of raw materials, work in progress, (where manufacturing account is not separately prepared) and finished goods. Trading account starts with opening stock on the debit side.
- (ii) **Purchases:** The total value of goods purchased after deducting purchase returns is debited to trading a/c. Purchases comprise of cash purchases and credit purchases.
- (iii) **Direct expenses:** Direct expenses are incurred to make the goods saleable. They include wages, carriage and freight on purchases, import duty, customs duty, clearing and forwarding charges manufacturing expenses or factory Expenses (where manufacturing account is not separately prepared). All direct expenses are extracted from trial balance.

**Items shown in trading account :**

**(B) Credit side:**

- (i) **Sales:** It includes both credit and cash sales. Sales returns are reduced from sales and net sales are shown on the credit side of trading account. The sales and returns are extracted from the trial balance.
- (ii) **Closing stock:** Closing stock is the value of goods remaining at the end of the accounting period. It includes closing stock of raw materials, work-in- progress (where manufacturing account is not separately prepared) and finished stock. The opening stock is ascertained from trial balance but closing stock is not a part of ledger. It is separately valued and given as an adjustment. If it is given in trial balance, it is after adjustment of opening and closing stocks in purchases. If closing stock is given in trial balance it is shown only as current asset in balance sheet. If closing stock is given outside trial balance, it is shown on credit side of trading account and also as current asset in the balance sheet

**Trading Account for the year ended 31<sup>st</sup> March....**

Particulars	Amount	Particulars	Amount
To opening Stock	Xxx	By Sales	
To Purchases		xxx	
xxx		Less Sales Returns	xxx
Less Purchase Returns	xxx	Or ( Returns inwards)	xxx
or(Returns Outwards)	xxx	<u>xxx</u>	
<u>xxx</u>		By Closing Stock	
To Direct Expenses ( expenses relating to Purchases & production)			
Wages			
Carriage inwards			
Freight			
Octroi			
Import Dty	xxx		
Motive Power,coal,Gas &	<u>xxx</u>		
Fuel			
Consumable Stores			
To Gross Profit c/d			xxx

## PROFIT AND LOSS ACCOUNT

### INTRODUCTION

Profit and loss account is prepared to ascertain the net profit of the business concern for an accounting period

### DEFINITION

In the words of Prof. Carter “Profit and loss account is an account into which all gains and losses are collected in order to ascertain the excess of gains over the losses or vice versa.”

### PREPARATION OF PROFIT AND LOSS ACCOUNT

Profit and loss account starts with gross profit brought down from trading account on the credit side. (If gross loss, on the debit side). All the indirect expenses are debited and all the revenue incomes are credited to the profit and loss account and then net profit or loss is calculated. If incomes or credit is more, than the expenses or debit, the difference is net profit. On the other hand if the expenses or debit side is more, the difference is net loss.

#### Debit side:

Expenses shown on the debit side of profit and loss account are classified into two categories

1. Operating expenses and
2. Non operating expenses

**Operating expenses:** These expenses are incurred to operate the business efficiently. They are incurred in running the organisation. Operating expenses include administration, selling, distribution, finance, depreciation and maintenance expenses.

**Non operating expenses:** These expenses are not directly associate with day today operations of the business concern. They include loss on sale of assets, extraordinary losses, etc.

### Credit side

Gross profit is the first item appearing on the credit side of profit and loss account. Other revenue incomes also appear on the credit side of profit and loss account. The other incomes are classified as operating incomes and non operating incomes.

**Operating incomes:** These incomes are incidental to business and earned from usual business carried on by the concern. Examples: discount received, commission earned, interest received etc.

**Non operating incomes:** These incomes are not related to the business carried on by the firm. Examples are profit on sale of fixed assets, refund of tax etc.

## PRINCIPLES OF PREPARING PROFIT OF LOSS ACCOUNT

(i) Only revenue receipts should be entered

(ii) Only revenue expenses together with losses should be taken into account.

(iii) Expenses and incomes relating only to the period for which the accounts are being prepared should be considered.

(iv) All expenses and income relating to the period concerned should be considered even if the expense has not yet been paid in cash or the income has not yet been received in cash.

