



# ACCOUNTING PROCESS



## UNIT -1 BASIC ACCOUNTING PROCEDURES – JOURNAL ENTRIES

### LEARNING OUTCOMES

**After studying this unit, you will be able to:**

- ◆ Understand meaning and significance of Double Entry System.
- ◆ Familiarize with the term 'account' and understand the classification of accounts into personal, real and nominal.
- ◆ Note the utility of such classification and sub-classifications.
- ◆ Understand how debits and credits are determined from transactions and events.
- ◆ Observe the points to be taken care of while recording a transaction in the journal.

## UNIT OVERVIEW

### Source Documents

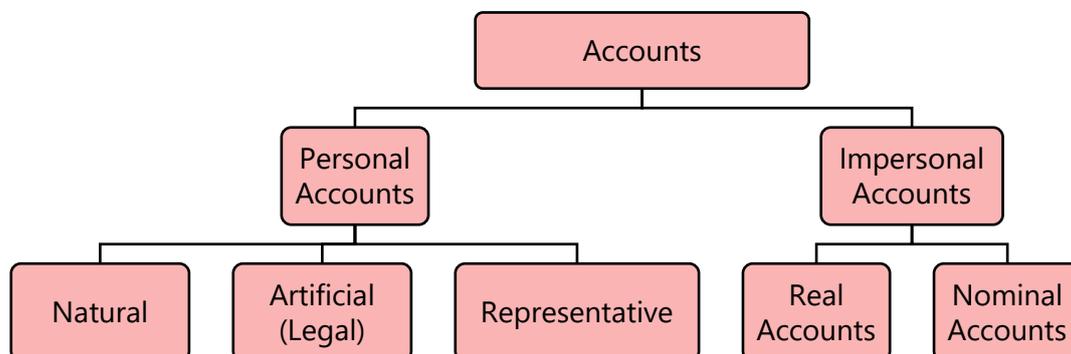
- All documents in records which contain financial records and act as evidence of transactions.

### Books of original entry and Ledger Accounts

- Purchase day book, Cash book, Sales day book and Purchases return book
- Accounts where information relating to a particular asset/liability, capital, income and expenses are recorded.

### Trial Balance

- It contains the totals from various ledger accounts and act as preliminary check on accounts before producing financial statements.



## 1.1 DOUBLE ENTRY SYSTEM

Double entry system of accounting is more than 500 years old. "Luca Pacioli" an Italian friar & mathematician published *Summa de Arithmetica, Geometria, Proportioni, et Proportionalita* ("Everything about Arithmetic Geometry and proportions"). The first book that described a double entry accounting system. Double entry system of book-keeping has emerged in the process of evolution of various accounting techniques. It is the only scientific system of accounting. According to it, every transaction has two-fold aspects—debit and credit and both the aspects are to be recorded in the books of accounts. Therefore, in every transaction at least two accounts are effected.

For example, on purchase of furniture either the cash balance will be reduced or a liability to the supplier will arise and new asset furniture is acquired. This has been made clear already, the Double Entry System records both the aspects. It may be defined as the system which recognises and records both the aspects of transactions. This system has proved to be

systematic and has been found of great use for recording the financial transactions for all kind of entities requiring use of money.



## 1.2 ADVANTAGES OF DOUBLE ENTRY SYSTEM

This system affords the under mentioned advantages:

- (i) By the use of this system the accuracy of the accounting work can be established, through the device of the trial balance.
- (ii) The profit earned or loss incurred during a period can be ascertained together with details.
- (iii) The financial position of the entity or the institution concerned can be ascertained at the end of each period, through preparation of the financial statements.
- (iv) The system permits accounts to be kept in as much details as necessary and, therefore provides significant information for the purpose of control and reporting.
- (v) Result of one year may be compared with those of previous years and reasons for the change may be ascertained.

In view of the above, the advantages of double entry system has been used extensively in all countries.



## 1.3 ACCOUNT

We have seen how the accounting equation becomes true in all cases. A person starts his business with say, ₹ 10,00,000 as capital with corresponding balance of cash ₹ 10,00,000. For example, transactions entered into by the entity will alter the cash balance in two ways, one will increase the cash balance and other will reduce it. Payment for goods purchased, salaries paid and rent expense paid, etc., will reduce the cash balance whereas sales of goods for cash and collection from customers will increase it.

We can change the cash balance with every transaction but this will be cumbersome. Instead it would be better if all the transactions that lead to an increase are recorded in one column and those that reduce the cash balance in another column; then the net result can be ascertained. If we add all increases to the opening balance of cash and then deduct the total of all decreases, we shall know the closing balance. In this manner, significant information will be available relating to cash.

The two columns which we referred above are put usually in the form of an account, called the 'T' form. This is illustrated below by taking imaginary figures:

## CASH

Particular		Increase (Receipt) ₹	Particular	Decrease (Payment) ₹
Opening Balance	(1)	10,00,000		(7) 1,00,000
	(2)	2,50,000		(8) 3,00,000
	(3)	2,00,000		(9) 2,00,000
	(4)	5,00,000		(10) 5,00,000
	(5)	1,35,000		
	(6)	4,00,000		(11) 12,00,000
			New or Closing Balance	1,85,000
		24,85,000		24,85,000

Since, each T-account shows only amounts and not transaction descriptions, we record each transaction in some way, such as by numbering used in this illustration. However, one can use date also for this purpose.

What we have done is to record the increase of cash on the left hand side and the decrease on the right hand side; the closing balance has been ascertained by deducting the total of payments, ₹ 23,00,000 from the total of the left - hand side. Such a treatment of receipts and payments of cash is very convenient.

Here we talked about only one account namely cash, now let us see how to make T-accounts when assets as well as liabilities are effected from a particular transaction.

Now, let us take some more examples:-

**Transaction 1:**

Initial investment by owners ₹ 25,00,000 in cash.

This will effect two accounts namely cash and capital. The asset cash increases and the stock holders' equity paid up capital also increases.

## CASH

	Increase		Decrease
(1)	25,00,000		

**CAPITAL**

	Decrease		Increase
		(1)	25,00,000

**Transaction 2:**

Paid cash to the creditors ₹ 14,00,000

This will effect cash account which will decrease and creditors account which is a liability will also decrease.

**CASH**

	Increase		Decrease
		(2)	14,00,000

**CREDITORS**

	Decrease		Increase
(2)	14,00,000		

The proper form of an account is as follows:

**Account**

Date	Particulars	Amount	Date	Particulars	Amount
		₹			

The columns are self-explanatory.

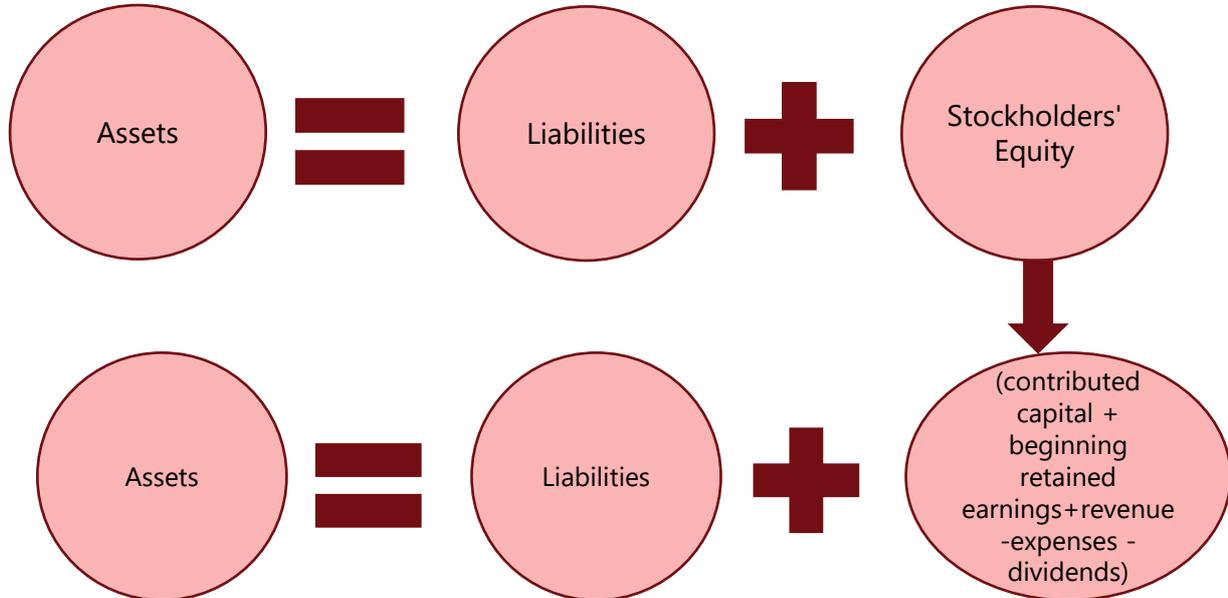
 **1.4 DEBIT AND CREDIT**

We have seen that in T-accounts increase and decrease entries are made on the left and right side of the accounts for assets respectively and vice-versa for liabilities. But, formally accountants use the term Debit (Dr.) to denote an entry on the left side of any account and Credit (Cr.) to denote an entry on the right side of any account.

We know that by deducting the total of liabilities from the total of assets the amount of capital is ascertained, as is indicated by the accounting equation.



To understand the equation better, let us expand it:-



Here,

- Contributed capital = the original capital introduced by the owner.  
 Beginning retained earnings = previous earnings not distributed to the shareholders.  
 Revenue = generated from the ongoing activities of the business  
 Expenses = cost incurred for the operations of the company.  
 Dividends = earnings distributed to the shareholders of the company

We have also seen that if there is any change on one side of the equation, it is bound to be similar change on the other side of the equation or amongst items covered by it or an opposite change on the same side of the equation. This is illustrated below:

Transactions	Total Assets ₹	= Liabilities ₹	+ Owner's Capital ₹
(1) Started business with cash ₹ 10,00,000	10,00,000		10,00,000
(2) Borrowed ₹ 5,00,000	+ 5,00,000	+ 5,00,000	
(3) Withdrew cash from business ₹ 2,00,000	- 2,00,000		- 2,00,000
(4) Loan repaid to the extent of ₹ 1,00,000	- 1,00,000	- 1,00,000	
(5) Bought furniture worth ₹ 3,00,000 with Cash	+3,00,000 <u>- 3,00,000</u>		
<b>Balance</b>	<b>12,00,000</b>	<b>= 4,00,000</b>	<b>+ 8,00,000</b>

As has been seen previously, what has been given above is suitable only if the number of transactions is small. But if the number is large, a different procedure of putting increases and decreases in different columns will be useful and this will also yield significant information. The transactions given above are being shown below according to this method.

Total Assets		= Liabilities		+ Owner's Capital	
Increase ₹	Decrease ₹	Decrease ₹	Increase ₹	Decrease ₹	Increase ₹
(1) 10,00,000					10,00,000
(2) 5,00,000			5,00,000		
(3)	2,00,000			2,00,000	
(4)	1,00,000	1,00,000			
<b>Total 15,00,000</b>	<b>3,00,000</b>	<b>1,00,000</b>	<b>5,00,000</b>	<b>2,00,000</b>	<b>10,00,000</b>
<b>Balance 12,00,000</b>			<b>4,00,000</b>		<b>+ 8,00,000</b>

It is a tradition that:

- (i) increases in assets are recorded on the left-hand side and decreases in them on the right-hand side; and
- (ii) in the case of liabilities and capital, increases are recorded on the right-hand side and decreases on the left-hand side.

When two sides are put together in T form, the left-hand side is called the 'debit side' and the right hand side is 'credit side'. When in an account a record is made on the debit or left-hand side, one says that one has debited that account; similarly to record an amount on the credit or right-hand side, it is said the account has been credited.

From the above, the following rules can be obtained:

- (i) When there is an increase in the amount of an asset, its account is debited; the account will be credited if there is a reduction in the amount of the asset concerned: Suppose a firm purchases furniture for ₹ 8,00,000, the furniture account will be debited by ₹ 8,00,000 since the asset has increased by this amount. Suppose later the firm sells furniture to the extent of ₹ 3,00,000 the reduction will be recorded by crediting the furniture account by ₹ 3,00,000.

## FURNITURE

	Increase		Decrease
(1) To Cash	8,00,000	(2) By Cash	3,00,000
		Balance	5,00,000

- (ii) If the amount of a liability increases, the increase will be entered on the credit side of the liability account, i.e. the account will be credited: similarly, a liability account will be debited if there is a reduction in the amount of the liability. Suppose a firm borrows ₹ 5,00,000 from Mohan; Mohan's account will be credited since ₹ 5,00,000 is now owing to him. If, later, the loan is repaid, Mohan's account will be debited since the liability no longer exists.

## MOHAN

	Decrease		Increase
(2) To Cash	5,00,000	(1) By Cash	5,00,000

- (iii) An increase in the owner's capital is recorded by crediting the capital account: Suppose the proprietor introduces additional capital, the capital account will be credited. If the owner withdraws some money, i.e., makes a drawing, the capital account will be debited.
- (iv) Profit leads to an increase in the capital and a loss to reduction: According to the rule mentioned in (iii) above, profit & incomes may be directly credited to the capital account and losses & expenses may be similarly debited.

However, it is more useful to record all incomes, gains, expenses and losses separately. By doing so, very useful information will be available regarding the factors which have contributed to the year's profits and losses. Later the net result of all these is ascertained and adjusted in the capital account.

- (v) Expenses are debited and Incomes are credited: Since incomes and gains increase capital, the rule is to credit all gains and incomes in the accounts concerned and since expenses and losses decrease capital, the rule is to debit all expenses and losses. Of course, if there is a reduction in any income or gain, the account concerned will be debited; similarly, for any reduction in an expenses or loss the concerned account will be credited.

The rules given above are summarised below:

- Increases in assets are debits; decreases are credits;
- Increases in liabilities are credits; decreases are debits;
- Increases in owner's capital are credits; decreases are debits;
- Increases in expenses are debits; decreases are credits; and
- Increases in revenue or incomes are credits; decreases are debits.

The terms debit and credit should not be taken to mean, respectively, favourable and unfavourable things. They merely describe the two sides of accounts.

Whether an entry is to the debit or credit side of an asset depends on the type of account and the transactions

Debit	Credit
Increase in Purchases	Increase in Sales
Increase in Expenses	Increase in revenue and Incomes
Increase in Assets	Increase in Liabilities and Owners' Capital

In the same way, decrease in purchases, expenses and assets are credits and decrease in sales, income, liabilities and owners' capital are debit.

### ILLUSTRATION 1

Following are the transactions entered into by R after he started his business. Show how various accounts will be affected by these transactions:

2022 April		(₹ in 000)
1.	R started business with	5,000
2.	He purchased furniture for	1,200
3.	Paid salary to his clerk	1,100
4.	Paid rent	1,150
5.	Received interest	2,000

## SOLUTION

2022 April	Explanation	Accounts Involved	Nature of Accounts	How affected	Debit (₹ in 000)	Credit (₹ in 000)
1.	₹ 5,000 cash invested in business	Bank and R's Capital	Asset Capital	Increased Increased	5,000	5,000
2.	Purchased furniture for ₹ 1,200	Furniture and Bank	Asset Asset	Increased Decreased	1,200	1,200
3.	Paid ₹ 1,100 to employee for salary	Salary & Bank	Expense Asset	Increased Decreased	1,100	1,100
4.	Paid Rent ₹ 1,150	Rent & Bank	Expense Asset	Increased Decreased	1,150	1,150
5.	Received interest ₹ 2,000	Cash & Interest	Asset Income	Increased Increased	2,000	2,000



## 1.5 TRANSACTIONS

In the system of book-keeping, students can notice that transactions are recorded in the books of accounts. A transaction is a type of event, which is generally external in nature and can be determined in terms of money. In an accounting period, every business has huge number of transactions which are analysed in financial terms and then recorded individually, followed by classification and summarisation process, to know their impact on the financial statements. A transaction is a two-way process in which value is transferred from one party to another. In it either a party receives a value in terms of goods etc. and passes the value in terms of money or vice versa. Therefore, one can easily make out that in a transaction, a party receives as well as passes the value to other party. For recording transaction, it is very important that they are supported by a substantial document like purchase invoices, bills, pay-slips, cash-memos, passbook etc.

Transactions analysed in terms of money and supported by proper documents are recorded in the books of accounts under double entry system. To analyse the dual aspect of each transaction, two approaches can be followed:

- (1) Accounting Equation Approach.
- (2) Traditional Approach.



## 1.6 ACCOUNTING EQUATION APPROACH

The relationship of assets with that of liabilities and owners' equity in the equation form is known as 'Accounting Equation'. Basic accounting equation comes into picture when sum total of capital and liabilities equalises assets, where assets are what the business owns and capital and liabilities are what the business owes. Under double entry system, every business transaction has two-fold effect on the business enterprise where each transaction affects changes in assets, liabilities or capital in such a way that an accounting equation is completed and equated. This accounting equation holds good at all points of time and for any number of transactions and events except when there are errors in accounting process.

Let us suppose that an individual started business by contributing ₹ 50,00,000 and taking loan of ₹10,00,000 from a bank to be repayable, after 5 years. He purchased furniture costing ₹ 10,00,000, and merchandise worth ₹ 50,00,000. For purchasing the merchandise he paid ₹ 40,00,000 to the suppliers and agreed to pay balance after 3 months.

The contribution by the owner is termed as capital; the loans are termed as liabilities. Whenever the loan is repayable in the short-run, say within one year, it is called short-term loan or liability. On the other hand, if the loan is repayable atleast after one year, it would be termed as long term loan or liability.

Some other short-term liabilities relating to credit purchase of merchandise are popularly called as trade payables, and for other purchases and services received on credit as expense payables. The short-term liabilities are also termed as current liabilities and long term liabilities are termed as non-current liabilities.

On the other hand, money raised has been invested in two types of assets—fixed assets and current assets. Furniture is a fixed asset, if it lasts long, say more than one year, and has utility to the business, while inventory and cash balance will not remain fixed for long as soon as the business starts to roll—these are current assets.

Often the owner's claim or fund in the business is called equity. Owner's claim implies capital invested plus any profit earned minus any loss incurred.

Now we have an equation:

Equity + Liabilities = Assets or, Equity + Long-Term Liabilities = Fixed Assets + Current Assets - Current Liabilities

Check : L.H.S.	(₹ in '000)
Equity	₹ 5,000
Long-term Liabilities	₹ 1,000
Current Liabilities	<u>₹ 1,000</u>
	₹ 7,000

Check : R. H. S.	(₹ in '000)
Assets	
Fixed Assets:	
Furniture	₹ 1,000
Current Assets:	
Inventory	₹ 5,000
Cash	<u>₹ 1,000</u>
	₹ 7,000

$$\begin{aligned} \text{Cash} &= \text{Capital} + \text{Loan} - \text{Furniture} - \text{Payment to Trade payables (₹' 000)} \\ &= ₹ 5,000 + ₹ 1,000 - ₹ 1,000 - ₹ 4,000 = ₹ 1,000 \end{aligned}$$

Let us use  $E_0$ ,  $L_0$  and  $A_0$  to mean Equity, Liabilities and Assets respectively at  $t_0$ . Thus the basic accounting equation becomes

$$E_0 + L_0 = A_0$$

$$\text{or } E_0 = A_0 - L_0 \dots (\text{Eq. 1})$$

(₹' 000)

Now, let us suppose that at the end of period inventory valuing ₹ 2,500 is in hand, cash ₹ 2,000; trade payables ₹ 500; bank loan ₹ 1,000 (interest was properly paid); furniture ₹ 800 {₹ 200 is taken as loss of value due to use (also known as depreciation)}. So at  $t_1$  -

<b>Assets:</b>	<b>(₹' 000)</b>
<b>Fixed assets</b>	
Furniture	₹ 800
<b>Current assets</b>	
Inventory	₹ 2,500
Cash	<u>₹ 2,000</u>
( $A_1$ )	<u>₹ 5,300</u>
<b>Liabilities:</b>	
Long-term Liabilities	₹ 1,000
Current Liabilities	<u>₹ 500</u>
( $L_1$ )	<u>₹ 1,500</u>
Equity ( $A_1 - L_1$ )	₹ 3,800

**Equity = Assets - Liabilities**

i.e.,  $E_1 = A_1 - L_1$

or  $E_1 + L_1 = A_1$  ... (Eq. 2)

Let us compare  $E_1$  with  $E_0$ . Equity is reduced by ₹ 12,00,000 (50,00,000 - 38,00,000). Reduction in equity is termed as loss incurred.

Since the business has incurred loss during the period,  $E_1$  becomes less than  $E_0$ .

$E_1 < E_0$  implies loss during  $t_{01}$

Similarly,  $E_2 < E_1$  implies loss during  $t_{12}$  and so on.

On the other hand,  $E_1 > E_0$  implies profit earned by business during  $t_{01}$ ,  $E_2 > E_1$  implies profit earned during  $t_{2\&1}$  and so on.

So if  $E_n > E_{n-1}$ , in general terms, equity has increased, while  $E_n < E_{n-1}$  implies that equity has decreased. Increase in equity is termed as profit while decrease in equity is termed as loss.

**ILLUSTRATION 2**

Develop the accounting equation from following information available at the beginning of accounting period:

<b>Particulars</b>	<b>(₹ in '000)</b>
Capital	51,000
Loan	11,500
Trade payables	5,700
Fixed Assets	12,800
Inventory	22,600
Trade receivables	17,500
Cash and Bank	15,300

At the end of the accounting period the balances appear as follows:

	<b>₹</b>
Capital	?
Loan	11,500
Trade payables	5,800
Fixed Assets	12,720

Inventory	22,900
Trade receivables	17,500
Cash at Bank	15,600

- (a) Reset the equation and find out profit.  
 (b) Prepare Balance Sheet at the end of the accounting period.