### Note:

All personal expenses of the proprietor must be debited to the capital or drawings accounts and must not be debited to the profit and loss account. Similarly any income has been earned from the private assets of the proprietor which is received by firm, it must be credited to the capital or drawings account.

### Profit & Loss Account for the year ended 31<sup>st</sup> March....

Particulars	Amount	Particulars	Amount
To Salaries		By Gross Profit b/d	
„ Advertisement		„ Interest Received	
„ Travelling Expenses		„ Discount Received	
„ Carriage Outwards		„ Commission Received	
„ Bank Charges		„ Rent Received	
„ Rent, Rates & Taxes		„ Income from Investments	
„ Printing & Stationery			
„ Postage & Telegram			
„ Telephone Charges			
„ Legal Charges			
“ Audit Fees			
„ Insurance			
„ General Expenses			
„ Depreciation			
„ Repairs & Maintenance			
„ Bad Debts			
„ Discount Allowed			
„ Commission Paid			
„ Interest on capital			
„ Rent			
„ Interest on Loans			

„ Discount on Bills Discounted			
„ Net Profit transferred to Capital a/c			

**Note: If the Debit side total is more than the Credit side total it will be Net Loss**

## **BALANCE SHEET**

### **INTRODUCTION**

A Balance Sheet is a statement prepared with a view to measure the financial position of a business on a certain fixed date. It comprises of lists of assets, liabilities and capital fund on a given date. It presents the financial position of a concern as revealed by the accounting records. It reflects the assets owned by the concern and the sources of funds used in the acquisition of those assets. Balance sheet may be called a ‘statement of equality’ in which equality is established by representing values of assets on one side and values of liabilities and owners' funds on the other side.

### **DEFINITIONS OF BALANCE SHEET:**

“Balance sheet is a ‘Classified summary’ of the ledger balances remaining after closing all revenue items into the profit and loss account.” - Cropper.

“Balance sheet is a screen picture of the financial position of a going business concern at a certain moment” - Francis.

### **CLASSIFICATION OF ASSETS AND LIABILITIES**

A clear and correct understanding of the basic divisions of the assets and liabilities and the meanings which they signify and the amounts which they represent is very essential for a proper perspective of financial position of a business concern. Assets and liabilities are classified under the following major headings.

#### **Assets:**

Assets are properties of business. They are classified on the basis of their nature. Different types of assets are as under:

- (i) **Fixed assets:** Fixed assets are the assets which are acquired and held permanently and used in the business with the objective of making profits.  
Land and building, Plant and machinery, Furniture and Fixtures are examples of fixed assets.
- (ii) **Current assets:** The assets of the business in the form of cash, debtors bank balances, bill receivable and stock are called current assets as they can be realised within an operating cycle of one year to discharge liabilities.
- (iii) **Tangible assets:** Tangible assets have definite physical shape or identity and existence; they can be seen, felt and have volume such as land, cash, stock etc. Thus tangible assets can be both fixed assets and current assets.
- (iv) **Intangible assets:** The assets which have no physical shape which cannot be seen or felt but have value are called intangible assets. Goodwill, patents, trademarks and

licences are examples of intangible assets. They are usually classified under fixed assets.

(v) **Fictitious assets:** Fictitious assets are not real assets. Past accumulated losses or expenses which are capitalized for the time being, expenses for promotion of organisations (preliminary expenses), discount on issue of shares, debit balance of profit and loss account etc. are the examples of fictitious assets.

(vi) **Wasting assets:** These assets are also called depleting assets. Assets such as mines, Timber forests, quarries etc. which become exhausted in value by way of excavation of the minerals, cutting of wood etc. are known as wasting assets. Such assets are usually natural resources with physical limitations.

(vii) **Contingent assets:** Contingent assets are assets, the existence, value possession of which

is based on happening or otherwise of specific events. For example, if a business firm has filed a suit for a particular property now in possession of other persons, the firm will get the property if the suit is decided in its favour. Till the suit is decided, it is a contingent asset.

## **Liabilities**

A liability is an amount which a business firm is 'liable to pay' legally. All the amounts

which are claims by outsiders on the assets of the business are known as liabilities. They are credit balances in the ledger. Liabilities are classified into four categories as given below.