**SOLUTION**

(All the figures in solution are in '000)

- (a) Accounting equation is given by

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

Let us use  $E_0$ ,  $L_0$  and  $A_0$  to mean equity, liabilities and assets respectively at the beginning of the accounting period.

$$E_0 = ₹ 51,000$$

$$\begin{aligned} L_0 &= \text{Loan} + \text{Trade payables} \\ &= ₹ 11,500 + ₹ 5,700 = ₹ 17,200 \end{aligned}$$

$$\begin{aligned} A_0 &= \text{Fixed Assets} + \text{Inventories} + \text{Trade receivables} + \text{Cash at Bank} \\ &= ₹ 12,800 + ₹ 22,600 + ₹ 17,500 + ₹ 15,300 = ₹ 68,200 \end{aligned}$$

So, at the beginning of accounting period

$$E_0 + L_0 = A_0$$

$$\text{i.e., } ₹ 51,000 + ₹ 17,200 = ₹ 68,200$$

Let us use  $E_1$ ,  $L_1$ ,  $A_1$  to mean equity, liabilities and assets respectively at the end of the accounting period.

$$\begin{aligned} L_1 &= \text{Loan} + \text{Trade payables} \\ &= ₹ 11,500 + ₹ 5,800 = ₹ 17,300 \end{aligned}$$

$$\begin{aligned} A_1 &= \text{Fixed Assets} + \text{Inventories} + \text{Trade receivables} + \text{Cash at Bank} \\ &= ₹ 12,720 + ₹ 22,900 + ₹ 17,500 + ₹ 15,600 = ₹ 68,720 \end{aligned}$$

$$E_1 = A_1 - L_1 = ₹ 68,720 - ₹ 17,300 = ₹ 51,420$$

$$\text{Profit} = E_1 - E_0 = ₹ 51,420 - ₹ 51,000 = ₹ 420$$

(b)

## Balance Sheet

Liabilities	₹	₹	Assets	₹
Capital			Fixed Assets	12,720
Balance	51,000		Inventories	22,900
Add: Profit	<u>420</u>	51,420	Trade receivables	17,500
Loan		11,500	Cash at Bank	15,600
Trade payables		<u>5,800</u>		_____
		68,720		68,720

## ILLUSTRATION 3

Mr. David. has provided following details related to his financials. Find out the missing figures:

Particulars	(₹ in '000)
Profits earned during the year	5,000
Assets at the beginning of year	A
Liabilities at the beginning of year	12,000
Assets at the end of the year	B
Liabilities at the end of the year	C
Closing capital	35,000
Total liabilities including capital at the end of the year	50,000

## SOLUTION

Computing opening capital:

(All figure in ₹' 000 )

Closing capital - profits earned during the year (35,000 - 5,000) = 30,000

We also know:

Assets = liabilities + capital

Therefore, opening assets (A) (12,000 + 30,000) = 42,000

Computation of liabilities at the end of the year:

Total liabilities including capital - closing capital (C) (50,000 - 35,000) = 15,000

Also assets at the end of the year (B) = closing capital + liabilities at the end of the year  
= 35,000 + 15,000 = 50,000



## 1.7 TRADITIONAL APPROACH

Under traditional approach of recording transactions one should first understand the term debit and credit and their rules. The term debit and credit have already been explained in para 1.4 of this Unit.

Transactions in the journal are recorded on the basis of the rules of debit and credit only. For the purpose of recording, these transactions are classified in three groups:

- (i) Personal transactions.
- (ii) Transactions related to assets and properties.
- (iii) Transactions related to expenses, losses, income and gains.

### 1.7.1 Classification of Accounts

- (i) **Personal Accounts:** Personal accounts relate to persons, trade receivables or trade payables. Example would be the account of Ram & Co., a credit customer or the account of Jhaveri & Co., a supplier of goods. The capital account is the account of the proprietor and, therefore, it is also personal but adjustment on account of profits and losses are made in it. This account is further classified into three categories:
  - (a) **Natural personal accounts:** It relates to transactions of human beings like Ram, Rita, etc.
  - (b) **Artificial (legal) personal accounts:** For business purpose, business entities are treated to have separate entity. They are recognised as persons in the eye of law for dealing with other persons. For example: Government, Companies (private or limited), Clubs, Co-operative societies etc.
  - (c) **Representative personal accounts:** These are not in the name of any person or organisation but are represented as personal accounts. For example: outstanding liability account or prepaid account, capital account, drawings account.
- (ii) **Impersonal Accounts:** Accounts which are not personal such as machinery account, cash account, rent account etc. These can be further sub-divided as follows:
  - (a) **Real Accounts:** Accounts which relate to assets of the firm but not debt. For example, accounts regarding land, building, investment, fixed deposits etc., are real accounts. Cash in hand and Cash at the bank accounts are also real.
  - (b) **Nominal Accounts:** Accounts which relate to expenses, losses, gains, revenue, etc. like salary account, interest paid account, commission received account. The net result of all the nominal accounts is reflected as profit or loss which is transferred to the capital account. Nominal accounts are, therefore, temporary.

### 1.7.2 Golden Rules of Accounting

All the above classified accounts have two rules each, one related to Debit and one related to Credit for recording the transactions which are termed as golden rules of accounting, as transactions are recorded on the basis of double entry system.

Types of Account	Account to be Debited	Account to be Credited
Personal Account	Receiver	Giver
Real Account	What comes in	What goes out
Nominal Account	Expense and losses	Income and gains

#### Example:-

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

- Started business with a capital of ₹ 50,00,000.
- Wages and salaries paid ₹ 50,000
- Rent received ₹ 2,00,000
- Purchased goods on credit ₹ 9,00,000
- Sold goods for ₹ 8,16,000 and received payment in cheque.

#### SOLUTION

Transaction	ACCOUNTS INVOLVED	NATURE	DEBIT OR CREDIT	Journal Entry
Started business with capital of ₹ 50,00,000	Bank account Capital account	Personal Personal	Debit (Receiver) Credit (giver)	Bank A/c Dr. To Capital A/c
Wages and salaries paid	Wages/salaries Bank	Nominal Personal	Debit (expense) Credit (giver)	Wages/ Salaries Dr. To Bank A/c
Rent received	Bank Rent	Personal Nominal	Debit (Receiver) Credit (income)	Bank A/c Dr. To Rent A/c
Purchases made on credit	Purchases Creditor	Nominal Personal	Debit (expense) Credit (giver)	Purchases A/c Dr. To Creditor A/c
Goods sold and payment received in cheque	Bank Sales	Personal Nominal	Debit (Receiver) Credit (gains)	Bank A/c Dr. To Sales A/c



## 1.8 MODERN CLASSIFICATION OF ACCOUNTS

Real, nominal and personal accounts is the traditional classification of accounts. Now, let us see the modern and more acceptable classification of accounts:-

Types of account	Normal balance of account	Account to be debited when there is:	Account to be credited when there is:
Asset account	Debit	Increase	Decrease
Liabilities account	Credit	Decrease	Increase
Capital account	Credit	Decrease	Increase
Revenue account	Credit	Decrease	Increase
Expenditure account	Debit	Increase	Decrease
Withdraw account	Debit	Increase	Decrease

Let us solve the same example with the modern approach now:-

Accounts involved	Nature	Debit/Credit	Reason
Cash	Asset	Debit	Increase
Capital	Liability	Credit	Increase
Wages/salaries paid	Expense	Debit	Increase
Cash	Asset	Credit	Decrease
Rent received	Revenue	Credit	Increase
Purchase	Expense	Debit	Increase
Creditor	Liability	Credit	Increase
Cash	Asset	Debit	Increase
Sales	Revenue	Credit	Increase



## 1.9 JOURNAL

Transactions are first entered in this book to show which accounts should be debited and which credited. Journal is also called subsidiary book. Recording of transactions in journal is termed as journalizing the entries. It is the book of original entry in which transactions are entered on a daily basis in a chronological order.

### 1.9.1 Journalising Process

All transactions may be first recorded in the journal as and when they occur; the record is chronological; otherwise it would be difficult to maintain the records in an orderly manner. Debits and credits are listed along with the appropriate explanations. There are basically two types of journals:-

1. General journal
2. Specialized journal

The latter is used when there are many repetitive transactions of the same nature. The form of the journal is given below:

#### JOURNAL

Date	Particulars	Ledger Folio (L.F.)	Amount Dr.	Amount Cr.
			₹	₹
(1)	(2)	(3)	(4)	(5)

The columns have been numbered only to make clear the following but otherwise they are not numbered. The following points should be noted:

- (1) In the first column the date of the transaction is entered-the year is written at the top, then the month and in the narrow part of the column the particular date is entered.
- (2) In the second column, the names of the accounts involved are written; first the account to be debited, with the word "Dr" written towards the end of the column. In the next line, after leaving a little space, the name of the account to be credited is written preceded by the word "To" (the modern practice shows inclination towards omitting "Dr." and "To"). Then in the next line the explanation for the entry together with necessary details is given-this is called narration.
- (3) In the third column the number of the page in the ledger on which the account is written up is entered.
- (4) In the fourth column the amounts to be debited to the various accounts concerned are entered.
- (5) In the fifth column, the amount to be credited to various accounts is entered.

### 1.9.2 Points to be taken into account while recording a transaction in the Journal

- Journal entries can be single entry (i.e. one debit and one credit) or compound entry (i.e. one debit and two or more credits or two or more debits and one credit or two or more debits and credits). In such cases, it is important to check that the total of both debits and credits are equal.
- If journal entries are recorded in several pages then both the amount column of each page should be totalled and the balance should be written at the end of that page and also that the same total should be carried forward at the beginning of the next page.

An entry in the journal may appear as follows:

			₹	₹
May 5	Bank Account	Dr.	14,50,000	
	To Mohan			14,50,000
	(Being the amount received from Mohan in payment of the amount due from him)			

We will now consider some individual transactions.

- (i) Mohan commences business with ₹ 50,00,000 in his bank account. This means that the firm has ₹ 50,00,000 in bank. According to the rules given above, the increase in an asset has to be debited. The firm also now owes ₹ 50,00,000 to the proprietor, Mohan as capital. The rule given above also shows that the increase in capital should be credited. Therefore, the journal entry will be:

Bank Account	Dr.	₹ 50,00,000	
To Capital Account			₹ 50,00,000
(Being capital introduced by Mohan)			

- (ii) Out of the above, ₹ 25,000 is withdrawn from the bank. By this transaction the bank balance is reduced by ₹ 25,000 and another asset, cash account, comes into existence. Since increase in assets is debited and decrease is credited, the journal entry will be:

Cash Account	Dr.	₹ 25,000	
To Bank Account			₹ 25,000
(Being cash withdrawn in Bank)			

- (iii) Furniture is purchased for ₹ 12,00,000. Applying the same reasoning as above the entry will be:

Furniture Account	Dr.	₹ 12,00,000	
To Bank Account			₹ 12,00,000
(Being Furniture purchased vide voucher No....)			

- (iv) Purchased goods for ₹ 4,00,000. The student can see that the required entry is:

Purchases Account	Dr.	₹ 4,00,000	
To Bank Account			₹ 4,00,000
(Being goods purchased vide voucher No....)			

- (v) Purchased goods for ₹ 10,00,000 on credit from M/s Ram Narain Bros. Purchase of merchandise is an expense item so it is to be debited. ₹ 10,00,000 is now owing to the supplier; his account should therefore be credited, since the amount of liabilities has increased. The entry will be:

Purchases Account	Dr.	₹ 10,00,000	
To M/s Ram Narain Bros.			₹ 10,00,000
(Being goods purchased on credit vide Bill No.....)			

- (vi) Sold goods to M/s Ram & Co. for ₹ 6,00,000. Amount is received in cheque. The amount of bank increases and therefore, the bank amount should be debited; sale of merchandise is revenue item so it is to be credited. The entry will be:

Bank Account	Dr.	₹ 6,00,000	
To Sales Account			₹ 6,00,000
(Being goods sold vide sales invoice No....)			

- (vii) Sold goods to Ramesh on credit for ₹ 13,00,000. The Inventories of goods has decreased and therefore, the goods account has to be credited. Ramesh now owes ₹ 13,00,000; that is an asset and therefore, Ramesh should be debited. The entry is:

Ramesh	Dr.	₹ 13,00,000	
To Sales Account			₹ 13,00,000
(Being goods sold vide Bill No....)			

- (viii) Received cheque from Ramesh ₹ 13,00,000. The amount of bank increased therefore the bank account has to be debited. Ramesh's liability towards firm has decreased in fact in this case he no longer owes any amount to the firm now, i.e., this particular form of assets has disappeared; therefore, the account of Ramesh should be credited. The entry is:

Bank Account	Dr.	₹ 13,00,000	
To Ramesh			₹ 13,00,000
(Being amount received vide cheque No.....against sales invoice No....)			

- (x) Paid rent ₹ 1,00,000. The bank balance has decreased and therefore, the bank account should be credited. No asset has come into existence because the payment is for services enjoyed and is an expense. Expenses are debited. Therefore, the entry should be:

Rent Account	Dr.	₹ 1,00,000	
To Bank Account			₹ 1,00,000
(Being rent paid for the month of .....)			

- (xi) Paid ₹ 22,000 to the clerk as salary. Applying the reasons given in (x) above, the required entry is:

Salary Account	Dr.	₹ 22,000	
To Bank Account			₹ 22,000
(Being salary paid to Mr..... for the month of .....)			

- (xii) Received ₹ 2,20,000 interest. The bank account should be debited since there is an increase in the bank balance. There is no increase in any liability; since the amount is not returnable to any one, the amount is an income, incomes are credited. The entry is:

Bank Account	Dr.	₹ 2,20,000	
To Interest Account			₹ 2,20,000
(Being interest received from.....for the period .....)			

When transactions of similar nature take place on the same date, they may be combined while they are journalised. For example, entries (x) and (xi) may be combined as follows:

Rent Account	Dr.	₹ 1,00,000	
Salary Account	Dr.	₹ 22,000	
To Bank Account (Being expenses done as per detail attached)			₹ 1,22,000

When journal entry for two or more transactions are combined, it is called composite journal entry. Usually, the transactions in a firm are so numerous that to record the transactions for a month will require many pages in the journal. At the bottom of one page the totals of the two columns are written together with the words "Carried forward" in the particulars column. The next page is started with the respective totals in the two columns with the words "Brought forward" in the particulars column.

#### ILLUSTRATION 4

Analyse transactions of M/s Sahil & Co. for the month of March, 2022 on the basis of double entry system by adopting the following approaches:

- (A) Accounting Equation Approach.  
 (B) Traditional Approach.

Transactions for the month of March, 2022 were as follows (figures are in '000):

- Sahil introduced capital through bank of ₹ 4,000.
- Cash withdrawn from the City Bank ₹ 200.
- Loan of ₹ 500 taken from Mr. Y.
- Salaries paid for the month of March, 2022, ₹ 300 and ₹ 100 is still payable for the month of March, 2022.
- Furniture purchased ₹ 500.

Required

What conclusions one can draw from the above analysis?

#### SOLUTION

- (A) Analysis of Business Transaction: Accounting Equation Approach

The accounting equation is

Assets = Liabilities + Capital

(₹ in '000)

ASSETS					=	CAPITAL	+	LIABILITIES	
	CASH	+	BANK	+	FURNITURE	=	CAPITAL	+	LIABILITIES
(a)	-	+	4,000	+	-	=	4,000	+	-
(b)	+200	+	-200	+	-	=	-	+	-
(c)	-	+	500	+	-	=	-	+	500
(d)	-	+	-300	+	-	=	-400	+	100
(e)	-	+	-500	+	500	=	-	+	-
<b>Balance</b>	<b>200</b>	<b>+</b>	<b>3,500</b>	<b>+</b>	<b>500</b>	<b>=</b>	<b>3,600</b>	<b>+</b>	<b>600</b>
			<b>4,200</b>				<b>4,200</b>		

## (B) Analysis of Business Transactions: Traditional Approach

Transaction	Analysis	Account Affected and Nature of Account	Rule	Entry
Introduction of ₹ 4,000 through bank by the proprietor	Bank has received the money; Owner has given Bank balance	Bank–Personal Capital–Personal	Debit the receiver Credit the giver	Debit Bank Credit Capital
Cash Withdrawn from Bank ₹ 200	Cash comes into business; Bank gives out cash	Cash–Real Bank–Personal	Debit what comes in Credit the giver	Debit Cash Credit Bank
Loan from Y ₹ 500	Bank receives the amount : Y pays through bank	Bank–Personal Y's Loan–Personal	Debit the receiver Credit the giver	Debit Bank Credit Y's Loan
Salary paid ₹ 300 and still payable ₹ 100	Cost of services used ₹ 400; Bank gives out ₹300; Still payable or outstanding for services received ₹ 100	Salary Nominal Bank–Personal Salary Outstanding–Personal	Debit all expenses Credit the giver  Credit the giver	Debit Salary (₹ 400) Credit Bank (₹ 300) Credit Salary outstanding (₹ 100)

Furniture purchased ₹ 500	Furniture is purchased; Bank gives out money	Furniture Real Bank–Personal	Debit what comes in Credit the giver	Debit Furniture Credit Bank
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**Conclusion:**

It is evident from above analysis that procedure for analysis of transactions, classification of accounts and rules for recording business transactions under accounting equation approach and traditional approach are different. But the accounts affected and entries entered/passed remains the same under both approaches. Thus, the recording of transactions in affected accounts on the basis of double entry system is independent of the method of analysis followed by a business enterprise. In other words, accounts to be debited and credited to record the dual aspect remains the same under both the approaches.

**ILLUSTRATION 5**

*Journalise the following transactions. Also state the nature of each account involved in the Journal entry.*

*Following figures are given in ('00)*

1. *December 1, 2022, Ajit started business with capital ₹ 4,00,000*
2. *December 3, he withdrew cash for business from the Bank ₹ 2,000.*
3. *December 5, he purchased goods by making payment through bank ₹ 15,000.*
4. *December 8, he sold goods for ₹ 16,000 and received payment through bank.*
5. *December 10, he purchased furniture and paid by cheque ₹ 2,500.*
6. *December 12, he sold goods to Arvind ₹ 2,400.*
7. *December 14, he purchased goods from Amrit ₹ 10,000.*
8. *December 15, he returned goods to Amrit ₹ 500.*
9. *December 16, he received from Arvind ₹ 2,300 in full settlement.*
10. *December 18, he withdrew goods for personal use ₹ 1,000.*
11. *December 20, he withdrew cash from business for personal use ₹ 2,000.*
12. *December 24, he paid telephone charges ₹ 110.*
13. *December 26, amount paid to Amrit in full settlement ₹ 9,450.*
14. *December 31, paid for stationery ₹ 200, rent ₹5,000 and salaries to staff ₹ 2,000 from bank.*

15. December 31, goods distributed by way of free samples ₹ 2,000.

**SOLUTION**

**JOURNAL**

(₹ in '00)

Sl. No	Date	Particulars		Nature of Account	L.F.	Dr.	Cr.
						Debit (₹)	Credit (₹)
1.	Dec. 1	Bank Account To Capital Account (Being commencement of business with capital)	Dr.	Personal A/c Personal A/c		4,00,000	4,00,000
2.	Dec. 3	Cash Account To Bank Account (Being cash withdrawn from the Bank)	Dr.	Real A/c Personal A/c		2,000	2,000
3.	Dec. 5	Purchases Account To Bank Account (Being purchase of goods for cash)	Dr.	Nominal A/c Personal A/c		15,000	15,000
4.	Dec. 8	Bank Account To Sales Account (Being goods sold for cash)	Dr.	Personal A/c Nominal A/c		16,000	16,000
5.	Dec. 10	Furniture Account To Bank Account (Being purchase of furniture, paid by cheque)	Dr.	Real A/c Personal A/c		2,500	2,500
6.	Dec. 12	Arvind Account To Sales Account (Being sale of goods on credit)	Dr.	Personal A/c Nominal A/c		2,400	2,400

7.	Dec. 14	Purchases Account To Amrit Account (Being purchase of goods from Amrit)	Dr.	Nominal A/c Personal A/c		10,000	10,000
8.	Dec. 15	Amrit To Purchases Returns Account (Being goods returned to Amrit)	Dr.	Personal A/c Nominal A/c		500	500
9.	Dec. 16	Bank Account Discount Account To Arvind Account (Being amount received from Arvind in full settlement and allowed him ₹ 100 as discount)	Dr. Dr.	Personal A/c Nominal A/c Personal A/c		2,300 100	2,400
10.	Dec. 18	Drawings Account To Purchases Account (Being withdrawal of goods for personal use)	Dr.	Personal A/c Nominal A/c		1,000	1,000
11.	Dec. 20	Drawings Account To Cash Account (Being cash withdrawal from the business for personal use)	Dr.	Personal A/c Real A/c		2,000	2,000
12.	Dec. 24	Telephone Expenses Account To Bank Account (Being telephone expenses paid)	Dr.	Nominal A/c Personal A/c		110	110

13.	Dec 26	Amrit Account To Bank Account To Discount Account (Being cash paid to Amrit and he allowed ₹ 50 as discount)	Dr.	Personal A/c Personal A/c Nominal A/c	9,500	9,450 50
14.	Dec. 31	Stationery Expenses Rent Account Salaries Account To Bank Account (Being expenses paid)	Dr. Dr. Dr.	Nominal A/c Nominal A/c Nominal A/c Personal A/c	200 5,000 2,000	7,200
15.	Dec. 31	Advertisement Expenses Account To Purchases Account (Being distribution of goods by way of free samples)	Dr.	Nominal A/c Nominal A/c	2,000	2,000

**ILLUSTRATION 6**

Show the classification of the following Accounts under traditional and accounting equation approach:

(a) Building; (b) Purchases; (c) Sales; (d) Bank Fixed Deposit; (e) Rent; (f) Rent Outstanding; (g) Cash; (h) Adjusted Purchases; (i) Closing Inventory; (j) Investments; (k) Trade receivables; (l) Sales Tax Payable, (m) Discount Allowed; (n) Bad Debts; (o) Capital; (p) Drawings; (q) Interest Receivable account; (r) Rent received in advance account; (s) Prepaid salary account; (t) Bad debts recovered account; (u) Depreciation account, (v) Personal income-tax account.

**SOLUTION****Nature of Account**

Sl. No.	Title of Account	Traditional Approach	Accounting Approach	Equation
(a)	Building	Real	Asset	
(b)	Purchases	Nominal	Expense	
(c)	Sales	Nominal	Revenue	

(d)	Bank Fixed Deposit	Personal	Asset
(e)	Rent	Nominal	Expense
(f)	Rent Outstanding	Personal	Liability
(g)	Cash	Real	Asset
(h)	Adjusted Purchases	Nominal	Expense
(i)	Closing Inventory	Real	Asset
(j)	Investment	Real	Asset
(k)	Trade receivables	Personal	Asset
(l)	GST Payable	Personal	Liability
(m)	Discount Allowed	Nominal	Expense
(n)	Bad Debts	Nominal	Expense
(o)	Capital	Personal	Capital
(p)	Drawings	Personal	Capital - Drawings
(q)	Interest receivable	Personal	Asset
(r)	Rent received in advance	Personal	Liability
(s)	Prepaid salary	Personal	Asset
(t)	Bad debts recovered	Nominal	Gain
(u)	Depreciation	Nominal	Expense
(v)	Personal Income Tax	Personal (Drawings)	Capital - Drawings

**ILLUSTRATION 7**

Transactions of Ramesh for April are given below. Journalise them.

2022			₹
April	1	Ramesh started business with	10,00,000
"	3	Bought goods for cash	50,000
"	5	Drew cash from bank	10,000
"	13	Sold to Krishna- goods on credit	1,50,000
"	20	Bought from Shyam goods on credit	2,25,000
"	24	Received from Krishna	1,45,000
"		Allowed him discount	5,000

"	28	Paid Shyam cash	2,15,000
"		Discount allowed	10,000
"	30	Cash sales for the month	8,00,000
		Paid Rent	50,000
		Paid Salary	1,00,000

**SOLUTION****JOURNAL**

Date 2022	Particulars		L.F.*	Amount (Dr.)	Amount (Cr.)
April 1	Bank Account	Dr.	1	10,00,000	
	To Capital Account (Being the amount invested by Ramesh in the business as capital)		4		10,00,000
" 3	Purchases Account	Dr.	7	50,000	
	To Bank Account (Being goods purchased for cash)		1		50,000
" 5	Cash Account	Dr.	5	10,000	
	To Bank Account (Being cash withdrawn from bank)		1		10,000
" 13	Krishna	Dr.	9	1,50,000	
	To Sales Account (Being goods sold to Krishna on credit)		11		1,50,000
" 20	Purchases Account	Dr.	7	2,25,000	
	To Shyam (Being goods bought from Shyam on credit)		10		2,25,000
" 24	Bank Account	Dr.	1	1,45,000	
	Discount Account	Dr.	12	5,000	
	To Krishna (Being cash received from Krishna and discount allowed to him)		9		1,50,000

" 28	Shyam	Dr.	10	2,25,000	
	To Bank Account		1		2,15,000
	To Discount Account		12		10,000
	(Being cash paid to Shyam and discount allowed by him)				
" 30	Bank Account	Dr.	1	8,00,000	
	To Sales Account		11		8,00,000
	(Being sales for the month of April 2022)				
" 30	Rent Account	Dr.	15	50,000	
	Salaries Account	Dr.	14	1,00,000	
	To Bank Account		1		1,50,000
	(Being the amount paid for rent and salary)				
	Total			27,60,000	27,60,000

### \*Ledger Folio imaginary



## 1.10 ADVANTAGES OF JOURNAL

In journal, transactions recorded on the basis of double entry system, fetch the following advantages:

1. As transactions are recorded in chronological order, one can get complete information about the business transactions on timely basis.
2. Entries recorded in the journal are supported by a note termed as narration, which is a precise explanation of the transaction for the proper understanding of the entry. One can know about the transactions through these narrations.
3. Journal forms the basis for posting the entries in the ledger and reduces the chances of error.



## 1.11 ACCOUNTING FOR GST

### 1.11.1 Introduction to GST

Goods and Services Tax (GST) is a comprehensive Indirect Tax\* which has subsumed multiple Indirect Taxes in India such as State Value added Tax (VAT) which was levied on sale of goods, Excise Duty, which was levied on manufacture or production of goods, Service Tax which was levied on provision of services etc. GST is a single tax on the supply of goods and services, right from the manufacturer to consumer.

\* An indirect tax is a tax whose incidence is borne by the consumers who ultimately consume the product or service. The immediate liability to pay the tax may fall upon another person such as a manufacturer or provider of service or seller of goods, but the same is collected from the person purchasing the goods (recipient of goods or services).

#### Pre-GST scenario:

Prior to introduction of GST, the following duties were levied:

- (a) On manufacture of goods: Excise Duty (levied by Central Government)
- (b) On sale of goods within the State: State Value Added Tax (VAT)
- (c) On sale of goods outside the State: Central Sales Tax (levied by Central Government)
- (d) On provision of services provided: Service Tax (levied by Central Government)

Since the taxes were levied by different authorities (central and state authorities), it was not possible to take the benefit of credit of taxes paid at different stages. For instance, when a trader received goods (say costing ₹ 1,00,000) from the manufacturer, excise duty (say @ 18% = ₹ 18,000) was levied on the goods sold by the manufacturer. When such trader would sell the goods to the customer, he would charge VAT (assume 18%). However, the trader could not avail the benefit of the credit of the excise duty of ₹ 18,000 paid in respect of the goods purchased from the manufacturer. Accordingly, the 'cost' of the goods to the trader would be ₹ 1,00,000 + ₹ 18,000 = ₹ 1,18,000, on which the trader would add his profit margin and levy VAT while selling to the consumer. This created a scenario wherein a tax (in our example, VAT) was levied on the tax (in our example, excise duty) also, in addition to the tax levied on the goods. This cascading effect (tax-on-tax) increased the price of the product, and resulted in an unjust enrichment at the cost of the ultimate consumer.

#### Post-GST scenario:

On introduction of GST, the tax to be levied at all stages right from manufacture up to final consumption was a single tax- GST, with credit of taxes paid at previous stages available as setoff. Thus, in the example above, the GST (erstwhile excise duty) of ₹ 18,000 paid by the

trader could be availed as a credit (an asset), for set off against the tax charged by the trader (a liability for the trader, which would be received from the consumer). Hence, the cost of the goods to the trader would be ₹ 1,00,000 only, as ₹ 18,000 can be set off against the GST charged by the trader to the consumer. The tax levied by the manufacturer to the trader becomes 'input tax' for the trader, since the goods are purchased by him (it is his input). The tax levied by the manufacturer to the trader, or the trader to the consumer is known as 'output tax' (since it is output for both the manufacturer and trader) both for the manufacturer and trader. The 'input tax' cannot be added to the cost of the goods or services procured, as it will be adjusted against the 'output tax' liability. In a nutshell, since the input tax is availed as a credit, only the value addition (i.e., the profit margin levied by the trader to the consumer in our example) will be taxed, with the burden of tax being borne by the final consumer.

### 1.11.2 Salient features of GST

- GST is levied on supply i.e., manufacture or sale of goods and provision of services. In other words, supply is taxable event which on its occurrence creates or attracts the liability to pay tax.
- Under GST, tax is levied only on the value added at each stage of the supply chain.
- GST is a destination-based consumption tax, i.e. the tax is levied at the place where the goods or services are consumed, rather than the place where they are produced.
- There is no **tax on tax** or cascading of taxes under GST system.
- Under GST, there is a harmonization of laws, procedures and rates of tax across the country.

### 1.11.3 Types of Taxes under GST

Before going through the types of taxes under GST, it is important to understand the concept of intra-State supply and inter-State supply under GST which determines the type of tax to be charged by the supplier.

The Concept of intra-state supply and inter-state supply depends upon on the location of the supplier and place of supply (place of supply is the place where goods/services are consumed).

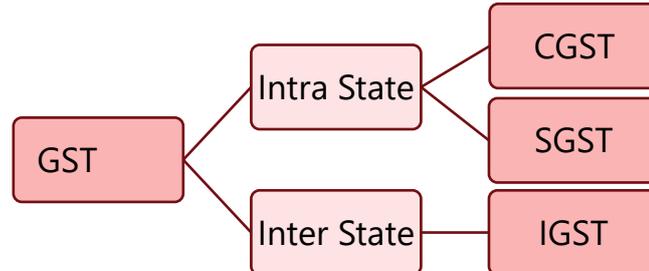
As a general rule, where the location of the supplier and the place of supply of goods or services are in the same State/Union territory, it is treated as **intra-State supply** of goods or services respectively.

Similarly, where the location of the supplier and the place of supply of goods or services are in (i) two different States or (ii) two different Union Territories or (iii) a State and a Union territory, it is treated as **inter-State supply** of goods or services respectively.

GST has a dual aspect with the Centre and States simultaneously levying on a common tax base. There are three main components of GST which are:

- (i) **Central Goods and Service Tax (CGST)** is levied and collected by the Centre on the “**Intra -State**” supply of goods and services.
- (ii) **State Goods and Services Tax (SGST)** is levied and collected by the State Governments (including Union Territories with legislature, for example Delhi, Pondicherry, Jammu and Kashmir) on “**Intra state**” supply of goods and services
- (iii) **Union Territory Goods and Service Tax (UTGST)** is levied and collected by Union Territories without Legislatures [i.e. Andaman and Nicobar Islands, Lakshadweep, Ladakh, Dadra and Nagar Haveli & Daman and Diu and Chandigarh] on “intra-state” supply of goods and services.
- (iv) **Integrated Goods and services tax (IGST):** It is the GST levied on the “**inter state**” supply of goods and services and is collected by the Centre. IGST is equivalent to the sum total of CGST and SGST.

*GST is a “Consumption Based Tax” i.e. the tax is received by the State in which the goods or services are consumed and not by the state in which the goods and services are manufactured.*



### 1.11.4 Input and Output GST

The tax paid by the recipient on procurement of goods /services is called **Input tax**. An entity at each stage is permitted to avail credit of GST paid on the purchase of goods and /or avilment of services and can set off this credit against the GST payable on the goods and/or services supplied by him. Thus, the final consumer bears the GST charged in the supply chain, with set-off benefits at all the previous stages. Hence, the tax will be levied only on the value added, which results in avoiding double taxation. For example, if tax payable by a manufacturer on the output, i.e. final product is ₹750 and he has already paid tax on ₹500 on input, i.e. purchases, then he can claim ‘Input Credit’ of ₹500 and he needs to deposit only ₹250 in cash.

**Output tax** means the GST charged on supply of goods or services made by a supplier.

**Input tax** means the credit of Input tax already paid.

### Utilisation of Input Tax Credit under GST

Tax credit of CGST, SGST and IGST can be utilized in the following manner:

- Utilization of IGST Credit: IGST credit has to be first utilized against IGST liability and if any balance is still available, the same can be utilized against CGST or/and SGST in any order and in any proportion.
- Utilization of CGST Credit: CGST credit has to be first utilized against CGST liability and if any balance is available, same can be utilized against IGST. However, CGST credit cannot be utilized against SGST.
- Utilization of SGST Credit: SGST credit has to be first utilized against SGST liability and if any balance is available, same can be utilized against IGST. However, SGST credit cannot be utilized against CGST.

	<b>Input GST (credit can be availed, hence asset)</b>	<b>Output GST (charged to the consumer, payable by the supplier, hence liability)</b>
Nature	At the time of purchases of goods (including fixed assets) or services, input GST A/c (CGST and SGST or IGST) is debited.	At the time of sale of goods/assets or supply of services, Output GST A/c (CGST and SGST or IGST) is credited.
Intra-state transaction	CGST paid is debited to "Input CGST Account" and SGST paid is debited to Input SGST".	CGST charged is credited to "Output CGST Account" and SGST charged is credited to "Output SGST Account "
Inter-state transaction	IGST paid is debited to "Input IGST Account".	IGST charged is credited to "Output IGST Account"
Reversal of GST	Input GST paid at the time of purchase are reversed in the following situations: (i) Purchases Return (ii) Drawings (iii) Goods distributed as free samples (iv) Goods distributed as gift (if the same does not qualify as "supply under GST").	Output GST charged is reversed when the goods are returned by the purchaser.

	(v) Goods lost in fire or theft. (vi) Input tax credit of supplies which are not allowed to be availed by recipient.	
Utilization of Input tax credit	Input GST A/c is credited when tax is paid by utilizing input tax.	

### Double entry book-keeping with GST

The Double entry book-keeping records need to show the GST values separately so that the purchases, expenses and sales are posted net i.e. without the addition of GST.

#### Journal entry in case of Sales of Goods or services

Account Receivable/Debtors A/c	Dr.	Gross Amount (including GST)
To Sales A/c		Net Amount (excluding GST)
To Output GST		Amount of GST

#### Journal entry in case of Purchase of Goods or services

Purchases A/c	Dr.	Net Amount (excluding GST)
Input GST A/c	Dr.	Amount of GST
To Account Payable/Creditors		Gross Amount (including GST)

#### Journal entry in case of Utilization of Input Tax Credit towards payment of Output Tax

Output CGST A/c	Dr.	Amount of GST liability
Output SGST A/c	Dr.	Amount of GST liability
Output IGST A/c	Dr.	Amount of GST liability
To Input CGST A/c		Amount of output GST liability paid utilizing Input CGST
To Input SGST A/c		Amount of output GST liability paid utilizing Input SGST
To Input IGST A/c		Amount of output GST liability paid utilizing Input IGST

**ILLUSTRATION 8**

Journalise the following transactions in the books of Mr. Rohit:

- (i) Purchased goods from Sahil for ₹ 50,000 plus CGST and SGST @ 9% each.
- (ii) Purchased goods from Sam for ₹ 40,000 at a trade discount of 10% plus CGST and SGST @ 9% each. ₹ 20,000 was paid immediately and balance payable after 3 months.
- (iii) Goods costing ₹ 20,000 withdrawn for personal use. Such goods were purchased by paying CGST and SGST @ 9% each.
- (iv) Paid rent to Gagandeep for ₹ 30,000 plus CGST and SGST @ 6% each.
- (v) Goods costing ₹ 5,000 (before trade discount of 10%) returned to Sam. Such goods were purchased by paying CGST and SGST @ 9% each.
- (vi) Purchased furniture for ₹ 44,800 including IGST @ 12%.
- (vii) Purchased machinery from M/s Symphony industries for ₹ 1,40,000 plus CGST and SGST @ 9% each. Paid ₹ 1,00,000 immediately and balance to be paid after two months.

**SOLUTION****In the books of Mr. Rohit**

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
(i)	Purchases A/c	Dr.	50,000	
	Input CGST A/c (50,000 x 9%)	Dr.	4,500	
	Input SGST A/c (50,000 x 9%)	Dr.	4,500	
	To Sahil's A/c			59,000
	(Being goods purchased from Sahil, CGST and SGST paid @ 9% each)			
(ii)	Purchases A/c (40,000 x 90%)	Dr.	36,000	
	Input CGST A/c (36,000 x 9%)	Dr.	3,240	
	Input SGST A/c (36,000 x 9%)	Dr.	3,240	
	To Sam's A/c			22,480
	To Bank A/c			20,000
	(Being goods purchased from Sam, CGST and SGST payable @ 9% each)			
(iii)	Drawings A/c*	Dr.	23,600	
	To Purchase A/c			20,000

	To Input CGST A/c (20,000 x 9%)			1,800
	To Input SGST A/c (20,000 x 9%)			1,800
	(Being goods withdrawn for personal use and input GST and input SGST debited at the time of purchase reversed)			
(iv)	Rent A/c	Dr.	30,000	
	Input CGST A/c (30,000 x 6%)	Dr.	1,800	
	Input SGST A/c (30,000 x 6%)	Dr.	1,800	
	To Gagandeep A/c			33,600
	(Being rent paid to Gagandeep)			
(v)	Sam's A/c	Dr.	5,310	
	To Purchases Return A/c **			4,500
	( 5,000 – 10% trade Discount)			
	To Input CGST A/c (4,500 x 9%)			405
	To Input SGST A/c (4,500 x 9%)			405
	(Being goods returned to Sam and input IGST debited at the time of purchases reversed)			
(vi)	Furniture A/c (WN 1)	Dr.	40,000	
	Input IGST A/c	Dr.	4,800	
	To Bank A/c			44,800
	(Being furniture purchased paid IGST @ 12%)			
(vii)	Machinery A/c	Dr.	1,40,000	
	Input CGST A/c (1,40,000 x 9%)	Dr.	12,600	
	Input SGST A/c (1,40,000 x 9%)	Dr.	12,600	
	To Bank A/c			1,00,000
	To Symphony Industries			65,200
	(Being machinery purchased and paid ₹ 1,00,000 immediately, CGST and SGST @ 9% each)			

\* The input tax availed earlier is reversed, because these goods are 'consumed' by Mr. Rohit himself. Since he cannot 'sell' goods to himself and charged output tax, the input tax thereon is reversed, since in this case Mr. Rohit himself is the ultimate consumer of those goods.

\*\* Since goods are returned to the supplier, the input tax credit availed earlier on those goods is to be reversed, since these goods are no longer available to be sold.

### Working Note.

1. Furniture purchased is including IGST @ 12%. So, value of furniture excluding IGST = ₹ 44,800 × 100/112 = ₹ 40,000. IGST = ₹ 40,000 × 12% = ₹ 4,800.

### ILLUSTRATION 9

Journalise the following transactions in the books of Ms. Nidhi traders

July, 2022

- 3 Sold Goods for ₹ 50,000, charged CGST and SGST @ 6% each.
- 4 Sold goods to Surjeet for ₹ 28,000 including CGST and SGST @ 6% each.
- 5 Received ₹ 25,200 from Surjeet in full settlement of his account of ₹ 28,000.
- 6 Sold goods to Kapil for ₹ 30,000 charged IGST @ 12%. Received ₹ 12,000 immediately and balance to be received after one month.
- 10 Kapil was allowed rebate of ₹ 5,000 as goods supplied to him were defective. These goods were sold by charging IGST @ 12%.
- 12 Sold goods to Manpreet for ₹ 1,00,000 at trade discount of 20% and charged IGST @ 12%
- 13 Goods of list price ₹ 20,000 returned by Manpreet.
- 17 Received commission of ₹ 15,000, charged CGST and SGST @ 6% each.

### SOLUTION

#### In the Books of Ms. Nidhi Journal

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
July, 2022				
3	Bank A/c To Sales A/c To Output CGST A/c To Output SGST A/c (Being goods sold for cash, charged CGST and SGST @ 6% each)	Dr.	56,000	50,000 3,000 3,000
4	Surjeet's A/c To Sales A/c	Dr.	28,000	25,000

	To Output CGST A/c			1,500
	To Output SGST A/c			1,500
	(Being goods sold to Surjeet, charged CGST and SGST @ 6% each )(refer W.N.)			
5	Bank A/c	Dr.	25,200	
	Discount Allowed A/c	Dr.	2,800	
	To Surjeet A/c			28,000
	(Being amount received from Surjeet in full settlement of ₹ 28,000 after allowing him discount of ₹ 2,800)			
6	Bank A/c	Dr.	12,000	
	Kapil's A/c	Dr.	21,600	
	To Sales A/c			30,000
	To Output IGST A/c			3,600
	(Being goods sold to Kapil, charged IGST @ 12% and received ₹ 12,000 in cash and balance receivable after one month)			
10	Rebate A/c *	Dr.	5,000	
	Output IGST A/c	Dr.	600	
	To Kapil's A/c			5,600
	(Being rebate allowed on goods sold to Kapil, Output IGST charged at the time of sales, now reversed)			
12	Manpreet's A/c	Dr.	89,600	
	To Sales A/c (1,00,000 x 80%)			80,000
	To Output IGST A/c (80,000 x 12%)			9,600
	(Being goods sold to Manpreet at trade discount of 20% and charged IGST @ 12%)			
13	Sales Return A/c	Dr.	16,000	
	Output IGST A/c	Dr.	1,920	
	To Manpreet A/c			17,920
	(Being goods returned by Manpreet and Output IGST charged at the time of sales now reversed)			

17	Cash A/c	Dr.		16,800	
	To Commission A/c				15,000
	To Output CGST A/c (15,000 x 6%)				900
	To Output SGST A/c (15,000 x 6%)				900
	(Being commission received charged CGST and SGST @ 6% each)				

\*Since rebate is on account of defective goods which cannot be sold/utilized further by Kapil, the output GST charged thereon is also reversed. This treatment is like that of Sales Return. If rebate was on account of other reasons (such as prompt payment), Output IGST would not be reversed.

### Working Note:

Goods sold to Surjeet is including CGST and SGST @ 6% each. So, sales excluding CGST and SGST = ₹ 28,000 × 100/112 = ₹ 25,000. CGST and SGST = ₹ 25,000 × 6% = ₹ 1,500 each.

### ILLUSTRATION 10

Record the following transactions in a Journal, assuming CGST and SGST@ 6% each.

- (i) Sold goods to Mukesh at the list price of ₹ 50,000 less 20% trade discount.
- (ii) Sold goods to Mukesh at the list price of ₹ 1,00,000 less 20% trade discount and 5% cash discount.
- (iii) Sold goods to Mukesh at the list price of ₹ 1,50,000 less 20% trade discount. Out of the amount due 60% is received out of which three-fourth is received by cheque.

### SOLUTION

#### Journal

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)	
(i)	Mukesh A/c	Dr.	44,800		
	To Sales A/c			40,000	
	To Output CGST A/c			2,400	
	To Output SGST A/c			2,400	
	(Being goods sold to Mukesh at a trade discount of 20% charged CGST and SGST @ 6% each)				

(ii)	Discount Allowed A/c	Dr.	4,000	
	Bank A/c		85,600	
	To Sales A/c			80,000
	To Output SGST A/c			4,800
	To Output SGST A/c			4,800
	(Being goods sold to Mukesh at a trade discount of 20% and 5% cash discount, charged CGST and SGST @ 6% each)*			
(iii)	Bank A/c	Dr.	60,480	
	Cash A/c	Dr.	20,160	
	Mukesh's A/c (refer W. N.)	Dr.	53,760	
	To Sales A/c (1,50,000 × 80%)			1,20,000
	To Output CGST A/c (1,20,000 × 6%)			7,200
	To Output SGST A/c (1,20,000 × 6%)			7,200
	(Being goods sold to Mukesh at a trade discount of 20% and received 60%, charged CGST and SGST @ 6% each)			

**\*Note :** After allowing cash discount of ₹ 4,000 ( ₹ 80,000 × 5%), the balance of ₹ 85,600 is received. Since discount is on account of prompt payment, output CGST and SGST is computed on value determine after deducting trade discount.