(1) **Owner's capital:** Capital is the amount contributed by the owners of the business. In addition to initial capital introduced, proprietors may introduce additional capital and withdraw some amounts from business over a period of time. Owner's capital is also called 'net worth'. Net worth is the total fund of proprietors on a particular date. It consists of capital, profits and interest on capital subject to reduction of drawings and interest on drawings.

In case of limited companies, capital refers to capital subscribed by shareholders. Net worth refers to paid up equity capital plus reserves and profits, minus losses.

(ii) **Long term Liabilities:** Liabilities repayable after specific duration of long period of time are called long term liabilities. They do not become due for payment in the ordinary 'operating cycle' of business or within a short period of time. Examples are long term loans and debentures. Long term liabilities may be secured or unsecured, though usually they are secured.

(iii) **Current liabilities:** Liabilities which are repayable during the operating cycle of business, usually within a year, are called short term liabilities or current liabilities. They

are paid out of current assets or by the creation of other current liabilities. Examples of current liabilities are trade creditors, bills payable, outstanding expenses, bank overdraft, taxes payable and dividends payable.

(iv) **Contingent liabilities:** Contingent liabilities will result into liabilities only if certain events happen. Examples are:

Bills discounted and endorsed which may be dishonored, unpaid calls on partly called shares held as investments

**BALANCE SHEET AS ON 31<sup>st</sup> March....**

<b>Liabilities</b>	<b>Amount</b>	<b>Assets</b>	<b>Amount</b>
<b>Current Liabilities:</b>		<b>Current Assets:</b>	
Bank Overdraft	xxx	Cash in hand	xxx
Bills Payable	xxx	Cash at Bank	xxx
Outstanding Expenses	xxx	Bills Receivable	xxx
Sundry Creditors	xxx	Sundry Debtors	xxx
Income received in Advance	xxx	Pre paid Expenses	xxx
<b>Long Term Liabilities:</b>		Accrued Incomes	xxx
Loans	xxx	Closing Stock	xxx
<b>Capital</b>		<b>Investments:</b>	
Opening Balance		In shares of Company	xxx
xxx		In Bonds	xxx
Add : Additional Capital		<b>Fixed Assets</b>	
xxx		Furniture & Fixtures	xxx
Add: Net Profit		Plant & Machinery	xxx
xxx		Building	xxx
Add: Interest on Capital		Land	xxx
<u>xxx</u>	<u>xxx</u>	Goodwill	<u>xxx</u>
	xxx		<u>xxx</u>
<u>xxx</u>			
- Less: Drawings	xxx		
Interest on Drawing	xxx		
Net Loss (if any)	<u>xxx</u>		
<u>xxx</u>			

**Rules in the Preparation of Final Accounts**

1. All items in Trial Balance must appear once in Final Accounts ( Either in Trading A/c or P/L A/c or Balance Sheet)
2. All Adjustments must appear twice in Final Accounts
3. Items in the Debit Column of the Trial Balance must appear either on the Debit side of Trading A/c or P/L A/c or on the Asset Side of Balance Sheet
4. Items in the Credit Column of the Trial Balance must appear either on the credit side of Trading A/c or Profit & Loss A/c or on the liabilities Side of the Balance Sheet.
5. All Real Accounts (other than relating to Goods) and Personal Accounts must appear in the Balance Sheet
6. All Nominal Accounts must appear in Trading & Profit & Loss Account
7. Stock in Trial Balance is Opening Stock

8. Stock in Adjustment is Closing Stock
9. Assets refers to ‘ What the Business has’ and ‘ What the business has to receive’
10. Liabilities refers to ‘ What the business has to pay’
11. Outstanding Expenses given in the Adjustment is to be added with the concerned expense in the Trading A/c or Profit & Loss A/c and is to be shown on the Liability side of the Balance Sheet.
12. Prepaid Expense given in the Adjustment is to be subtracted from the concerned expense in the Profit & Loss A/c and is to be shown on the Asset side of the Balance Sheet.
13. While showing the Bad Debts , New Reserve for Bad Debts is to be added and the Existing Reserve is to be Subtracted.