**Working Note:** After allowing trade discount of ₹ 30,000 on ₹ 1,50,000 = ₹ 1,20,000, 60% of the balance amount i.e. ₹ 1,34,400 (₹ 1,20,000 + 12% GST ₹ 14,400) is paid in cash and by cheque.

Hence, the amount paid in cash and cheque = ₹ 1,34,400 × 60% = ₹ 80,640.

Amount paid by cheque = ₹ 80,640 × 3/4 = ₹ 60,480

Amount paid in cash = ₹ 80,640 × 1/4 = ₹ 20,160

Mukesh's A/c = (₹ 1,20,000 + ₹ 14,400 – ₹ 60,480 – ₹ 20,160) = ₹ 53,760

## SUMMARY

- ◆ The accounting process starts with the recording of transactions in the form of journal entries.
- ◆ The recording is based on double entry system. This book or register called journal is the book of first or original entry.
- ◆ Next step is to post the entries in the ledger which is covered in the next unit.

## TEST YOUR KNOWLEDGE

### True and False

1. *In accounting equation approach, equity + Long-term liabilities = fixed asset + current assets – current liabilities.*
2. *In the traditional approach, for an entity a debtor will be receiver after sale of goods.*
3. *The rule of nominal account states that all expenses & losses are recorded on credit side.*
4. *Journal proper is also called a subsidiary book.*
5. *Capital account has a debit balance.*
6. *Purchase account is a nominal account.*
7. *All the personal & real account are recorded in P&L A/c.*
8. *Asset side of balance sheet contains all the personal & nominal accounts.*
9. *Capital account is a personal account.*
10. *Journal is also known as the book of original entry.*

### Multiple Choice Question

1. *The rent paid to landlord is credited to*
  - (a) *Landlord's account.*
  - (b) *Rent account.*
  - (c) *Cash account.*
2. *In case of a debt becoming bad, the amount should be credited to*
  - (a) *Trade receivables account.*

- (b) *Bad debts account.*
- (c) *Cash account.*
3. *A Ltd. has a ₹ 35,000 account receivable from Mohan. On January, 22, Mohan makes a partial payment of ₹ 21,000 to A Ltd. The journal entry made on January, 22 by A Ltd. to record this transaction includes:*
- (a) *A credit to the cash received account of ₹ 21,000.*
- (b) *A credit to the Accounts receivable account of ₹ 21,000.*
- (c) *A debit to the cash account of ₹ 14,000.*
4. *Which financial statement represents the accounting equation -*  
*Assets = Liabilities + Owner's equity:*
- (a) *Income Statement*
- (b) *Statement of Cash flows*
- (c) *Balance Sheet.*
5. *Which account is the odd one out?*
- (a) *Office furniture & Equipment.*
- (b) *Freehold land and Buildings.*
- (c) *Inventory of materials.*
6. *The debts written off as bad, if recovered subsequently are*
- (a) *Credited to Bad Debts Recovered Account*
- (b) *Credited to Trade Receivables Account.*
- (c) *Debited to Profit and Loss Account.*
7. *In Double Entry System of Book-keeping every business transaction affects:*
- (a) *Two accounts*
- (b) *Two sides of the same account.*
- (c) *The same account on two different dates.*
8. *A sale of goods to Ram for cash should be debited to:*
- (a) *Ram*
- (b) *Cash*
- (c) *Sales*

### Theory Questions

1. Write short note on classification of accounts.
2. Distinguish between Real account and nominal account.

### Practical Questions

1. Show the classification of the following Accounts under traditional and accounting equation approach:

a	Rent outstanding	g	Capital
b	Closing Inventory	h	Sales Tax Payable
c	Sales	i	Trade receivables
d	Bank Fixed Deposit	j	Depreciation
e	Cash	k	Drawings
f	Bad Debts		

2. Pass Journal Entries for the following transactions in the books of Gamma Bros.

- (i) Employees had taken inventory worth ₹ 1,00,000 (Cost price ₹ 75,000) on the eve of Deepawali and the same was deducted from their salaries in the subsequent month.
- (ii) Wages paid for erection of Machinery ₹ 18,000.
- (iii) Income tax liability of proprietor ₹ 17000 was paid out of petty cash.
- (iv) Purchase of goods from Naveen of the list price of ₹ 2,00,000. He allowed 10% trade discount, ₹ 5,000 cash discount was also allowed for quick payment.

3. Calculate the missing amount for the following.

	Assets	Liabilities	Capital
(a)	15,00,000	2,50,000	?
(b)	?	1,50,000	75,000
(c)	14,50,000	?	13,75,000
(d)	57,00,000	- 2,80,000	?

4. Show the effect of increase = (+), decrease = (-) and no change=(0) on the assets of the following transactions:

- a. Purchased office furniture, payment to be made next month.

- b. Collected cash for repair services
- c. Goods sold on credit.
- d. Withdrawal of cash by the owner for personal use.
- e. Hired an employee as sales manager of the north wing.
- f. Returned goods worth ₹ 50,000.
- g. One of our debtor agreed to pay his dues to Mr. C who is a creditor of the company with the same amount being due to him.
- h. Entered into an agreement with Mehta & Co. to purchase all raw materials from their company from next year.

Also give reasons for your answers.

5. Following is the information provided by Mr. Gopi pertaining to year ended 31st March 2022. Find the unknowns, showing computation to support your answer:

<b>Particulars</b>	<b>₹</b>	<b>Particulars</b>	<b>₹</b>
Machinery	12,00,000	Trade Receivables	B
Accounts Payable	1,00,000	Loans	C
Inventory	60,000	Closing Capital	D
Total Liabilities including capital	14,15,000	Opening Capital	10,00,000
Cash	A	Loss incurred during the year	35,000
Bank	80,000	Capital Introduced during the year	1,00,000

Additional Information: During the year sales of ₹ 15,55,000 was made of which ₹ 15,00,000 have been received.

5. Pass journal entries for the following transactions in the books of Mr. Manish:
  - (i) Purchased goods from Sonu for ₹ 3,00,000 at a trade discount of 10% plus CGST and SGST @ 6% each.
  - (ii) Sold goods to Mohit for ₹ 1,00,000 and charged CGST and SGST @ 5% each. Out of the amount due 40% is received by cheque immediately.
  - (iii) Goods costing ₹ 25,000 withdrawn for personal use. Such Goods were purchased by paying CGST and SGST @ 6% each.

(iv) Machinery purchased from M/s Bright Industries for ₹ 2,00,000 plus CGST and SGST @ 9% each. Paid ₹ 1,00,000 immediately by cheque and balance to be paid after two months.

## ANSWERS/HINTS

### True and False

1. True: As per the modern accounting equation approach- it is the basic formula in the accounting process
2. False: In the traditional approach, a debtor will be giver since he will be paying money for the sale of goods by the entity.
3. False: The rule of nominal account states that all expenses & losses are recorded on debit side.
4. True: It is one of the book where in the transactions not entered in the other books are entered in this book.
5. False: Capital account has a credit balance.
6. True: As it is considered as an expense.
7. False: All the personal & real account are recorded in balance sheet.
8. False: Asset side of balance sheet contains all the personal & real accounts.
9. True: As it is in the name of the proprietor who is bringing in the capital to the business.
10. True: As the transactions are entered first in this book as a first hand record.

### Multiple Choice Questions

1.	(c)	2.	(a)	3.	(b)	4.	(c)	5.	(c)	6.	(a)
7.	(a)	8.	(b)								

### Theoretical Questions

1. a. Accounts are broadly classified into assets, liabilities and capital. The basic accounting equation specifies broad categories, which are as follows:
  - (i) **Assets:** These are resources controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise, namely cash, stock of goods, land, buildings, machinery etc.

- (ii) **Liabilities:** These are financial obligations of an enterprise other than owner's equity namely long term loans, creditors, outstanding expenses etc.
- (iii) **Capital:** It generally refer to the amounts invested in an enterprise by its owner(s), the accretion to it or a reduction in it. Since capital is affected by expenses and incomes of revenue nature, there are two more categories of accounts, namely expenses and incomes. The difference between incomes and expenses are taken into capital account.
  - **Expenses:** These represents those accounts which show the amount spent or even lost in carrying on operations.
  - **Incomes:** These represent those accounts which show the revenue amounts earned by the enterprise.

However, traditionally accounts are classified as follows:

- (i) **Personal Accounts:** These accounts relate to persons, institutions, debtors or creditors.
  - (ii) **Impersonal Accounts:** These represent accounts which are not personal. These can be further sub-divided as follows:
    - **Real Accounts:** These accounts relate to assets of the firm but not debt e.g. accounts relating to land, buildings, cash in hand etc.
    - **Nominal accounts:** These accounts relate to expenses, losses, gains, revenues etc.
2. A real account is an account relating to properties and assets, other than personal accounts of the firm. Examples are land, buildings, machinery, cash, investments etc. Nominal accounts relate to expenses or losses, incomes and gains. Examples are: wages, salaries, rent, depreciation etc. The net result of all the nominal accounts is reflected as profit or loss which is transferred to the capital account. Nominal accounts are therefore, temporary. The real accounts are shown in the balance sheet along with personal accounts.

## Practical Problems

### 1. Nature of Account

Sl. No.	Title of Account	Traditional Approach	Accounting Equation Approach
a	Rent Outstanding	Personal	Liability
b	Closing Inventory	Real	Asset
c	Sales	Nominal	Revenue
d	Bank Fixed Deposit	Personal	Asset
e	Cash	Real	Asset
f	Bad Debts	Nominal	Expense
g	Capital	Personal	Capital
h	Sales Tax Payable	Personal	Liability
i	Trade receivables	Personal	Asset
j	Depreciation	Nominal	Expense
k	Drawings	Personal	Capital -Drawings

### 2. Journal Entries in the books of Gamma Bros.

	Particulars		Dr. Amount ₹	Cr. Amount ₹
(i)	Salaries A/c To Purchase A/c (Being entry made for inventory taken by employees)	Dr.	75,000	75,000
(ii)	Machinery A/c To Bank A/c (Being wages paid for erection of machinery)	Dr.	18,000	18,000
(iii)	Drawings A/c To Petty Cash A/c (Being the income tax of proprietor paid out of business money)	Dr.	17,000	17,000

(iv)	Purchase A/c To Naveen A/c (Being goods purchased from Naveen)	Dr.	1,80,000	1,80,000
	Naveen A/c To Bank To Discount Received A/c (Being amount paid for the goods purchased from Naveen for ₹ 2,00,000. 10% trade discount and cash discount of ₹ 5,000 allowed by him)	Dr.	1,80,000	1,75,000 5,000

**Note:**

- i. Here wages paid on erection of machinery have been capitalised therefore machinery account has been debited directly instead of wages being recorded as an expenditure.
  - ii. The students may also note that trade discount is allowed on the list price of goods. It is deducted to compute the invoice amount of the goods to be recorded in the books. Cash discount is a discount allowed in case of early payments to the seller. The entry is made in the books of accounts for cash discount.
3. (a) 12,50,000  
(b) 2,25,000  
(c) 75,000  
(d) 59,80,000

These have been solved using the Accounting Equation:

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

4.

S. No.	Increase (+) / Decrease (-) / No Change (0) in Assets	Reasons
(a)	+	Furniture has been purchased making it an increase in assets and also it being purchased on credit it increases liability and there is no outflow of assets like cash or bank.
(b)	+	Cash has flowed in for services provided making it an increase in assets.

(c)	+	For goods sold, it is a decrease in inventory (assets) but correspondingly there is an increase in debtors. However, there will be a net increase in assets because goods sold on profit. Though if goods are sold at cost; it will result in no change whereas if sold at below cost; it will result in decrease in assets.
(d)	-	Here cash has been withdrawn from business resulting in decrease in assets and capital.
(e)	0	Only hiring of employee has been done resulting in no change in assets.
(f)	-	Outflow of goods has resulted in decrease in assets while money owed to creditors reduce on the liability side.
(g)	-	Both assets and liabilities reduced by same amounts meaning a decrease in assets.
(h)	0	Only a purchase agreement has been entered into with no transaction taking place yet.

5. Trade Receivable Balance (B) = Sales- Amount received during the year  
= ₹ (15,55,000 – 15,00,000) = ₹ 55,000.

Since, we know Assets = Capital + Liabilities

Therefore, balance of assets is also ₹ 14,15,000

So, total assets:

Particulars	₹
Total Assets	14,15,000
Less: Machinery	(12,00,000)
Less: Inventory	(60,000)
Less: Bank	(80,000)
Less: Receivables	(55,000)
Cash (A)	20,000

#### Computation of Closing Capital (D):

Particulars	₹
Opening Capital	10,00,000
Add: Introduced during the year	1,00,000
Less: Loss incurred during the year	(35,000)
Closing Capital	10,65,000

So, Loan amount (C) = Total Liabilities and capital - Closing Capital - Trade Payables  
 = ₹ (14,15,000 - 10,65,000 - 1,00,000) = ₹ 2,50,000

5. **Journal entries in the books of Mr. Manish**

S No.	Particulars	L.F.	Amount Dr. (₹)	Amount Cr. (₹)
(i)	Purchases A/c Dr. Input CGST A/c Dr. Input SGST A/c Dr. To Sonu's A/c (Being goods purchased from Sonu, CGST and SGST payable @ 6% each)		2,70,000 16,200 16,200	3,02,400
(ii)	Bank A/c Dr. Mohit's A/c Dr. To Sales A/c To Output CGST A/c To Output SGST A/c (Being goods sold to Mohit, charged CGST and SGST @ 5% each and received 40% in cash)		44,000 66,000	1,00,000 5,000 5,000
(iii)	Drawings A/c Dr. To Purchase A/c To Input CGST A/c To Input SGST A/c (Being goods withdrawn for personal use and input CGST and input SGST debited at the time of purchase reversed)		28,000	25,000 1,500 1,500
(iv)	Machinery A/c Dr. Input CGST A/c Dr. Input SGST A/c Dr. To Bank A/c To Bright Industries (Being machinery purchased and paid ₹ 1,00,000 immediately, CGST and SGST @ 9% each)		2,00,000 18,000 18,000	1,00,000 1,36,000

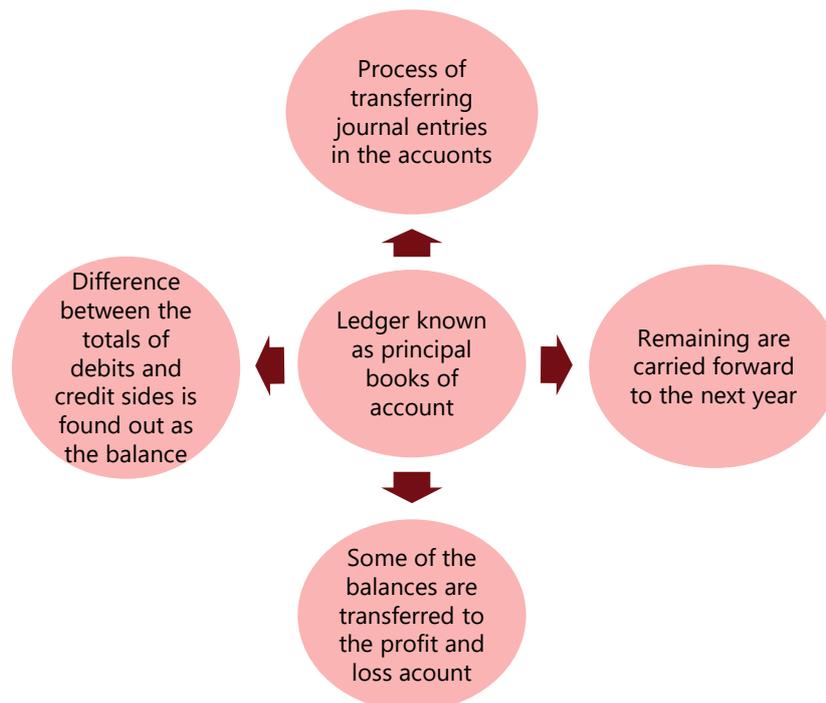
## UNIT 2 : LEDGERS

### LEARNING OUTCOMES

After studying this unit, you will be able to:

- ◆ Understand the concept of Ledgers.
- ◆ Learn the technique of ledger posting and how to balance an account.
- ◆ Learn the technique of opening accounts each year taking closing balances of the previous year. Note also the use of term 'balance c/d' and 'balance b/d'

### UNIT OVERVIEW





## 2.1 INTRODUCTION

After recording the original transactions in the journal, recorded entries are classified and grouped into by preparation of accounts. The book which contains all set of accounts (viz. personal, real and nominal accounts), is known as Ledger. It is known as principal books of account in which account-wise balance of each account is determined.



## 2.2 SPECIMEN OF LEDGER ACCOUNTS

A ledger account has two sides-debit (left side of the account) and credit (right side of the account). Each of the debit and credit side has four columns. (i) Date (ii) Particulars (iii) Journal folio i.e. page from where the entries are taken for posting and (iv) Amount.

Dr.				Account				Cr.			
Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)



## 2.3 POSTING

The process of transferring the debit and credit items from journal to classified accounts in the ledger is known as posting.

### 2.3.1 Rules regarding Posting of Entries in the Ledger

1. Separate account is opened in ledger book for each distinct account and entries from Journal are posted to respective account accordingly.
2. It is a practice to use words 'To' and 'By' while posting transactions in the ledger. The word 'To' is used in the particular column with the accounts written on the debit side while 'By' is used with the accounts written in the particular column of the credit side. These 'To' and 'By' do not have any meanings but are used to the account debited and credited.
3. The concerned account debited in the journal should also be debited in the ledger but reference should be of the respective credit account.

## 2.4 BALANCING AN ACCOUNT

At the end of each month or year or any particular reporting period, it may be necessary to ascertain the balance in an account. Suppose a person has bought goods worth ₹1,000 and has paid only ₹ 850; he owes ₹150 and that is the balance in his account. To ascertain the balance in any account, both the sides of the account is totalled and smaller amount is deducted from the bigger amount to ascertain the difference. If the credit side is bigger than the debit side, it is a credit balance and vice a versa. The credit balance is written on the debit side as, "To Balance c/d"; c/d means "carried down". By doing this, two sides will be equal. The totals are written on the two sides opposite one another.

Then the credit balance is written on the credit side as "By balance b/d (i.e., brought down)". This is the opening balance for the new period. The debit balance similarly is written on the credit side as "By Balance c/d", the totals then are written on the two sides as shown above and then the debit balance written on the debit side as, "To Balance b/d", as the opening balance of the new period.

It should be noted that nominal accounts are not balanced; the balance in the end are transferred to the profit and loss account. Only personal and real accounts balances are ultimately shown in the balance sheet at the end of the accounting period. The capital account is adjusted for profit or loss (i.e net of nominal accounts) at the end of accounting period.

### ILLUSTRATION 1

Prepare the Stationery Account of a firm for the month of Jan. 2022 duly balanced off, from the following details:

2022		₹
Jan. 1	Inventory of stationery	480
Jan. 5	Purchase of stationery by cheque	800
Jan. 15	Purchase of stationery on credit from Five Star Stationery Mart	1,280

### SOLUTION

Dr.		Stationery Account		Cr.	
Date	Particulars	₹	Date	Particulars	₹
1.1.2022	To Balance b/d	480	31.1.2022	By Balance c/d	2,560
5.1.2022	To Bank A/c	800			
15.1.2022	To Five Star Stationery				

	Mart A/c	1,280			
		2,560			2,560
1.2.2022	To Balance b/d	2,560			

**ILLUSTRATION 2**

Prepare the ledger accounts on the basis of following transactions in the books of a trader.

Debit Balances on January 1, 2022:

Cash in Hand ₹ 8,000, Cash at Bank ₹ 25,000, inventory of Goods ₹ 20,000, Building ₹ 10,000.  
Trade receivables: Vijay ₹ 2,000 and Madhu ₹ 2,000.

Credit Balances on January 1, 2022:

Trade payables: Anand ₹ 5,000 and Kapil ₹ 7,000, Capital ₹ 55,000

Following were further transactions in the month of January, 2022:

Jan. 1 Purchased goods worth ₹ 5,000 (payable at later date) for cash less 20% trade discount and 5% cash discount.

Jan. 4 Received ₹ 1,980 from Vijay and allowed him ₹ 20 as discount.

Jan. 8 Purchased plant from Mukesh for ₹5,000 and paid ₹100 as cartage for bringing the plant to the factory and another ₹200 as installation charges.

Jan. 12 Sold goods to Rahim on credit ₹600.

Jan. 15 Rahim became insolvent and could pay only 50 paise in a rupee.

Jan. 18 Sold goods to Ram for cash ₹1,000.

**SOLUTION**

Dr.				Cr.			
<b>Cash Account</b>							
Date 2022	Particulars	J.F.	₹	Date 2022	Particulars	J.F.	₹
Jan. 1	To Balance b/d		8,000	Jan. 1	By Purchases A/c		3,800
Jan. 4	To Vijay		1,980	Jan. 8	By Plant A/c		300
Jan. 15	To Rahim		300	Jan. 31	By Balance c/d		7,180
Jan. 18	To Sales A/c		1,000				
			11,280				11,280
Feb. 1	To Balance b/d		7,180				

Dr. **Bank Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 1	To Balance b/d		25,000	Jan. 31	By Balance c/d		25,000
			25,000				25,000
Feb. 1	To Balance b/d		25,000				

Dr. **Inventory Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 1	To Balance b/d		20,000	Jan. 31	By Balance c/d		20,000
			20,000				20,000
Feb. 1	To Balance b/d		20,000				

Dr. **Building Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 1	To Balance b/d		10,000	Jan. 31	By Balance c/d		10,000
			10,000				10,000
Feb. 1	To Balance b/d		10,000				

Dr. **Vijay** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 1	To Balance b/d		2,000	Jan. 4	By Cash A/c		1,980
					By Discount A/c		20
			2,000				2,000

Dr. **Madhu** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 1	To Balance b/d		2,000	Jan. 31	By Balance c/d		2,000
			2,000				2,000
Feb. 1	To Balance b/d		2,000				

Dr. **Anand** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 31	To Balance c/d		5,000	Jan. 1	By Balance b/d		5,000
			5,000				5,000
				Feb. 1	By Balance b/d		5,000

Dr. **Kapil** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 31	To Balance c/d		7,000	Jan. 1	By Balance b/d		7,000
			7,000				7,000
				Feb. 1	By Balance b/d		7,000

Dr. **Capital Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 31	To Balance c/d		55,000	Jan. 1	By Balance b/d		55,000
			55,000				55,000
				Feb. 1	By Balance b/d		55,000

Dr. **Purchases Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 1	To Cash		3,800				
Jan. 1	To Cash Discount		200	Jan. 31	By Balance c/d		4,000
			4,000				4,000
Feb. 1	To Balance b/d		4,000				

Dr. **Discount Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 4	To Vijay		20	Jan. 1	By Purchases A/c		200
Jan.31	To Balance c/d		180				200
			200				200
				Feb. 1	By Balance b/d		180

Dr. **Plant Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 8	To Mukesh		5,000	Jan. 31	By Balance c/d		5,300
Jan. 8	To Cash A/c		300				5,300
			5,300				5,300
Feb. 1	To Balance b/d		5,300				

Dr. **Mukesh** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 31	To Balance c/d		5,000	Jan. 8	By Plant A/c		5,000
			5,000				5,000
				Feb. 1	By Balance b/d		5,000

Dr. **Sales Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 31	To Balance c/d		1,600	Jan. 12	By Rahim		600
			1,600	Jan. 18	By Cash A/c		1,000
				Feb. 1	By Balance b/d		1,600

Dr. **Rahim** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 12	To Sales A/c		600	Jan. 15	By Cash A/c		300
			600	Jan. 15	By Bad Debts A/c		300
							600

Dr. **Bad Debts Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Jan. 15	To Rahim		300	Jan. 31	By Balance c/d		300
			300				300
Feb. 1	To Balance b/d		300				

**ILLUSTRATION 3**

The following data is given by Mr. S, the owner, with a request to compile only the two personal accounts of Mr. H and Mr. R, in his ledger, for the month of April, 2022.

- 1 Mr. S owes Mr. R ₹ 15,000; Mr. H owes Mr. S ₹ 20,000.
- 4 Mr. R sold goods worth ₹ 60,000 @ 10% trade discount to Mr. S.
- 5 Mr. S sold to Mr. H goods prices at ₹ 30,000.

- 17 Record a purchase of ₹ 25,000 net from R, which were sold to H at a profit of ₹15,000.
- 18 Mr. S rejected 10% of Mr. R's goods of 4th April.
- 19 Mr. S issued a cash memo for ₹10,000 to Mr. H who came personally for this consignment of goods, urgently needed by him.
- 22 Mr. H cleared half his total dues to Mr. S, enjoying a ½% cash discount (of the payment received, ₹ 20,000 was by cheque).
- 26 R's total dues (less ₹10,000 held back) were cleared by cheque, enjoying a cash discount of ₹1,000 on the payment made.
- 29 Close H's Account to record the fact that all except ₹ 5,000 was cleared by him, by a cheque, because he was declared bankrupt.
- 30 Balance R's Account.

**SOLUTION****In the books of Mr. S**

Dr.			Cr.		
<b>Mr. H Account</b>					
Date	Particulars	₹	Date	Particulars	₹
1.4.2022	To Balance b/d	20,000	22.4.2022	By Bank A/c	20,000
5.4.2022	To Sales A/c	30,000	22.4.2022	By Cash A/c (Note 2)	24,775
17.4.2022	To Sales A/c	40,000	29.4.2022	By Discount Allowed A/c	225
			29.4.2022	By Bank A/c	40,000
			29.4.2022	By Bad Debts A/c	5,000
		90,000			90,000

Dr.			Cr.		
<b>Mr. R Account</b>					
Date	Particulars	₹	Date	Particulars	₹
18.4.2022	To Purchase Returns A/c	5,400	1.4.2022	By Balance b/d	15,000
			4.4.2022	By Purchases A/c	54,000
26.4.2022	To Bank A/c	77,600	17.4.2022	By Purchases A/c	25,000
26.4.2022	To Discount Received A/c	1,000			
30.4.2022	To Balance c/d	10,000			
		94,000			94,000
			1.5.2022	By Balance b/d	10,000

**Working Notes:**

- (1) Sale of ₹ 10,000 on 19th April is a cash sales, therefore, it will not be recorded in the Personal Account of Mr. H; and
- (2) On 22nd April, Mr. H owes Mr. S ₹ 90,000, amount paid by Mr. H  $\frac{1}{2}$  of ₹ 90,000 less  $\frac{1}{2}\%$  discount i.e., ₹ 45,000 – ₹ 225 = ₹ 44,775. Out of this amount, ₹ 20,000 paid by cheque and the balance of ₹ 24,775 in cash.

**Note:** The balance of all nominal accounts is transferred to Profit and Loss account at the time of preparation of financial statements as the nominal Accounts are in the nature of revenue/incomes/gains or expenses/losses. Thus, the net result of all nominal accounts is reflected in profit and loss Account for an accounting period which is transferred to Capital Account. The balance of all the accounts relating to assets and liabilities (personal and real) are reflected in the Balance Sheet at the end of accounting period.

**SUMMARY**

- ♦ Process of transferring journal entries in the accounts opened in Ledger is called posting.
- ♦ Ledger is known as principal books of accounts and it provides full information regarding all the financial transactions pertaining to any individual account.
- ♦ The difference between the totals of debits and credit sides is found out as the balance. Some of these balances (i.e nominal accounts) are transferred to the profit and loss account and some are carried forward to the next period/year i.e., shown in the balance sheet, depending upon the nature of the account.

**TEST YOUR KNOWLEDGE****True and False**

1. *A ledger is also known as the principal book of accounts.*
2. *Cash account has a debit balance.*
3. *Posting is the process of transferring the accounts from ledger to journal.*
4. *At the end of the accounting year, all the nominal accounts of the ledger book are balanced.*
5. *Ledger records the transactions in a chronological order.*

6. *If the total debit side is greater than the total of credit side, we get a credit balance as opening balance.*
7. *Ledger accounts of assets will always be debited when they are increased.*

### **Multiple Choice Questions**

1. *The process of transferring the debit and credit items from a Journal to their respective accounts in the ledger is termed as*
  - (a) *Posting*
  - (b) *Purchase*
  - (c) *Balancing of an account*
2. *The technique of finding the net balance of an account after considering the totals of both debits and credits appearing in the account is known as*
  - (a) *Posting*
  - (b) *Purchase*
  - (c) *Balancing of an account*
3. *Journal and ledger records transactions in*
  - (a) *A chronological order and analytical order respectively.*
  - (b) *An analytical order and chronological order respectively.*
  - (c) *A chronological order only*
4. *Ledger book is popularly known as*
  - (a) *Secondary book of accounts*
  - (b) *Principal book of accounts*
  - (c) *Subsidiary book of accounts*
5. *At the end of the accounting year all the nominal accounts of the ledger book are*
  - (a) *Balanced but not transferred to profit and loss account*
  - (b) *Not balanced and also the balance is not transferred to the profit and loss account*
  - (c) *Not balanced and their balance is transferred to the profit and loss account.*

## Theory Questions

1. What do you mean by principal books of accounts?
2. What are the rules of posting of journal entries into the Ledger?

## Practical Questions

1. Journalize the following transactions, post them in the Ledger and balance the accounts on 31<sup>st</sup> December.
  1. X started business with a capital of ₹ 20,000
  2. He purchased goods from Y on credit ₹ 4,000
  3. He paid cash to Y ₹ 2,000
  4. He sold goods to Z ₹ 4,000
  5. He received cash from Z ₹ 6,000
  6. He further purchased goods from Y ₹ 4,000
  7. He paid cash to Y ₹ 2,000
  8. He further sold goods to Z ₹ 4,000
  9. He received cash form Z ₹ 2,000

## ANSWERS/HINTS

### True and False

1. True: Since it classifies all the amounts related to a particular account and then it is used as the base for preparing the Trial balance, a ledger is also known as principal books of accounts.
2. True: Being an asset under the modern equation approach, cash account has a debit balance.
3. False: Posting is the process of transferring the balances from journal to ledger.
4. False: At the end of the accounting year, all the nominal accounts of the ledger book are totaled and transferred to P&L A/c.
5. False: Ledger records the transactions in analytical order. But journal records the transactions in a chronological order.

6. *False: If the total of debit side is greater than the total of credit side, we get a debit balance as the opening balance.*
7. *True: The increase to an asset shall be debited since the original balance is also debit.*

### Multiple Choice Questions

1.	(a)	2.	(c)	3.	(a)	4.	(b)	5.	(c)		
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### Theoretical Questions

1. *Ledger is known as principal books of accounts and it provides full information regarding all the transactions pertaining to any individual account. Ledger contains all set of accounts (viz. personal, real and nominal accounts).*
2. *Rules regarding posting of entries in the ledger:*
- Separate account is opened in ledger book for each account and entries from the Journal are posted to respective accounts accordingly.*
  - It is a practice to use words 'To' and 'By' while posting transactions in the ledger. The word 'To' is used in the particular column with the accounts written on the debit side while 'By' is used with the accounts written in the particular column of the credit side. These 'To' and 'By' do not have any meanings but are used to the account debited and credited.*
  - The concerned account debited in the journal should also be debited in the ledger but reference should be of the respective credit account.*

### Practical Questions

1. **Journal**

Particulars	L.F.	Debit ₹	Credit ₹
Cash A/c To Capital A/c (Being commencement of business)	Dr.	20,000	20,000
Purchase A/c To Y (Being purchase of goods on credit)	Dr.	4,000	4,000
Y To Cash (Being amount paid to Y)	Dr.	2,000	2,000

Z To Sales A/c (Being goods sold to Z)	Dr.		4,000	4,000
Bank A/c To Z (Being amount received from Z)	Dr.		6,000	6,000
Purchase A/c To Y (Being purchase of goods on credit from Y)	Dr.		4,000	4,000
Y To Cash A/c (Being amount paid to Y)	Dr.		2,000	2,000
Z To Sales A/c (Being goods sold to Z)	Dr.		4,000	4,000
Cash A/c To Z (Being cash received from Z)	Dr.		2,000	2,000
<b>TOTAL</b>			<b>48,000</b>	<b>48,000</b>

Dr.

**Cash Account**

Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Capital A/c	20,000		By Y	2,000
	To Z	6,000		By Y	2,000
	To Z	2000		By Balance c/d	24,000
		28,000			28,000
Feb. 1	To Balance b/d	24,000			

Dr.

**Capital Account**

Cr.

Date	Particulars	₹	Date	Particulars	₹
Jan. 31	To Balance c/d	20,000		By Cash A/c	20,000
		20,000			20,000
			Feb. 1	By Balance b/d	20,000

Dr. **Purchase Account** Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Y	4,000	Jan 31.	By Balance c/d	8,000
	To Y	4,000			
		8,000			8,000
Feb.1	To Balance b/d	8,000			

Dr. **Y's Account** Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Cash	2,000		By Purchases	4,000
	To Cash	2,000		By Purchases	4,000
Jan. 31	To Balance c/d	4,000			
		8,000			8,000
				By Balance b/d	4,000

Dr. **Z's Account** Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Sales	4,000		By Cash A/c	6,000
	To Sales	4,000		By Cash A/c	2,000
		8,000			8,000

Dr. **Sales Account** Cr.

Date	Particulars	₹	Date	Particulars	₹
Jan. 31	To Balance c/d	8,000		By Z	4,000
				By Z	4,000
		8,000			8,000
			Feb. 1	By Balance b/d	8,000

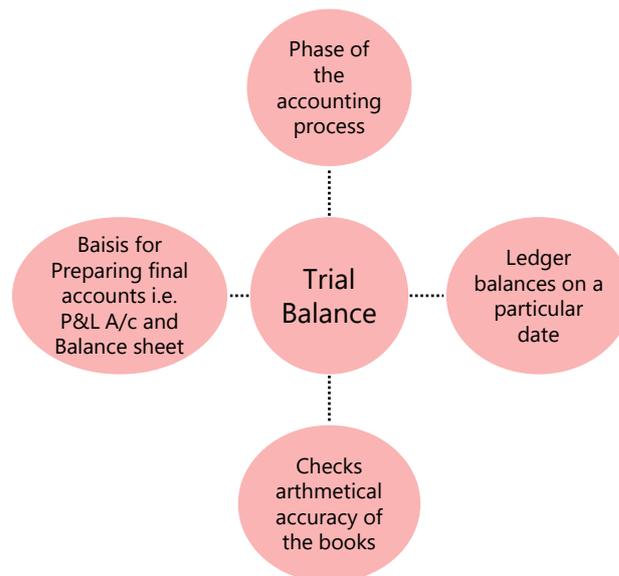
## UNIT 3 : TRIAL BALANCE

### LEARNING OUTCOMES

After studying this unit, you will be able to:

- ◆ Learn the technique of taking balances from ledger accounts to prepare trial balance.
- ◆ Understand what is trial balance and what purposes it can serve..

### UNIT OVERVIEW



Trial balance contains various ledger balances on a particular date. It forms the basis for preparing the financial statement i.e. profit and loss account and balance sheet. If it tallies, it means that the accounts are arithmetically accurate but certain errors may still remain undetected. Therefore, it is very important to carefully journalise and post the entries, following the rules of accounting.



### 3.1 INTRODUCTION

Preparation of trial balance is the third phase in the accounting process. After posting the accounts in the ledger, a statement is prepared to show separately the debit and credit balances. Such a statement is known as the trial balance. It may also be prepared by listing each and every account and entering in separate columns the totals of the debit and credit sides. Whichever way it is prepared, the totals of the two columns should agree. An agreement indicates arithmetic accuracy of the accounting work; if the two sides do not agree, then there is simply an arithmetic error(s).

This follows from the fact that under the Double Entry System, the amount written on the debit sides of various accounts is always equal to the amounts entered on the credit sides of other accounts and vice versa. Hence the totals of the debit sides must be equal to the totals of the credit sides. Also total of the debit balances will be equal to the total of the credit balances. Once this agreement is established, there is reasonable confidence that the accounting work is free from clerical errors, though it is not a proof of cent per cent accuracy, because some errors of principle and compensating errors may still remain. Generally, to check the arithmetic accuracy of accounts, trial balance is prepared at monthly intervals. But because double entry system is followed, one can prepare a trial balance any time. Though a trial balance can be prepared any time but it is preferable to prepare it at the end of the reporting period which may be month end/quarter end/year end to ensure the arithmetic accuracy of all the accounts before the preparation of the financial statements. It may be noted that trial balance is a statement and not an account.



### 3.2. OBJECTIVES OF PREPARING THE TRIAL BALANCE

The preparation of trial balance has the following objectives:

- (i) Trial balance enables one to establish whether the posting and other accounting processes have been carried out without committing arithmetical errors. In other words, the trial balance helps to establish arithmetical accuracy of the books of accounts.
- (ii) Financial statements are normally prepared on the basis of agreed trial balance; otherwise the financial statements will not give true and fair picture of the financial transactions.
- (iii) The trial balance serves as a summary of what is contained in the ledger; the ledger may have to be seen only when details are required in respect of an account.

The form of the trial balance is simple as shown below:

### Trial Balance

as at.....

S.No	Ledger Accounts	Dr. Amount	Cr. Amount
		(Total or Balance)	(Total or Balance)
		₹	₹

The under mentioned points may be noted:

- (i) A trial balance is prepared as on a particular date which should be mentioned at the top.
- (ii) In the second column the name of the account is written.
- (iii) In the third column the total of the debit side of the account concerned or the debit balance, if any is entered.
- (iv) In the fourth column, the total of the credit side or the credit balance is written.
- (v) The third and fourth columns are totalled at the end.



### 3.3 LIMITATIONS OF TRIAL BALANCE

One should note that the agreement of Trial Balance is not a conclusive proof of accuracy. In other words, in spite of the agreement of the trial balance some errors may remain. These may be of the following types:

- (i) Transaction has not been entered at all in the journal.
- (ii) A wrong amount has been written in both columns of the journal.
- (iii) A wrong account has been mentioned in the journal.
- (iv) An entry has not at all been posted in the ledger.
- (v) Entry is posted twice in the ledger.

Still, the preparation of the trial balance is very useful; without it, the preparation of financial statements, would be difficult.



### 3.4 METHODS OF PREPARATION OF TRIAL BALANCE

#### 1. TOTAL METHOD

Under this method, every ledger account is totalled and that total amount (both of debit side and credit side) is transferred to trial balance. In this method, trial balance can be prepared as soon as ledger account is totalled. Time taken to balance the ledger accounts is saved under this method as balance can be found out in the trial balance itself. The difference of totals of each ledger account is the balance of that particular account. This method is not commonly used as for the preparation of the financial statements, only net balance of the ledger account is required. Therefore, the trial balance compiled under this method cannot be used directly for preparation of the financial statements.

#### ILLUSTRATION 1

Given below is a ledger extract relating to the business of X and Co. as on March, 31, 2022. You are required to prepare the Trial Balance by the Total Amount Method.

Dr. **Cash Account** Cr.

Particulars	₹	Particulars	₹
To Capital A/c	10,000	By Furniture A/c	3,000
To Ram's A/c	25,000	By Salaries A/c	2,500
To Cash Sales	500	By Shyam's A/c	21,000
		By Cash Purchases	1,000
		By Capital A/c	500
		By Balance c/d	7,500
	35,500		35,500

Dr. **Furniture Account** Cr.

Particulars	₹	Particulars	₹
To Cash A/c	3,000	By Balance c/d	3,000
	3,000		3,000

Dr. **Salaries Account** Cr.

Particulars	₹	Particulars	₹
To Cash A/c	2,500	By Balance c/d	2,500
	2,500		2,500

Dr. **Shyam's Account** Cr.

Particulars	₹	Particulars	₹
To Cash A/c	21,000	By Purchases A/c	25,000
To Purchase Returns A/c	500	(Credit Purchase)	
To Balance c/d	3,500		–
	25,000		25,000

Dr. **Purchases Account** Cr.

Particulars	₹	Particulars	₹
To Cash A/c (Cash Purchases)	1,000	By Balance c/d	26,000
To Sundries as per Purchases Book (Credit Purchases)	25,000		–
	26,000		26,000

Dr. **Purchases Returns Account** Cr.

Particulars	₹	Particulars	₹
To Balance c/d	500	By Sundries as per Purchases Return Book	500
	500		500

Dr. **Ram's Account** Cr.

Particulars	₹	Particulars	₹
To Sales A/c (Credit Sales)	30,000	By Sales Returns A/c	100
		By Cash A/c	25,000
		By Balance c/d	4,900
	30,000		30,000

Dr. **Sales Account** Cr.

Particulars	₹	Particulars	₹
To Balance c/d	30,500	By Cash A/c (Cash Sales)	500
		By Sundries as per Sales Book (Credit Sales)	30,000
	30,500		30,500

Dr. **Sales Returns Account** Cr.

Particulars	₹	Particulars	₹
To Sundries as per Sales Returns Book	100	By Balance c/d	100
	100		100

Dr. **Capital Account** Cr.

Particulars	₹	Particulars	₹
To Cash A/c	500	By Cash A/c	10,000
To Balance c/d	9,500		
	10,000		10,000

### SOLUTION

#### Trial Balance of X and Co. as at 31.03.2022

Sl. No.	Name of Account	Total Debit ₹	Total Credit ₹
1.	Cash A/c	35,500	28,000
2.	Furniture A/c	3,000	
3.	Salaries A/c	2,500	
4.	Shyam's A/c	21,500	25,000
5.	Purchases A/c	26,000	
6.	Purchases Returns A/c		500
7.	Ram's A/c	30,000	25,100
8.	Sales A/c		30,500
9.	Sales Returns A/c	100	
10.	Capital A/c	500	10,000
		1,19,100	1,19,100

## 2. BALANCE METHOD

Under this method, every ledger account is balanced and those balances only are carried forward to the trial balance. This method is used commonly by the accountants and helps in the preparation of the financial statements. Financial statements are prepared on the basis of the balances of the ledger accounts.

**ILLUSTRATION 2**

Taking the same information as given in Illustration 1, prepare the Trial Balance by Balance Method.

**SOLUTION****Trial Balance of X and Co. as at 31.03.2022**

Sl. No.	Name of Account	Debit Balance ₹	Credit Balance ₹
1.	Cash A/c	7,500	
2.	Furniture A/c	3,000	
3.	Salaries A/c	2,500	
4.	Shyam's A/c		3,500
5.	Purchases A/c	26,000	
6.	Purchases Returns A/c		500
7.	Ram's A/c	4,900	
8.	Sales A/c		30,500
9.	Sales Returns A/c	100	
10.	Capital A/c		9,500
		44,000	44,000

**3. TOTAL AND BALANCE METHOD**

Under this method, the above two explained methods are combined. This has been explained with the help of the following example:

**Trial Balance of X as at 31.03.2022**

Sl. No.	Heads of Account	Debit Balance (₹)	Credit Balance (₹)	Debit Total (₹)	Credit Total (₹)
1.	Cash Account	7,500		35,500	28,000
2.	Furniture Account	3,000		3,000	
3.	Salaries Account	2,500		2,500	
4.	Shyam's Account		3,500	21,500	25,000

5.	Purchases Account	26,000		26,000	
6.	Purchase Returns Account		500		500
7.	Ram's Account	4,900		30,000	25,100
8.	Sales Account		30,500		30,500
9.	Sale Returns Account	100		100	
10.	Capital Account		9,500	500	10,000
	Total	44,000	44,000	1,19,100	1,19,100

### 3.5 ADJUSTED TRIAL BALANCE (THROUGH SUSPENSE ACCOUNT)

If the trial balance does not agree after transferring the balance of all ledger accounts including cash and bank balance and also errors are not located timely, then the trial balance is tallied by transferring the difference of debit and credit side to an account known as suspense account. This is a temporary account opened to proceed further and to prepare the financial statements timely.