**Example:**

From the following trial balance of Mr. Nagaraj prepare the final accounts for the year ended 31.3.13

	Debit	Credit
Land & Building	50,000	
Purchases	1,10,000	
Stock on 1.4.12	40,000	
Returns	1,500	2,500
Wages	10,000	
Salaries	9,000	
Office Expenses	2,400	
Carriage inwards	1,200	
Carriage Outwards	2,000	
Discount	750	1,200
Bad Debts	1,200	
Sales		2,05,000
Capital Account		1,30,000
Insurance	1,500	
Commission		1,500
Plant & Machinery	50,000	
Furniture & Fixtures	10,000	
Bills Receivable	20,000	
Sundry Debtors	40,000	
Sundry Creditors		25,000
Cash in Hand	1,500	
Cash at Bank	4,500	
Office Equipment	12,000	
Bills Payable		2,350
	<b>3,67,550</b>	<b>3,67,550</b>

The following adjustments are required:

1. Closing Stock amounted to Rs.60,000
2. Outstanding Liabilities: Wages Rs.2,000 ; Rent Rs.3,000
3. Depreciate Land & Buildings at 5% and Plant & Machinery at 10% , Office Equipment and Furniture and Fixtures at 10%
4. Raise a bad and doubtful debts reserve at 5% on sundry debtors
5. Insurance premium Prepaid Rs.200
6. Provide interest on Capital at 5%

**Solution**

**Trading & Profit & Loss Account for the year ended 31.03.2013**

Particulars	Amount	Particulars	Amount
To Opening Stock	40,000	By Sales	
To Purchases		2,05,000	2,03,500
1,10,000	1,07,500	Less Sales Returns	60,000
Less Purchase Returns		<u>1,500</u>	
<u>2,500</u>	12,000	By Closing Stock	
To Wages	1,200		
10,000	<u>1,02,800</u>		
Add Outstanding Wages	<b><u>2,63,500</u></b>		<b><u>2,63,500</u></b>
<u>2,000</u>			1,02,800
To Carriage inwards	9,000		1,200
To Gross Profit c/d	2,400	By Gross Profit b/d	1,500
	2,000	By Discount	
	750	By Commission	
To Salaries			
To Office Expenses	3,200		
To Carriage Outwards			
To Discount Allowed	1,300		
To Bad Debts	3,000		
1,200			
Add New RBDD(40,000x5%)	2,500		
<u>2,000</u>	5,000		
To Insurance	1,200		
1,500	1,000		
Less Prepaid	6,500		
<u>200</u>	<u>67,650</u>		
To Rent Outstanding	<b><u>1,05,500</u></b>		<b>1,05,500</b>
To Depreciation:			
Building (50,000 x5/100)			
Plant &			

Machinery(50,000x10/100) Office Equipment (12,000 x10/100) Furniture (10,000x10/100) To Interest on Capital (1,30,000x5%) To Net Profit transferred to Capital a/c			
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**Balance Sheet as at 31.03.2013**

Liabilities	Amount	Assets	Amount
<b>Current liabilities :</b>		<b>Current Assets :</b>	
Bills Payable	2,350	Cash in Hand	1,500
Sundry Creditors	25,000	Cash at Bank	4,500
Outstanding Wages	2,000	Bills Receivable	20,000
Outstanding Rent	3,000	Sundry Debtors	38,000
<b>Capital</b>		40,000	60,000
Opening Capital		Less New RBDD	200
1,30,000		<u>2,000</u>	
Add Interest on Capital	2,04,150	Closing Stock	
6,500		Prepaid Insurance	47,500
Add Net Profit		<b>Fixed Assets :</b>	
<u>67,650</u>		Land & Building	45,000
		50,000	9,000
		Less Depreciation	
		<u>2,500</u>	
		Plant & Machinery	10,800
		50,000	<u>2,36,500</u>
	<b><u>2,36,500</u></b>	Less Depreciation	
		<u>5,000</u>	
		Furniture & Fixtures	
		10,000	
		Less Depreciation	
		<u>1,000</u>	
		Office Equipment	
		12,000	
		Less Depreciation	
		<u>1,200</u>	

## **SINGLE ENTRY SYSTEM**

### **Meaning**

Single Entry System is a system of book keeping in which for some transactions both the aspects are recorded, for some only one aspect is recorded and for some transaction no record is made. It is not based on the Double entry system of Book keeping .