### 3.6 RULES OF PREPARING THE TRIAL BALANCE

While preparing the trial balance from the given list of ledger balances, following rules should be taken into account:

1. The balances of all (i) assets accounts (ii) expenses accounts (iii) losses (iv) drawings are placed in the debit column of the trial balance.
2. The balances of all (i) liabilities accounts (ii) income accounts (iii) gains (iv) capital are placed in the credit column of the trial balance.

#### ILLUSTRATION 3

From the following ledger balances, prepare a trial balance of Anuradha Traders as on 31st March, 2022:

Account Head	₹
Capital	1,00,000
Sales	1,66,000
Purchases	1,50,000

<i>Sales return</i>	1,000
<i>Discount allowed</i>	2,000
<i>Expenses</i>	10,000
<i>Trade receivables</i>	75,000
<i>Trade payables</i>	25,000
<i>Investments</i>	15,000
<i>Cash at bank and in hand</i>	37,000
<i>Interest received on investments</i>	1,500
<i>Insurance paid</i>	2,500

**SOLUTION****Trial Balance of Anuradha Traders as on 31.03.2022**

<b>Particulars</b>	<b>Dr. balance ₹</b>	<b>Particulars</b>	<b>Cr. balance ₹</b>
Purchases	1,50,000	Capital	1,00,000
Sales return	1,000	Sales	1,66,000
Discount allowed	2,000	Trade payables	25,000
Expenses	10,000	Interest received on investments	1,500
Trade receivables	75,000		
Investments	15,000		
Cash at bank and in hand	37,000		
Insurance paid	2,500		
<b>Total</b>	<b>2,92,500</b>		<b>2,92,500</b>

**ILLUSTRATION 4**

One of your clients, Mr. Singhania has asked you to finalise his accounts for the year ended 31st March, 2022. Till date, he himself has recorded the transactions in books of accounts. As a basis for audit, Mr. Singhania furnished you with the following statement.

	Dr. Balance (₹)	Cr. Balance (₹)
Singhanian's Capital		1,556
Singhanian's Drawings	564	
Leasehold premises	750	
Sales		2,750
Dues from customers		530
Purchases	1,259	
Purchases return	264	
Loan from bank		256
Trade payables	528	
Trade expenses	700	
Cash at bank	226	
Bills payable	100	
Salaries and wages	600	
Inventories (1.4.2021)		264
Rent and rates	463	
Sales return	—	<u>98</u>
	5,454	5,454

The closing inventory on 31st March, 2022 was valued at ₹ 574. Mr. Singhanian claims that he has recorded every transaction correctly as the trial balance is tallied. Check the accuracy of the above trial balance.

### SOLUTION

#### Corrected Trial Balance of Mr. Singhanian as on 31st March, 2022

Particulars	Dr. Amount ₹	Cr. Amount ₹
Singhanian's Capital		1,556
Singhanian's Drawings	564	
Leasehold premises	750	
Sales		2,750

Dues from customers (refer note 1 below)	530	
Purchases	1,259	
Purchases returns (refer note 2 below)		264
Loan from Bank		256
Trade payables (refer note 3 below)		528
Trade expenses	700	
Cash at Bank	226	
Bills payable (refer note 4 below)		100
Salaries and Wages	600	
Inventory (1.4.2021) (refer note 5 below)	264	
Rent and rates	463	
Sales return (refer note 6 below)	98	
	5,454	5,454

**Notes:**

1. Dues from customers is an asset, so its balance will be a debit balance.
2. Purchases return account always shows a credit balance because assets go out.
3. Balance in Trade payables is a liability, so its balance will be a credit balance.
4. Bills payable is a liability, so its balance will be a credit balance.
5. Inventory (opening) represents assets, so it will have a debit balance.
6. Sales return account always shows a debit balance because assets come.

**ILLUSTRATION 5**

The following trail balance as on 31<sup>st</sup> March, 2022 was drawn from the books of fintech traders:

	L.F.	Dr. Balance (₹)	Cr. Balance (₹)
<i>Building</i>		60,000	-
<i>Machinery</i>		17,000	-
<i>Return Outward</i>		2,600	-
<i>Bad Debts</i>		2,800	-
<i>Cash</i>		400	-

<i>Discount Received</i>		3,000	-
<i>Bank Overdraft</i>		10,000	-
<i>Creditors</i>		50,000	-
<i>Purchases</i>		1,00,000	-
<i>Capital</i>		-	73,600
<i>Fixtures</i>		-	5,600
<i>Sales</i>		-	1,04,000
<i>Debtors</i>		--	60,000
<i>Interest Received</i>		-	2,600
<i>Input CGST A/c</i>		-	3,000
<i>Input SGST A/c</i>		-	3,000
<i>Input IGST A/c</i>		-	4,800
<i>Output CGST A/c</i>		5,400	-
<i>Output SGST A/c</i>		5,400	-
<i>Total</i>		2,56,600	2,56,600

Even though the debit and credit sides agree, the trial Balance contains certain errors. Check the accuracy of trial balance.

### SOLUTION

#### Corrected Trial Balance of Fintech traders as on 31st March, 2022

	<i>L.F.</i>	<i>Dr. Balance (₹)</i>	<i>Cr. Balance (₹)</i>
Building		60,000	-
Machinery		17,000	-
Return Outward		-	2,600
Bad Debts		2,800	-
Cash		400	-
Discount Received		-	3,000
Bank Overdraft		-	10,000
Creditors		-	50,000
Purchases		1,00,000	-
Capital		-	73,600

Fixtures		5,600	-
Sales		-	1,04,000
Debtors		60,000	-
Interest Received		-	2,600
Input CGST A/c		3,000	-
Input SGST A/c		3,000	-
Input IGST A/c		4,800	-
Output CGST A/c		-	5,400
Output SGST A/c		-	5,400
		2,56,600	2,56,600

## SUMMARY

- ◆ Trial balance contains various ledger balances on a particular date.
- ◆ It forms the basis for preparing financial statement i.e. profit and loss account and balance sheet.
- ◆ If it tallies, it means that the accounts are arithmetically accurate but certain errors may still remain undetected.
- ◆ It is very important to carefully journalize and post the entries, following the rules of accounting.

## TEST YOUR KNOWLEDGE

### True and False

1. *Preparing trial balance is the third phase of accounting process.*
2. *Trial balance forms a base for the preparation of Financial statement.*
3. *Agreement of trial balance is a conclusive proof of accuracy.*
4. *A trial balance will tally in case of compensating errors.*
5. *A trial balance can find the missing entry from the journal.*
6. *Suspense account opened in a trial balance is a permanent account.*
7. *The balance of purchase returns account has a credit balance.*

### Multiple Choice Questions

1. A trial balance will not balance if \_\_\_\_\_
  - (a) Correct journal entry is posted twice.
  - (b) The purchase on credit basis is debited to purchases and credited to cash.
  - (c) ₹ 500 cash payment to creditor is debited to Trade payables for ₹ 50 and credited to cash as ₹ 500.
  
2. ₹ 1, 500 received from sub-tenant for rent and entered correctly in the cash book is posted to the debit of the rent account. In the trial balance \_\_\_\_\_
  - (a) The debit total will be greater by ₹ 3,000 than the credit total.
  - (b) The debit total will be greater by ₹ 1,500 than the credit total.
  - (c) Subject to other entries being correct the total will agree.
  
3. After the preparation of ledgers, the next step is the preparation of \_\_\_\_\_
  - (a) Trading accounts
  - (b) Trial balance
  - (c) Profit and loss account
  
4. After preparing the trial balance the accountant finds that the total of debit side is short by ₹ 1,500. This difference will be \_\_\_\_\_
  - (a) Credited to suspense account
  - (b) Debited to suspense account
  - (c) Adjusted to any of the debit balance account

S.No.	Account heads	Debit (₹)	Credit (₹)
1.	Sales		15,000
2.	Purchases	10,000	
3.	Miscellaneous expenses	2,500	
4.	Salaries		2,500
	Total	12,500	17,500

The difference in trial balance is due to \_\_\_\_\_

- (a) Wrong placing of sales account
- (b) Wrong placing of salaries account
- (c) Wrong placing of miscellaneous expenses account

### Theory Questions

1. What is the trial balance? And how it is prepared?
2. Explain objectives of preparation of trial balance.
3. Even if the trial balance agrees, some errors may remain. Do you agree? Explain.

### Practical Question

1. An inexperienced bookkeeper has drawn up a Trial Balance for the year ended 30th June, 2022.

	Debit (₹)	Credit (₹)
Provision for Doubtful Debts	200	–
Bank Overdraft	1,654	–
Capital	–	4,591
Trade payables	–	1,637
Trade receivables	2,983	–
Discount Received	252	–
Discount Allowed	–	733
Drawings	1,200	–
Office Furniture	2,155	–
General Expenses	–	829
Purchases	10,923	–
Returns Inward	–	330
Rent & Rates	314	–
Salaries	2,520	–
Sales	–	16,882
Inventory	2,418	–
Provision for Depreciation on Furniture	364	–
<b>Total</b>	<b>24,983</b>	<b>25,002</b>

#### Required:

Draw up a 'Corrected' Trial Balance, debiting or crediting any residual errors to a Suspense Account.

## ANSWERS/HINTS

### True and False

1. *True: Preparing trial balance is the third phase of accounting process which forms the base for the preparation of the final accounts.*
2. *True: Based on trial balance only, we can prepare financial statement.*
3. *False: Agreement of trial balance gives only arithmetical accuracy, there can still be errors in preparing the trail balance.*
4. *True: Since compensating errors cancel out due to their compensating nature of the amounts, hence the Trial balance tallies.*
5. *False: A trial balance cannot find the missing entry from the journal.*
6. *False: Suspense account opened in a trial balance is a temporary account*
7. *True: As purchases is debited, any returns shall be credited (treated in opposite way).*

### Multiple Choice Questions

1.	(c)	2.	(a)	3.	(b)	4.	(b)	5.	(b)		
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### Theoretical Questions

1. Preparation of trial balance is the third phase in the accounting process. After posting the accounts in the ledger, a statement is prepared to show separately the debit and credit balances. Such a statement is known as the trial balance.  
  
Trial balance contains various ledger balances on a particular date. It forms the basis for preparing the financial statements i.e. profit and loss account and balance sheet. If is tallies, it means that the accounts are arithmetically accurate but certain errors may still remain undetected. Therefore, it is very important to carefully journalise and post the entries, following are rules of accounting.
2. The preparation of trial balance has the following objectives:
  - (i) Trial balance enables one to establish whether the posting and other accounting processes have been carried out without committing arithmetical errors. In other words, the trial balance helps to establish arithmetical accuracy of the books of accounts.
  - (ii) Financial statements are normally prepared on the basis of agreed trial balance.
  - (iii) The trial balance serves as a summary of what is contained in the ledgers.

3. In spite of the agreement of the trial balance some errors may remain. These may be of the following types:
- (i) Transaction has not been entered at all in the journal.
  - (ii) A wrong amount has been written in both columns of the journal.
  - (iii) A wrong account has been mentioned in the journal.
  - (iv) An entry has not at all been posted in the ledger.
  - (v) Entry is posted twice in the ledger.

### Practical Question

1. **Trial Balance as on 30th June, 2022**

Heads of Accounts	Debit ₹	Credit ₹
Provision for Doubtful Debts	–	200
Bank overdraft	–	1,654
Capital	–	4,591
Trade payables	–	1,637
Trade receivables	2,983	–
Discount Received	–	252
Discount allowed	733	–
Drawings	1,200	–
Office furniture	2,155	–
General Expenses	829	–
Purchases	10,923	–
Returns Inward	330	–
Rent & Rates	314	–
Salaries	2,520	–
Sales	–	16,882
Inventory	2,418	–
Provision for Depreciation on Furniture	–	364
Suspense Account (Balancing figure)	1,175	–
<b>Total</b>	<b>25,580</b>	<b>25,580</b>

## UNIT – 4 SUBSIDIARY BOOKS

### LEARNING OUTCOMES

After studying this unit, you will be able to:

- ◆ Understand the techniques of recording transactions in Purchase Book, Sales Book; Returns Inward Book and Returns Outward Book; Bills Receivable and Bills Payable Book.
- ◆ Learn the technique of posting from Subsidiary Books to Ledger.
- ◆ Understand that even if subsidiary books are maintained, journalisation is required for many other transactions and events.
- ◆ Learn the difference between the subsidiary books and principal books.

### UNIT OVERVIEW

#### Principal books

- Ledger
- Cash books

#### Subsidiary books

- Purchases and Sales book, Purchase and Sales return books
- Bill payable and Bills receivable books
- Journal Proper



## 4.1 INTRODUCTION

In a business, most of the transactions generally relate to receipts and payments of cash, sale of goods and their purchase. It is convenient to keep a separate register for each such class of transactions one for receipts and payments of cash, one for purchase of goods and one for sale of goods. A register of this type is called a book of original entry or of prime entry. The transactions recorded in such books will not require journal entries. The system by which transactions of a class are first recorded in the specified book, specially meant for it and on the basis of which ledger accounts are then prepared is known as the Practical System of Book keeping or even the English System. It should be noted that in this system, there is no departure from the rules of the double entry system.

These books of original or prime entry are also called subsidiary books since ledger accounts are prepared on their basis without further processing of ledger posting. Normally, the following subsidiary books are used in a business:

- (i) Cash Book to record receipts and payments of cash, including receipts into and payments out of the bank.
- (ii) Purchases Book to record credit purchases of goods dealt in or of the materials and stores required in the factory.
- (iii) Purchase Returns Book to record the returns of goods and materials previously purchased.
- (iv) Sales Book to record the sales of the goods dealt in by the firm.
- (v) Sale Returns Book to record the returns of goods made by the customers sold to them earlier.
- (vi) Bills Receivable Book to record the receipts of promissory notes or hundies from various parties.
- (vii) Bills Payable Book to record the issue of the promissory notes or hundies to other parties.
- (viii) Journal (proper) to record the transactions which cannot be recorded in any of the seven books mentioned above.

It may be noted that in all the above cases the word "Journal" may be used for the word "book".

### Advantages of Subsidiary Books

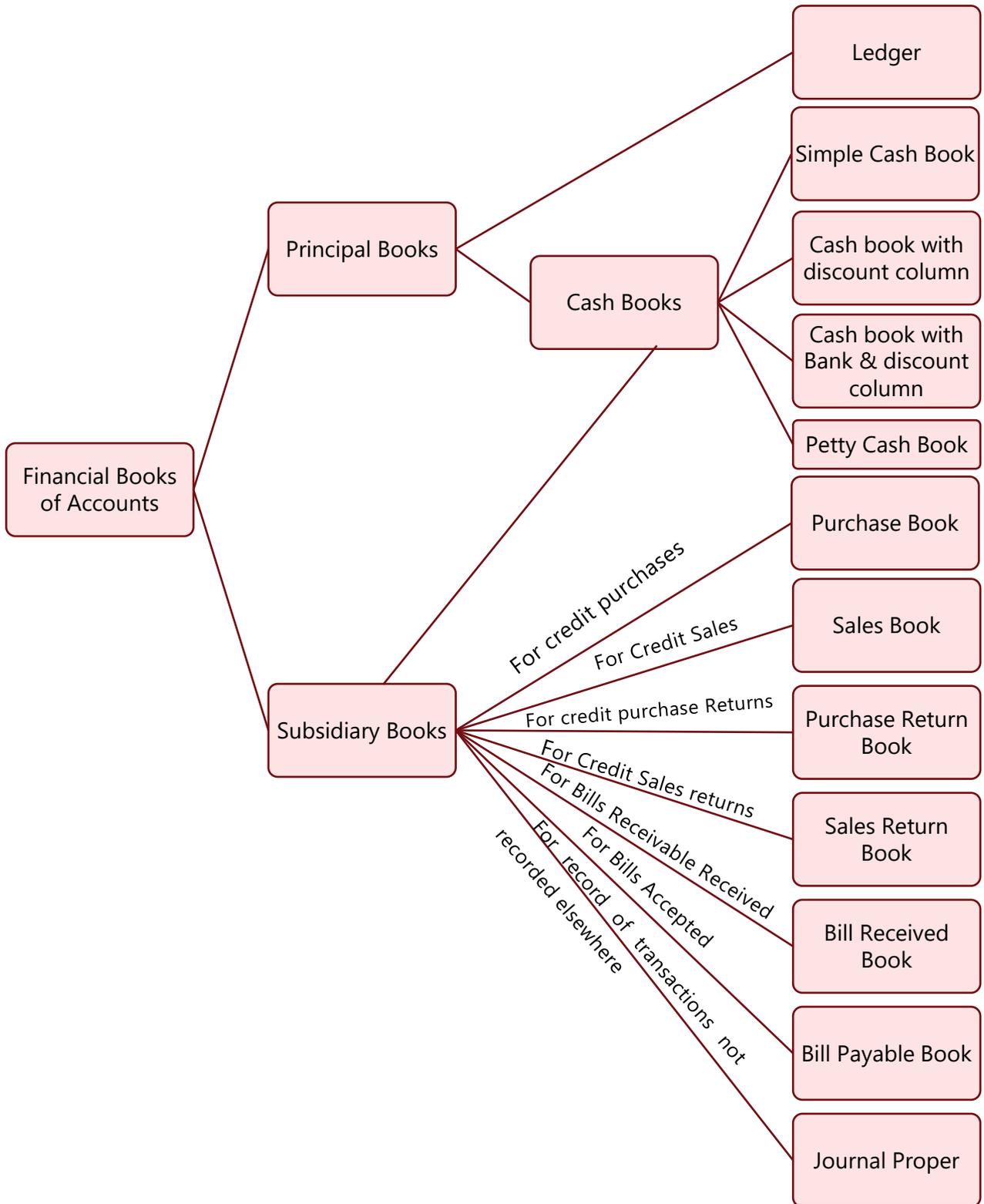
The use of subsidiary books affords the undermentioned advantages:

- (i) **Division of work:** Since in the place of one journal there will be so many subsidiary books, the accounting work may be divided amongst a number of clerks.
- (ii) **Specialization and efficiency:** When the same work is allotted to a particular person over a period of time, he acquires full knowledge of it and becomes efficient in handling it. Thus the accounting work will be done efficiently.
- (iii) **Saving of the time:** Various accounting processes can be undertaken simultaneously because of the use of a number of books. This will lead to the work being completed quickly.
- (iv) **Availability of information:** Since a separate register or book is kept for each class of transactions, the information relating to each class of transaction be available at one place.
- (v) **Facility in checking:** When the trial balance does not agree, the location of the error or errors is facilitated by the existence of separate books. Even the commission of errors and frauds will be checked by the use of various subsidiary books.



## 4.2 DISTINCTION BETWEEN SUBSIDIARY BOOKS AND PRINCIPAL BOOKS

The books in which transactions are first recorded to enable further processing are called subsidiary books. The ledger and the cash book are the principle books since they furnish information for preparation of the trial balance and financial statements. The following chart will help you in understanding the difference between Subsidiary Books and Principal Books.





### 4.3 PURCHASES BOOK

To record the credit purchases of goods dealt in or materials used in the business, a separate register called the Purchases Book or the Purchases Journal, is usually maintained by firms. The format is given below:

Date	Particulars	Details ₹	Amount ₹

It should be remembered that:

- (i) Cash purchases are not entered in this book since these will be entered in the cash book; and
- (ii) Credit purchases of items other than goods or materials, such as office furniture or typewriters are journalised - they are not entered in the Purchases Book.

The particulars column is meant to record the name of the supplier and name of the articles purchased and the respective quantities. The amount in respect of each article is entered in the details column. After totalling the various amounts included in a single purchase, the amount for packing, or other charges is added and the amount for trade discount is deducted. The net amount is entered in the amount column. The total in the amount column shows the total purchase made in a period.

#### ILLUSTRATION 1

*The Rough Book of M/s. Narain & Co. contains the following :*

**2022**

- Feb.**
1. Purchased from Brown & Co. on credit :  
5 gross pencils @ ₹100 per gross,  
1 gross register @ ₹ 240 per doz.  
Less : Trade Discount @ 10%
  2. Purchased for cash from the Stationery Mart;  
10 gross exercise books @ ₹ 300 per doz.
  3. Purchased computer for office use from M/s. office Goods Co. on credit for ₹ 30,000.
  4. Purchased on credit from The Paper Co.  
5 reams of white paper @ ₹100 per ream.

10 reams of ruled paper @ ₹150 per ream.

Less : Trade Discount @ 10%

5. Purchased one dozen gel pens @ ₹15 each from  
M/s. Verma Bros. on credit.

Make out the Purchase Book of M/s. Narain & Co.

### SOLUTION

#### Purchases Book

Date	Particulars	Details	Amount
<b>2022</b>		₹	₹
Feb. 1	M/s. Brown & Co. 5 gross pencils @ ₹ 100 per gross 1 gross register @ ₹ 240 per doz.	500.00 <u>2880.00</u> 3380.00	
	Less : 10% trade discount	<u>(338)</u>	3,042
"4	The Paper Co. 5 reams white paper @ ₹ 100 per ream 10 reams ruled paper @ ₹ 150 per ream	500.00 <u>1500.00</u> 2,000.00	
	Less : 10% trade discount	<u>(200.00)</u>	1,800
5	M/s. Verma Bros. 1 doz. gel pens @ ₹ 15 each	180	<u>180</u>
		Total	5022

**Note :** Purchases of cash and purchase of computer are not recorded in the Purchase Book.

### ILLUSTRATION 2

Enter the following transactions in Purchase Book and post them into ledger.

**2022**

- April 4 Purchased from Ajay Enterprises, Delhi  
100 Doz. Rexona Hawai Chappal @ ₹ 120 per doz.  
200 Doz. Palki Leather Chappal @ ₹ 300 per Doz.

Less : Trade discount @ 10%

Freight charged ₹ 150.

April 15 Purchased from Balaji Traders, Delhi

50 doz. Max Shoes @ ₹ 400 per doz.

100 pair Sports Shoes @ ₹ 140 per pair.

Less : Trade discount @ 10%.

Freight charged ₹ 200.

April 28 Purchased from Tripti Industries, Bahadurgarh

40 pair leather shoes @ ₹ 400 per pair

100 doz. Rosy Hawai Chappal @ ₹ 180 per doz.

Less : Trade discount @ 10%.

Freight charged ₹ 100.

### SOLUTION

#### Purchase Book

Date 2022	Particulars	Details	Gross Amount	Trade Discount	Net Price	Freight	Total Amount
April 4	Ajay Enterprises						
	100 doz Rexona Hawai chappal @ ₹ 120 per doz - ₹ 12,000	12,000					
	200 doz Palki Leather Chappal @ ₹ 300 per doz - ₹ 60,000	60,000					
	Less: trade discount @ 10%		72,000	7,200	64,800	150	64,950
April 15	Balaji Traders, Delhi						
	50 doz max Shoes @ ₹ 400 per doz - ₹ 20,000	20,000					
	100 pair Sports shoes @ ₹ 140 per pair - ₹ 14,000	14,000					
	Less: Trade discount @ 10%		34,000	3,400	30,600	200	30,800

April 28	Tripti Industries, Bahadurgarh						
	40 pair Leather shoes @ ₹ 400 per pair - ₹ 16,000	16,000					
	100 doz Rosy Hawai Chappal: @ ₹ 180 per doz - ₹ 18,000	18,000					
	Less: Trade discount @ 10%						
			<u>34,000</u>	<u>3,400</u>	<u>30,600</u>	<u>100</u>	<u>30,700</u>
			1,40,000	14,000	1,26,000	450	1,26,450

**Ledgers**

Dr. **Purchases A/c** Cr.

2022		₹	2022		₹
April 30	To amount as per purchase book	1,26,000			

Dr. **Freight A/c** Cr.

2022		₹	2022		₹
April 30	To amount as per purchase book	450			

Dr. **Ajay Enterprises** Cr.

2022		₹	2022		₹
			April 4	By Purchase A/c (From Purchase Book)	64,800
				By Freight A/c (From Purchase Book)	150

Dr. **Balaji Traders** Cr.

2022		₹	2022		₹
			April 15	By Purchase A/c (From Purchase Book)	30,600
				By Freight A/c (From Purchase Book)	200

Dr. **Tripati Industries** Cr.

2022		₹	2022		₹
			April 28	By Purchase A/c (From Purchase Book)	30,600
				By Freight A/c (From Purchase Book)	100

## POSTING THE PURCHASES BOOK

The Purchases Book shows the names of the parties from whom goods have been purchased on credit. These parties are now trade payables. Their accounts have to be credited for the respective amounts shown in the purchase book. The total of the amounts column shows the credit purchases made in a period. The amount is debited to the Purchase Account to indicate receipt of goods. In Illustration 1, the Purchases Account is debited by ₹ 5,022, M/s. Brown & Co. is credited by ₹ 3,042, The Paper Company by ₹1,800 and M/s. Verma Bros. by ₹180. The total of the amounts put on the credit side equals the debit. Thus the double entry is completed.



## 4.4 SALES BOOK

The Sales Book is a register specially kept to record credit sales of goods dealt in by the firm, cash sales are entered in the Cash Book and not in the Sales Book. Credit sales of items other than the goods dealt in by the firm are not entered in the Sales Book rather they are journalised. The rules are the same as for the Purchases Book.

Entries in the Sales Book are also made in the same manner as in the Purchase Book. The particulars column will record the name of the customers concerned together with particulars and quantities of the goods sold. For each item, the amount is entered in the details column; after totalling the amounts for one sale, charges for packing etc; are added and the trade discount, if any is deducted: the net amount is put in the outer column. The total of this column will show the total credit sales for a period.

### ILLUSTRATION 3

*The following are some of the transaction of M/s Kishore & Sons of the year 2022 as per their Waste Book. Make out their Sales Book.*

*Sold to M/s. Gupta & Verma on credit:*

*30 shirts @ ₹ 800 per shirt.*

*20 trousers @ ₹1,000 per trouser.*

Less : Trade Discount @ 10%

Sold furniture to M/s. Sehgal & Co. on credit ₹8,000.

Sold 50 shirts to M/s. Jain & Sons @ ₹800 per shirt.

Sold 13 shirts to Cheap Stores @ ₹750 each for cash.

Sold on credit to M/s. Mathur & Jain.

100 shirts @ ₹750 per shirt

10 overcoats @ ₹5,000 per overcoat.

Less: Trade Discount @ 10%

### SOLUTION

#### Sales Book

Date	Particulars	Details ₹	Amount ₹
2022	M/s. Gupta & Verma		
	30 shirts @ ₹800	24,000	
	20 Trousers @ ₹1,000	20,000	
		44,000	
	Less : 10%	(4,400)	
	Sales as per invoice no. dated .....		39,600
	M/s. Jain & Sons 50 shirts @ ₹800		
	Sale as per invoice no. dated .....		40,000
	M/s Mathur & Jain		
	100 shirts @ ₹750	75,000	
	10 overcoats @ ₹5,000	50,000	
		1,25,000	
	Less : 10%	(12,500)	
	Sales as per invoice no. dated.....		1,12,500
		Total	1,92,100

**Note :** Cash sale and sale of furniture are not entered in Sales Book.

## POSTING THE SALES BOOK

The names appearing in the Sales Book are of those parties which have received the goods. The accounts of the parties have to be debited with the respective amounts. The total of the Sales Book shows the credit sales made during the period concerned; the amount is credited to the Sales Account. In the Illustration 3, ₹ 1,92,100 is credited to the Sales Account; ₹39,600 is debited to M/s. Gupta and Verma ₹40,000 to M/s Jain and Sons and ₹1,12,500 to M/s Mathur & Jain. The amount put on the credit side is equal to the total of the amount put on the debit side. Thus, the double entry principle is followed correctly.

## 4.5 SALES RETURNS BOOK OR RETURNS INWARD BOOK

If customers frequently return the goods sold to them, it would be convenient to record the returns in a separate book, which is named as the Sales Returns Book or the Returns Inward Book. The rules of the book is similar to the Sales Book and entries are also made in the same manner. The following, assumed figures, will illustrate this:

### Returns Inward Book

Date	Particulars	Details	L.F.	Amount
2022				₹
June 7	Sunil Bank & Co.			
	6 Copies-Double Entry			
	Bookkeeping by T.S. Grewal @ ₹ 7	42.00		
	Less : Trade Discount 10%	(4.20)		37.80
	Kailash & Co.			
	1 Copy-Business Methods by R.K. Gupta			<u>3.50</u>
		Total		41.30

## 4.6 PURCHASE RETURNS OR RETURNS OUTWARD BOOK

Such a book conveniently records return of goods or material purchased to the suppliers. However, if the returns are not frequent, it may be sufficient to record the transaction in the journal. The rules of the Purchase Returns or Returns Outward Book is similar to that of the Purchase Book; entries are also similarly made, as the illustration given below shows:

**Returns Outward Book**

<b>Date 2022</b>	<b>Particulars</b>	<b>₹</b>	<b>Amount ₹</b>
June 2	Premier Electric Co. One 36" Usha Ceiling Fan		175.00
" 28	Mohan Electric Co. Ten Iron Heaters	150.00	
	Less : Discount	<u>(15.00)</u>	<u>135.00</u>
	Total		310.00

**POSTING OF THE RETURN BOOKS**

The Sales Return Book will show the total of the returns made by customers. The total of the sales returns is in reduction of the sales. Therefore, the amount may be debited to the Sales Account but, usually, a separate account called Returns Inward Account is opened and the total of the sales returns is debited to this accounts. The customers who have returned the goods are credited with the respective amounts.

It should be noted that on goods being received and accepted back from the customers, a credit note is issued to the customers concerned. This shows the amount to be credited to the customer's account.

Similarly, when goods are returned to suppliers they will issue the necessary credit note; also the firm returning the goods will issue a debit note to the supplier, indicating the amount for which the supplier account is being debited.

The total of Returns Outwards Book shows the total purchase returns made. The amount can be credited to the Purchase Account, but in practice, it is credited to a separate account called Purchase Returns or Returns Outward Account. The suppliers whose names appear in the Book have received the goods, so their accounts are debited. This is shown in the illustration given below:

**ILLUSTRATION 4**

*Post the following into the ledger*

**Returns Outward Book**

<b>Date 2022</b>	<b>Particulars</b>	<b>Details ₹</b>	<b>Amount ₹</b>
Nov. 20	Rajindra Prakash & Sons		

" 30	One 36" Usha Ceiling Fan	200.00	
	Less : Trade Discount @ 10%	<u>(20.00)</u>	180.00
	Modern Electric Company		100.00
	Total		280.00

**SOLUTION****Ledger**Dr. **Rajindra Parkash & Sons** Cr.

Date 2022	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
Nov. 20	To Returns Outward A/c (From Returns Outward Book)		180.00				

Dr. **Modern Electric Co.** Cr.

Date 2022	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
Nov. 30	To Returns Outward A/c (From Returns Outward Book)		100.00				

Dr. **Returns Outward Account** Cr.

Date 2022	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
				Nov. 30	By Sundries as per Returns Outward Book		280.00

**BILLS RECEIVABLE BOOKS AND BILLS PAYABLE BOOKS**

If the firm usually receives a number of promissory notes or hundies, it would be convenient to record the transaction in a separate book called the Bills Receivable Book. Similarly, if promissory notes or hundies are frequently issued, the Bills Payable Book will be convenient. This will be discussed later.



## 4.7 IMPORTANCE OF JOURNAL

Students are now familiar with the journal. They also know that :

- (i) Cash transactions are recorded in the cash book;
- (ii) Credit purchases of goods or materials are recorded in the purchases book;
- (iii) Credit sales of goods are recorded in the sales book;
- (iv) Returns from customers are recorded in the sale returns book; and
- (v) Returns to suppliers are entered in the purchase returns book.

Bill received or accepted transactions are entered in the bills receivable books or the bills payable books, if these are maintained. Apart from the transactions mentioned above, there are other entries also which have to be recorded. For them the proper place is the journal. In fact, if there is no special book meant to record a transaction, it is recorded in the journal (proper). The role of the journal is thus restricted to the following types of entries:

- (i) **Opening entries** : When books are started for the new year, the opening balance of assets and liabilities are journalised.
- (ii) **Closing entries** : At the end of the year, the profit and loss account is prepared. For this purpose, the nominal accounts are transferred to profit and loss account. This is done through journal entries called closing entries.
- (iii) **Rectification entries** : If an error has been committed, it is rectified through a journal entry.
- (iv) **Transfer entries** : If some amount is to be transferred from one account to another, the transfer will be made through a journal entry.
- (v) **Adjusting entries** : At the end of the year the amount of expenses or income may have to be adjusted for amounts received in advance or for amounts not yet settled in cash. Such an adjustment is also made through journal entries. Usually, the entries pertain to the following:
  - (a) Outstanding expenses, i.e., expenses incurred but not yet paid;
  - (b) Prepared expenses, i.e., expenses paid in advance for future period;
  - (c) Interest on capital, i.e., the interest on proprietor's investment in the business; and
  - (d) Depreciation, i.e., fall in the value of the assets used on account of wear and tear.

For above type of transactions/events, journal entries are necessary.

- (vi) **Entries on dishonour of Bills :** If someone who accepted a promissory note (or bill) is not able to pay in on the due date, a journal entry will be necessary to record the non-payment or dishonour of bills.
- (vii) **Miscellaneous entries :** The following entries will also require journalising:
- Credit purchase of items other than goods dealt in or materials required for production of goods e.g. credit purchase of furniture or machinery will be journalised.
  - An allowance to be given to the customers or a charge to be made to them after the issue of the invoice.
  - Receipt or issue of promissory notes, if separate bill books have not been maintained.
  - If an amount becomes irrecoverable, say, because, of the customer becoming insolvent.
  - Effects of accidents such as loss of property by fire.
  - Transfer of net profit to capital account.

**ILLUSTRATION 5**

From the following transactions, prepare the Purchases Returns Book of Alpha & Co., a saree dealer :

Date	Debit Note No.	Particulars
04.01.2022	101	Returned to Goyal Mills, Surat - 5 polyester sarees @ ₹ 1,000.
09.01.2022		Garg Mills, Kota - accepted the return of goods (which were purchased for cash) from us - 5 Kota sarees @ ₹ 400.
16.01.2022	102	Returned to Mittal Mills, Bangalore - 5 silk sarees @ ₹ 2,600.
30.01.2022		Returned one computer (being defective) @ ₹ 35,000 to B & Co.

**SOLUTION****Purchase Returns Book**

Date	Debit Note No.	Name of supplier	L.F.	Amount
2022				
Jan. 4	101	Goyal Mills, Surat		5,000
Jan. 16	102	Mittal Mills, Bangalore		13,000
Jan. 31		Purchases Returns Account (Cr.)		18,000

## SUMMARY

- ◆ Instead of recording all journal entries in one register, it is better to categorize the entries on the basis of type of transactions.
- ◆ Various subsidiary books are maintained so as to record transactions of one type in each register. These are also called books of original entry or prime entry.
- ◆ Example of subsidiary books are purchases book, sales book, purchase returns books, sales returns book, bills receivable book, bills payable book etc. On the basis of these subsidiary books, the ledger accounts are prepared.

## TEST YOUR KNOWLEDGE

### True and False

1. *Transactions recorded in the purchase book include only purchases of goods on credit transactions.*
2. *Transactions regarding the purchase of fixed asset are recorded in the purchase book.*
3. *Cash sales are recorded in the sales book.*
4. *Subsidiary books are also known as the books of original entry.*
5. *Bills receivable book is a subsidiary book.*
6. *Return inward book is also known as purchase return book.*
7. *Purchase of a second hand machinery will be recorded in purchase book.*
8. *Total of sales return book may be posted to the debit side of sales account.*
9. *If the sales are on a frequent basis, the transactions are recorded in the sales book.*

### Multiple Choice Questions

1. *In Purchases Book, the record is in respect of \_\_\_\_\_*
  - (a) *Cash purchase of goods.*
  - (b) *Credit purchase of goods dealt in.*
  - (c) *All purchases of goods.*
2. *The Sales Returns Book records \_\_\_\_\_*
  - (a) *The return of goods purchased.*

- (b) Return of anything purchased.
- (c) Return of goods sold.
3. The Sales Book \_\_\_\_\_
- (a) Is a part of journal.
- (b) Is a part of the ledger.
- (c) Is a part of the balance sheet.
4. The weekly or monthly total of the Purchase Book is \_\_\_\_\_
- (a) Posted to the debit of the Purchases Account.
- (b) Posted to the debit of the Sales Account.
- (c) Posted to the credit of the Purchases Account.
5. The total of the Sales Book is posted to \_\_\_\_\_
- (a) Credit of the Sales Account.
- (b) Credit of the Purchases Account.
- (c) Credit of the Capital Account.
6. In which book of original entry, will you record an allowance of ₹50 which was offered for an early payment of cash of ₹1,050 \_\_\_\_\_.
- (a) Sales Book
- (b) Cash Book
- (c) Journal Proper (General Journal)
7. A second hand motor car was purchased on credit from B Brothers for ₹10,000 will be recorded in \_\_\_\_\_.
- (a) Journal Proper (General Journal)
- (b) Sales Book
- (c) Cash Book
- (d) Purchase Book
8. In which book of original entry, will you record a bills receivable of ₹1,000, which was received from a debtor in full settlement for a claim of ₹1,100, is dishonoured \_\_\_\_\_.
- (a) Purchases Return Book

- (b) *Bills Receivable Book*
- (c) *Journal Proper (General Journal)*

### Theory Questions

1. *Which subsidiary books are normally used in a business?*
2. *What are the advantages of subsidiary books?*

### Practical Questions

1. *Enter the following transactions in Sales Book of M/s. Pranat Engineers Ltd., Delhi.*  
*2022*  
*Jan. 2. Sold to M/s. Ajanta Electricals, Delhi 5 pieces of Ovens @ ₹6,000/- each less Trade discount @ 10%.*  
*8 Sold to M/s. Electronics Plaza, 10 pieces of Tablets @ ₹8,000/- each less trade discount 5%.*  
*15 Sold to M/s. Haryana Traders, 5 pieces of Juicers @ ₹3,500/- each less trade discount @ 10%.*
2. *Post into the ledger, the entries of Sales Book prepared in Question 1.*

### ANSWERS/HINTS

#### True and False

1. True: Since cash purchases are taken to the cash book, it is only credit transactions that are recorded in the purchases book.
2. False: Transactions regarding the purchase of fixed asset are not recorded in the purchase book, only the credit purchases of goods are recorded in it.
3. False: Credit sales are recorded in the sales book.
4. True: Subsidiary books are maintained as an alternate to the journal.
5. True: Bills receivable is one of the subsidiary book.
6. False: Return inward book is also known as sales return book.
7. False: Purchase of a second hand machinery will not be recorded in purchase book.
8. True: Since sales return is reduction from the total sales value, it is debited in the sales account.

9. True: When there are numerous transactions then there are subsidiary books like the sales book where there are recorded instead of regular journal entries.

### Multiple Choice Questions

1.	(b)	2.	(c)	3.	(a)	4.	(a)	5.	(a)	6.	(b)
7.	(a)	8.	(c)								

### Theoretical Questions

- Refer para 4.1 of this unit for subsidiary books normally mainlined in a business.
- For advantages of Subsidiary Books, refer para 4.1 of this unit.

### Practical Problems

#### 1. Sales Book

Date	Particulars	Gross Amount (₹)	Trade Discount (₹)	Net Price (₹)
2022				
Jan. 2	M/s. Ajanta Electricals 5 pieces of Ovens @ ₹ 6,000 each Less: 10% discount	30,000	3,000	27,000
8	M/s. Electronics Plaza 10 pieces of Tablets @ ₹ 8,000 each, less 5% trade discount	80,000	4,000	76,000
15	M/s. Haryana Traders 5 pieces of Juicers @ ₹ 3,500 each, less 10% trade discount	<u>17,500</u>	<u>1,750</u>	<u>15,750</u>
		1,27,500	8,750	1,18,750

#### 2. Ledger

##### M/s. Ajanta Electricals

Date 2022	Particulars	L.F.	Amount (₹)	Date 2022	Particulars	L.F.	Amount (₹)
Jan. 2	To Sales A/c (From Sales Book)		27,000				

**M/s. Electronics Plaza**

Date 2022	Particulars	L.F.	Amount (₹)	Date 2022	Particulars	L.F.	Amount (₹)
Jan. 8	To Sales A/c (From Sales Book)		76,000				

**M/s. Haryana Traders**

Date 2022	Particulars	L.F.	Amount (₹)	Date 2022	Particulars	L.F.	Amount (₹)
Jan. 15	To Sales A/c (From Sales Book)		15,750				

**Sales Account**

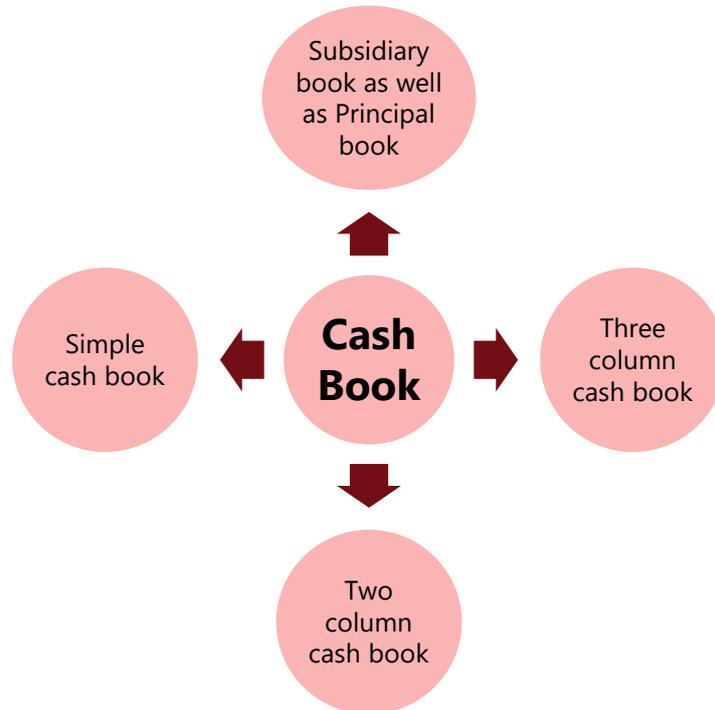
Date 2022	Particulars	L.F.	Amount (₹)	Date 2022	Particulars	L.F.	Amount (₹)
				Jan. 31	By Sundries (As per Sales Book)		1,18,750

## UNIT 5 : CASH BOOK

### LEARNING OUTCOMES

**After studying this unit, you will be able to:**

- ◆ Understand that a Cash Book is a type of subsidiary book but treated as a principal book.
- ◆ Be familiar with various kinds of Cash Books, viz., Simple Cash Book, Two-column Cash Book and Three-column Cash Book.
- ◆ Learn the technique of preparation of Simple Cash Book and how to balance it.
- ◆ See how Double-Column Cash Book is prepared adding discount column alongwith cash column.
- ◆ Understand the techniques of preparing Three-column Cash Book.
- ◆ Understand what is a Petty Cash Book and the Imprest System of Petty Cash.
- ◆ Note the advantages of the Petty Cash Book.
- ◆ Learn how to maintain a Petty Cash Book and how to post the entries of the Petty Cash Book in the ledger.
- ◆ Understand the accounting of credit/debit sales transactions.

**UNIT OVERVIEW** 

## 5.1 CASH BOOK - A SUBSIDIARY BOOK AND A PRINCIPAL BOOK

Cash transactions are straightaway recorded in the Cash Book and on the basis of such a record, ledger accounts are prepared. Therefore, the Cash Book is a subsidiary book. But the Cash Book itself serves as the cash account and the bank account; the balances are entered in the trial balance directly. The Cash Book, therefore, is part of the ledger also. Hence, it has also to be treated as the principal book. The Cash Book is thus both a subsidiary book and a principal book.