### **Features**

### **Types**

Types of Single Entry System

Pure single entry system is that system under which only Personal Accounts are maintained.

Simple Single Entry System is that system of under which along with Personal Accounts, a Cash Book is also maintained.

Quai Single Entry System is that system ,under which , in addition to Personal Accounts and Cash Book subsidiary books are also maintained.

### **Advantages**

It is economical

Very simple to maintain and easy to understand

Suitable for sole trading and small partnership firms

Disadvantages of Single Entry System

- 1.No arithmetical accuracy
- 2.Difficult to ascertain financial position
- 3.Profit & Loss account cannot be prepared.
- 4.Encourages Fraud
5. Rectification of errors is difficult.

### Difference between Single Entry & Double Entry

Basis of difference	Double Entry	Single Entry
Accounts	All personal, real and nominal accounts are opened	Only personal accounts and cash accounts are opened.
Both aspects	Both the aspects of a transaction are recorded	In some cases both and in other cases only one aspect is recorded.
Trial Balance	Can be prepared	Cannot be prepared
P/L A/C	Can be prepared	Cannot be prepared
Balance sheet	Can be prepared to know the financial position	Cannot be prepared to know the financial position
Method	Scientific Method	Unscientific Method
Reliability	Most Reliable	Not Reliable
Utility	Suitable for all types of business	Suitable only for Sole trading and Partnership firms.

### Disadvantages

#### Ascertainment of Profit under Single Entry System

1. Statement of Affairs Method or Net Worth Method
2. Conversion Method

**Statement of Affairs Method:** Under this method statement of affairs is prepared to find out the Capital. The closing capital is compared with the Opening capital and the difference is considered as the profit or loss. Adjustments are made for the additional capital introduced or the drawings made by the proprietors

**Profit or loss under single entry system can be ascertained under the following two methods**

#### Net Worth Method or Statement of Affairs Method or Capital Comparison Method

Under Single entry system , a regular Trading & Profit and Loss Account cannot be prepared, because no record is kept of the nominal accounts. Roughly profit or loss is ascertained by comparing the financial position of the business at the commencement of the period with that at the close of the period. This necessitates the preparation of two **Statements of Affairs. Statement of Affairs is a statement prepared by setting forth the assets and liabilities on any given date.** The excess of assets over liabilities as shown by each such statement will represent the then capital and a comparison of the capitals at the two dates will reveal either Profit or Loss

### Difference between Statement of Affairs & Balance Sheet

Statement of Affairs	Balance Sheet
It is prepared under Single Entry System of book keeping.	1.It is prepared under Double Entry system Of book keeping.
It is prepared to ascertain the Capital Balance as on a particular date.	2.It is prepared to know the financial position of a concern as on a particular date.
It is prepared from ledger balances and partly from other particulars and estimates etc.	3.It is prepared only from the balances of Ledger Accounts.
Capital is the excess of assets over liabilities.	4. Capital account is taken from the Ledger.
Omission of assets or liabilities cannot be traced.	5. Omission of any asset or liability can be easily be traced as the totals will not tally.

#### Example

Prepare Statement of Affairs from the following information under Single Entry:

	Opening	Closing
Stock	80,000	95,000
Debtors	1,50,000	1,30,000
Cash	5,000	8,000
Prepaid Expenses	3,000	1,000
Outstanding Expenses	4,000	6,000
Creditors	42,000	37,000
Machinery	10,000	15,000
Furniture	1,000	1,000

#### Statement of Affairs

Liabilities	Opening	Closing	Assets	Opening	Closing
Outstanding Expenses	4,000	6,000	Stock	80,000	95,000
Creditors	42,000	37,000	Debtors	1,50,000	1,30,000
Capital ( Balancing Figure)	2,03,000	2,07,000	Cash	5,000	8,000
			Prepaid Expenses	3,000	1,000
			Machinery	10,000	15,000

	<u>2,49,000S</u>	<u>2,50,000</u>	Furniture	<u>1,000</u>	<u>1,000</u>
				<u>2,49,000</u>	<u>2,50,000</u>

**Example:**

Mr. Ram lal keeps his books under single entry system.

Particulars	1.1.2012	31.12.2013
Bank Overdraft	10,000	12,000
Furniture	20,000	20,000
Land & Building	70,000	70,000
Investments	---	10,000
Sundry Debtors	20,000	30,000
Sundry Creditors	30,000	40,000
Stock	45,000	50,000
Motor Car (1.7.2012)	---	20,000
Cash	10,000	20,000
Plant & Machinery	40,000	40,000

During the year he withdraw Rs.10,000 for personal use. On 1.7.2012 he introduced further capital of Rs.20,000 by selling his private house.

Adjustments:

1. Appreciate Land & Building by 20%
2. Debtors include Rs.1,000 from a customer who is insolvent and is irrecoverable.
3. Maintain Provision for Doubtful Debts at 5% on Debtors
4. Depreciate Plant & Machinery at 10% , Furniture at 5% and Motor Car at 10%

Prepare a statement showing profit or loss for the year 202012 and a revised statement of affairs as on that date.

**NOTE: Here we are asked to prepare a statement showing Profit or Loss. For that Opening Capital & Closing Capital is to be found out first by preparing statement of affairs as on 1.1.12 & 31.12.12. Revised statement of Affairs is to be prepared after considering all the adjustments given in the Question**

**Solution:**

**STATEMENT OF AFFAIRS as on ...**

<b>Liabilities</b>	<b>1.1.12</b>	<b>31.12.12</b>	<b>Assets</b>	<b>1.1.12</b>	<b>31.12.12</b>
Sundry Creditors	30,000	40,000	Furniture	20,000	20,000
Bank Overdraft	10,000	12,000	Land & Building	70,000	70,000
Capital(Bal.Figure)	1,65,000	2,08,000	Investments	---	10,000
			Sundry Debtors	20,000	30,000
			Stock	45,000	50,000
			Motor Car	---	20,000
			Cash	10,000	20,000
			Plant & Machinery	<u>40,000</u>	<u>40,000</u>
	<u>2,05,000</u>	<u>2,60,000</u>		<u>2,05,000</u>	<u>2,60,000</u>

**STATEMENT OF PROFIT OR LOSS**

Capital at the end of the year		2,08,000
Add: Drawings during the year		<u>10,000</u>
		2,18,000
Less: Additional Capital		<u>20,000</u>
Adjusted Capital at the End		1,98,000
Less : Capital at the beginning of the year		<u>1,65,000</u>
Gross Profit		33,000
Add: Appreciation in Building		<u>14,000</u>
		47,000
Less: Bad Debts	1,000	
Less: Provision for Doubtful Debts (5% on 29,000)	1,450	
Depreciation:		
On Plant & Machinery(40,000 x10%)	4,000	
On Furniture (20,000x5%)	1,000	
On Motor Car (20,000x 10%x6/12	<u>1,000</u>	
		<u>8,450</u>
		<u>38,550</u>

**STATEMENT OF AFFAIRS (REVISED) as on 31.12.2012**

<b>Liabilities</b>	<b>Amount</b>	<b>Assets</b>	<b>Amount</b>
Sundry Creditors	40,000	Cash	20,000
Bank Overdraft	12,000	Stock	50,000
Capital		Sundry Debtors 30,000	
1,65,000		Less Bad Debts <u>1,000</u>	
Add Net Profit		29,000	
38,550		Less Provision for	
Add Additional Capital <u>20,000</u>		Doubtful Debts <u>1,450</u>	27,550
2,23,550	2,13,550	Investments	10,000
Less Drawings		Furniture(20,000 -- 1,000)	19,000
<u>10,000</u>		Land & Building (70,000 + 14,000)	84,000
		Motor Car (20,000—1,000)	19,000
		Plant & Machinery(40,000—4,000)	<u>36,000</u>
	<b>2,65,550</b>		<b>2,65,550</b>