## 5.2 KINDS OF CASH BOOK

The main Cash Book may be of the three types:

- (i) Simple Cash Book;
- (ii) Two-column Cash Book;
- (iii) Three-column Cash Book.

In addition to the main Cash Book, firms also generally maintain a petty cash book but that is purely a subsidiary book.

### SIMPLE CASH BOOK

Such a cash book appears like an ordinary account, with one amount column on each side. The left-hand side records receipts of cash and the right-hand side the payments.

**Balancing:** The cash book is balanced like other accounts. The total of receipts column is always greater than total of payments column. The difference is written on the credit side as 'By balance c/d'. The totals are then entered in the two columns opposite one another and then on the debit side the balance is written as "To Balance b/d", to show cash balance in hand in the beginning of next period.

### ILLUSTRATION 1

*Enter the following transactions in a Simple Cash Book:*

2022		₹
Jan.1	Cash in hand	1,200
"5	Received from Ram	300
"7	Paid Rent	30
"8	Sold goods for cash	300
"10	Paid to Shyam	700
"27	Purchased Furniture	200
"31	Paid Salaries	100
"31	Rent due, not yet paid, for January	30

### SOLUTION

Dr.		Cash Book				Cr.	
Date 2022	Receipts	L.F.	Amount ₹	Date 2022	Payments	L.F.	Amount ₹
Jan. 1	To Balance b/d		1,200	Jan. 07	By Rent A/c		30
" 5	To Ram A/c		300	" 10	By Shyam A/c		700
" 8	To Sales A/c		300	" 27	By Furniture A/c		200

			" 31	By Salaries A/c	100
			" 31	By Balance c/d	770
		1,800			1,800
2022					
Feb. 1	To Balance b/d	770			

**Note :**

- (i) In the simple cash book only the cash receipts and cash payments are recorded.
- (ii) The total of debit side is always greater than the total of credit side since the payment cannot exceed the available cash.
- (iii) The simple cash book is like an ordinary account.
- (iv) Rent due not yet paid for January has not been recorded in the cash book because no cash has been paid, hence it will be recorded through normal Journal entry.

**DOUBLE-COLUMN CASH BOOK**

If along with column for "Amount" to record cash receipts and cash payments another column is added on each side to record the cash discount allowed or the discount received, or a column on the debit side showing bank receipts and another column on the credit side showing payments through bank. It is a double-column cash book.

Cash discount is an allowance which often accompanies cash payments. For example, if a customer owes ₹ 500 but is promised that 2% will be deducted if payment is made within a certain period, the customer can clear his account by paying promptly ₹ 490. Cash received will be ₹ 490 and ₹ 10 will be the discount for the firm receiving the payment and discount is a loss; for the person making the payment it is a gain. Since cash discount is allowed only if cash is paid, it is convenient to add a column for discount allowed on the receipt side of the cash book and a column for discount received on the payment side of the cash book.

**Balancing:** It should be noted that the discount columns are not balanced. They are merely totalled. The total of the discount column on the receipts side shows total discount allowed to customers and is debited to the Discount Account. The total of the column on the payments side shows total discount received and is credited to the Discount Account. The Cash columns are balanced, as already shown. The bank columns are also balanced and the balancing figure is called bank balance. Thus a double column cash book should have two columns on each side comprising of either cash and discount transaction or cash and bank transactions.

In the cash column on the debit side, actual cash received is entered; the amount of the discount allowed, if any, to the customer concerned is entered in the discount column. Similarly, actual cash paid is entered in the cash column on the payments side and discount received in the discount column. Also the bank column on the debit side records all receipts through bank and the same column on the credit side shows payment through bank.

**ILLUSTRATION 2**

Ganesh commenced business on 1st April, 2022 with ₹ 2,000 as capital. He had the following cash transactions in the month of April 2022:

		₹			₹
April 1	Purchased furniture and paid cash	250	April 7	Paid for petty expenses	15
"2	Purchased goods	500	" 8	Cash purchases	150
"4	Sold goods for cash	950			
"5	Paid cash to Ram Mohan	560	13	Paid for labour	1,000
"6	He allowed discount	10	""	Paid Ali & Sons	400
"6	Received cash from Krishna & Co.	600	""	They allowed discount	8
	Allowed discount	20			

Make out the two-column Cash Book (Cash and discount column) for the month of April, 2022.

**SOLUTION****Cash Book**

Dr. Date 2022	Receipts	L.F.	Discount ₹	Amount ₹	Date 2022	Payments	L.F.	Discount ₹	Cr. Amount ₹
April 1	To Capital A/c			2,000	April 1	By Furniture A/c			250
" 4	To Sales A/c			950	" 2	By Purchases A/c			500
" 6	To Krishna A/c		20	600	" 5	By Ram Mohan		10	560
					" 7	By Petty Expenses A/c			15

				" 8	By Purchases A/c			150
				" 13	By wages A/c			1,000
				" 13	By Ali & Sons		8	400
				" 30	By Balance c/d			675
			20				18	3,550
May 1	To Balance b/d							675

To summarise:

- (i) the discount columns in the cash book are totalled;
- (ii) they are not balanced; and
- (iii) their totals are entered in the discount received/paid account in the ledger.

**Note:** The person who pays, is credited by both the cash paid by him and the discount allowed to him. Similarly, the person to whom payment is made, is debited with both the amount paid and the discount allowed by him.

### THREE-COLUMN CASH BOOK

A firm normally keeps the bulk of its funds at a bank; money can be deposited and withdrawn at will if it is current account. Probably payments into and out of the bank are more numerous than strict cash transactions. There is only a little difference between cash in hand and money at bank. Therefore, it is very convenient if, on each side in the cash book, another column is added to record cash deposited at bank (on the receipt side of the cash book) and payments out of the bank (on the payment side of the cash book).

For writing up the three-column cash book the under mentioned points should be noted:

1. While commencing a new business, the amount is written in the cash column if cash is introduced and in the bank column if it is directly put into the bank with the description "To Capital Account". If a new cash book is being started for an existing business, the opening balances are written as : "To Balance b/d".
2. All receipts are written on the receipts side, cash in the cash column and cheques in the bank column. If any discount is allowed to the party paying the amount, the discount is entered in the discount column. In the particulars column the name of the account in respect of which payment has been received is written.
3. All payments are written on the payments side, cash payment in the cash column and payments by cheques in the bank column. If some discount has been received from the party receiving the payment, it is entered in the discount column.

4. *Contra Entries*: Often cash is withdrawn from bank for use in the office. In such a case the amount is entered in the bank column on the payments side and also in the cash column on the receipts side. In the reverse case of cash being sent to the bank, the amount is recorded in the bank column on the receipts side and in cash column on payment side. Against such entries, the letter "C" should be written in the L.F column, to indicate that these are contra transaction and no further posting is required for them.

Note: If initially cheques received are entered in the cash column and then sent to the bank, the entry is as if cash has been sent to the bank.

While recording contra entries, the basic but important rules should be followed -

- |     |                   |     |
|-----|-------------------|-----|
| (a) | The Receiver      | Dr. |
|     | The Giver         | Cr. |
| (b) | All what comes in | Dr. |
|     | All what goes out | Cr. |

e.g. where a Cash Book with separate columns for Bank Account is maintained.

- (a) If cash is deposited in Bank Account, the Bank will be the Receiver, hence it will be Debited and as the cash is going out, cash will be credited.
- (b) If cash is withdrawn from the Bank Account, the Bank will be the Giver, hence it will be Credited and, as the cash is coming in, cash will be Debited.
5. If some cheque sent to the bank is dishonoured, i.e., the bank is not able to collect the amount, it is entered in the bank column on the credit side with the name of the concerned party in the particulars column.
6. If some cheque issued by the firm is not paid on presentation, it is entered in the Bank column on the debit side with the name of the party to whom the cheque was given.
7. In a rare case, a cheque received may be given to some other party, i.e., endorsed. On receipt, it must have been entered in the bank column on the debit side; on endorsement the amount will be written in the bank column on the credit side.

The advantages of such type of Cash Book are that -

- (a) the Cash Account and the Bank Account are prepared simultaneously, therefore the double entry is completed in the Cash Book itself. Thus the contra entries can be easily cross-checked in Cash column in one side and the Bank column in the other side of the Cash Book. Also the chances of error are reduced.

- (b) the information regarding Cash in Hand and the Bank Balance can be obtained very easily and quickly as there is no need to prepare Ledger of the Bank Account.

In case of maintaining more than one Bank Account, separate column can be add for each Bank Account. Transactions between these two or more Bank Accounts can be recorded and tallied with a much less effort.

Suppose, there are two Bank Accounts namely PNB Current Account and SBI-Cash Credit Account. Now, if a cheque is issued from PNB cheque Book to SBI Account, the receiver - i.e., SBI Account will be debited and the giver i.e. the PNB Account shall be credited.

**Balancing:** The discount columns are totalled but not balanced. The cash columns are balanced exactly in the same manner as indicated for the simple cash book. The process is similar for balancing the bank columns also. It is possible, however, that the bank may allow the firm to withdraw more than the amount deposited i.e., to have an overdraft, In such a case, the total of the bank column on the credit side is bigger than the one on the debit side. The difference is written on the debit side as "To Balance c/d." Then the totals are written on the two sides opposite one another, the balance is then entered on the credit side as "By Balance b/d."

However, in usual cases debits into the bank will exceed the withdrawals or payments out of the bank. Then the bank columns are balanced just like the cash columns.

### ILLUSTRATION 3

Enter the following transactions in Cash Book with Discount and Bank Columns. Cheques are first treated as cash receipt.

2022		₹
Jan.1	Chandrika commences business with Cash	20,000
" 3	He paid into Current A/c	19,000
" 4	He received cheque from Kirti & Co. on account	600
" 7	He pays in bank Kirti & Co.'s cheque	600
" 10	He pays Rattan & Co. by cheque and is allowed discount ₹ 20	330
" 12	Tripathi & Co. pays into his Bank A/c	475
" 15	He receives cheque from Warshi and allows him discount ₹ 35	450

"	20	He receives cash ₹ 75 and cheque ₹ 100 for cash sale	
"	25	He pays into Bank, including cheques received on 15th and 20th	1,000
"	27	He pays for cash purchase	275
"	30	He pays sundry expenses in cash	50

**SOLUTION**

Dr.						Cr.					
<b>Cash Book</b>											
Date	Receipts	L.F.	Discount ₹	Cash ₹	Bank ₹	Date	Payments	L.F.	Discount ₹	Cash ₹	Bank ₹
2022						2022					
Jan. 1	To Capital A/c			20,000		Jan. 3	By Bank A/c	C		19,000	
3	To Cash	C			19,000	7	By Bank A/c	C		600	
4	To Kirti & Co.			600		10	By Ratan & Co.		20		330
7	To Cash	C			600	25	By Bank A/c	C		1,000	
12	To Tripathi & Co.				475	27	By Purchases A/c			275	
15	To Warshi		35	450		30	By S. Exp. A/c			50	
20	To Sales A/c			175							
25	To Cash	C			1,000						
						31	By Balance c/d			300	20,745
			35	21,225	21,075				20	21,225	21,075
Feb. 1	To Balance b/d			300	20,745						

**5.3 POSTING THE CASH BOOK ENTRIES**

Students would have seen that the cash columns in the cash book is actually the cash account and the bank column is actually bank account. Also, the discount columns are memorandum columns, meant only to provide information about the total discount allowed and total discount received.

The debit side columns for cash and bank indicate receipts. Therefore, the amounts debited in the cash book should be put to the credit of the account in respect of which cash or cheque has been received. For instance, in the cash book given above we see that ₹175 have been received for sale of goods. For posting, the amount is credited to the Sales Account as "By Cash ₹175." We also see M/s. Warsi have paid ₹450 and also they have been allowed ₹ 35 as discount; thus they have discharged a debt of ₹485. In the account of M/s. Warsi, the posting is on the credit side as

By Cash	₹ 450
By Discount	₹ 35
or as:	
By Sundries	₹ 485

All payments are recorded on the credit side. The particulars columns show on what account payments have been made. In the ledger accounts concerned the amount is put on the debit side. For example, the cash book shows that a cheque for ₹ 330 has been issued to M/s. Ratan & Co. and also that they have allowed a discount of ₹ 20; thus an obligation of ₹ 350 has been met. In the account of M/s. Ratan & Co. the posting is:

To Bank	₹ 330
To Discount	₹ 20
Or	
To Sundries	₹ 350

The rule thus develops: From the debit side of the cash book, credit the various accounts with their respective amounts (including any discount that may have been allowed); from the credit side of cash book, the posting will be to the debit of the accounts mentioned in the particular column with their respective amounts (including the discount which may have been received).

As has been shown already, the total of the discount columns on the debit side is debited to the discount account; the total of the column discount on the credit side is credited to the discount account. From the cash book given on the previous page ₹ 35 is debited and ₹ 20 be credited to the discount account.



## 5.4 PETTY CASH BOOK

In the firm a number of small payments, such as for telegrams, taxi fare, cartage, etc., have to be made. If all these payments are recorded in the cash book, it will become unnecessarily heavy. Also, the main cashier will be overburdened with work. Therefore, it is usual for firms to appoint a person as 'Petty Cashier' and to entrust the task of making small payments say below ₹ 200, to him. Of course he will be reimbursed for the payments made. Later, on an analysis, the respective account may be debited.

### IMPREST SYSTEM OF PETTY CASH

It is convenient to entrust a definite sum of money to the petty cashier in the beginning of a period and to reimburse him for payments made at the end of the period. Thus, he will have

again the fixed amount in the beginning of the new period. Such a system is known as the imprest system of petty cash.

The system is very useful specially if an analytical Petty Cash Book is used. The book has one column to record receipt of cash (which is only from the main cashier) and other columns to record payments of various types. The total of the various columns show why payments have been made and then the relevant accounts can be debited.

- (i) The amount fixed for petty cash should be sufficient for the likely small payments for a relatively short period, say for a week or a fortnight.
- (ii) The reimbursement should be made only when petty cashier prepares a statement showing total payments supported by vouchers, i.e., documentary evidence and should be limited to the amount of actual disbursements.
- (iii) The vouchers should be filed in order.
- (iv) No payment should be made without proper authorisation. Also, payments above a certain specified limit should be made only by the main cashier.
- (v) The petty cashier should not be allowed to receive any cash except for reimbursement.

In the petty cash book the extreme left-hand column records receipts of cash. The money column towards the right hand side shows total payments for various purposes; a column is usually provided for sundries to record infrequent payments. The sundries column is analysed. At the end of the week or the fortnight the petty cash book is balanced. The method of balancing is the same as for the simple cash book.

#### ILLUSTRATION 4

Prepare a Petty Cash Book on the imprest System from the following:

2022			₹
Jan.	1	Received ₹100 for petty cash	
"	2	Paid bus fare	.50
"	2	Paid cartage	2.50
"	3	Paid for Postage	5.00
"	3	Paid wages for casual labourers	6.00
"	4	Paid for stationery	4.00
"	4	Paid Bus charges	2.00
"	5	Paid for the repairs to chairs	15.00
"	5	Bus fare	1.00

"	5	Cartage	4.00
"	6	Postage	7.00
"	6	Bus charges	3.00
"	6	Cartage	3.00
"	6	Stationery	2.00
"	6	Refreshments to customers	5.00

**SOLUTION****Petty Cash Book**

Receipts ₹	Date 2022	V. No.*	Particulars	Total ₹	Con- veyance ₹	Cartage ₹	Statio- nery ₹	Postage ₹	Wages ₹	Sundries ₹
100	Jan.1		To Cash							
	2	1	By Conveyance	.50	.50					
		2	By Cartage	2.50		2.50				
	3	3	By Postage	5.00				5.00		
		4	By Wages	6.00					6.00	
	4	5	By Stationery	4.00			4.00			
		6	By Conveyance	2.00	2.00					
	5	7	By Repairs to Furniture	15.00						15.00
		8	By Conveyance	1.00	1.00					
		9	By Cartage	4.00		4.00				
	6	10	By Postage	7.00				7.00		
	"	11	By Conveyance	3.00	3.00					
	"	12	By Cartage	3.00		3.00				
	"	13	By Stationery	2.00			2.00			
	"	14	By General Expenses	5.00						5.00
				60.00	6.50	9.50	6.00	12.00	6.00	20.00
			By Balance c/d	40.00						
100				100.00						
40.00			To Balance b/d							
60.00	8		To Cash							

\* Voucher Numbers

### ADVANTAGES OF PETTY CASH BOOK

There are mainly three advantages:

- (i) Saving of time of the chief cashier;
- (ii) Saving in labour in writing up the cash book and posting into the ledger; and
- (iii) Control over small payments.

### POSTING THE PETTY CASH BOOK

In the ledger, a petty cash account is maintained, when an amount is given to the petty cashier, the petty cash account is debited. Each week or fortnight, the total of the payments made is credited to this account. The petty cash account will then show the balance in the hand of the cashier; on demand he should be able to produce it for counting. At the end of the period/year, the balance is shown in the balance sheet as part of cash balance.

Of course, the payments must be debited to their respective accounts as shown by the petty cash book. For this two methods may be used:

- (i) From the petty cash book the total of the various columns may be directly debited to the concerned accounts; or
- (ii) A journal entry may first be prepared on the basis of the petty cash book, debiting the accounts shown by the various analysis columns, and crediting the total of the payment of the petty cash accounts.

For Illustration 4 the journal entry and relevant accounts are as follows:

2022		Dr. ₹	Cr. ₹
Jan. 6	Conveyance Account	6.50	
	Cartage Account	9.50	
	Stationery Account	6.00	
	Postage Account	12.00	
	Wages Account	6.00	
	Repairs Account	15.00	
	General Expenses Account	5.00	
	To Petty Cash Account		60.00
	(Being the analysis of the Petty Cash Book for the week ending Jan. 6)		

Entry for cash handed over to the Petty Cashier		
Petty Cash Account	60	
To Cash Account		60
(Being Cash received)		

**Petty Cash Account**

Date 2022	Particulars	Folio	Amount ₹	Date 2022	Particulars	Folio	Amount ₹
Jan.1	To Cash		100.00	Jan. 6	By Sundries:		
"6	To Cash		60.00		Conveyance		6.50
					Cartage		9.50
					Stationery		6.00
					Postage		12.00
					Wages		6.00
					Repairs		15.00
					General Expenses		5.00

**ILLUSTRATION 5**

Enter the following transaction in Cash Book with Discount and Bank columns. Cheques are first treated as cash receipts –

2022		₹
March 1	Cash in Hand	15,000
	Overdraft in Bank	500
2	Cash Sales	3,000
3	Paid to Sushil Bros. by cheque	3,400
	Discount received	100
5	Sales through credit card	2,800
6	Received cheque from Srijan	6,200
7	Endorsed Srijan's cheque in favour of Adit	
9	Deposit into Bank	6,800
10	Received cheque from Aviral and deposited the same into Bank by allowing discount of ₹ 50	3,600

12	<i>Adit informed that Srijan's cheque is dishonoured. Now cash is received from Srijan and amount is paid to Adit through own cheque</i>	
15	<i>Sales through Debit Card</i>	3,200
24	<i>Withdrawn from Bank</i>	1,800
28	<i>Paid to Sanchit by cheque</i>	3,000
30	<i>Bank charged 1% commission on sales through Debit/Credit Cards</i>	

**SOLUTION**

Dr. **Cash Book** Cr.

Date	Particulars	L.F.	Discount ₹	Cash ₹	Bank ₹	Date	Particulars	L.F.	Discount ₹	Cash ₹	Bank ₹
2022						2022					
March 1	To Balance b/d			15,000		March 1	By Balance b/d				500
2	To Sales			3,000		3	By Sushil Bros.		100		3,400
5	To Sales				2,800	7	By Adit			6,200	
6	To Srijan			6,200		9	By Bank	C		6,800	
9	To Cash A/c	C			6,800	12	By Adit				6,200
10	To Aviral		50		3,600	24	By Cash A/c	C			1,800
12	To Srijan			6,200		28	By Sanchit				3,000
15	To Sales A/c				3,200	30	By Commission				60
24	To Bank A/c	C		1,800		31	By Balance c/d			19,200	1,440
			50	32,200	16,400				100	32,200	16,400

**Note:** If the received cheque is endorsed to the other party on the same day, then no entry is required. However, in the above case posting has been done through cash column as the endorsement is done on next day.



## 5.5 ENTRIES FOR SALE THROUGH CREDIT/DEBIT CARDS

Now-a-days sales through Credit/Debit Cards are issued by almost every Bank in India either directly or with collaboration of some other agencies. HSBC Card, SBI Card, BOB Card, ICICI Bank Card, HDFC Card and Andhra Bank Card are some of the popular Cards.

The procedure for issuing Credit/Debit Cards are as follows -

1. A small Plastic Card, called Credit Card is issued by the bank to a prospective customer, after verifying his credibility, which is generally measured by his income sources. Debit Card is issued by bank to a customer who has an account with the bank. Now a days ATM Card issued by the bank can also be used as Debit Card. This card would contain an embossed 16 digit number and also the name of the cardholder.
2. Generally Bank charges annual subscription fees from the credit card holder. No fee is charged in case of Debit Card, though some banks charge a nominal fee on Debit Card also.
3. When the Card holder intends to buy some goods or services through Credit or Debit Card, the seller insert the customer's debit/credit card in the card machine and inputs the amount of sales and gives back to customers for feeding the password (i.e Personal Identification Number – PIN) for authorising the transactions. One copy of the receipt is given to the customer and other once is kept by the sellier for its record.
4. The seller sums up the different amounts sold like this and submits, generally everyday, to his bank all the forms. The amount is credited by the bank to the seller's account and debited to the account of the Bank or the company issuing the Credit/Debit Card.
5. The bank issuing the Card, charges commission for each such transaction, which varies between 1% to 4% and is immediately debited to seller's bank account.
6. The bank sends a monthly statement to the card holder. In case of Debit Card the account is immediately debited to the card holder's account, whereas in case of Credit Card, card holder has to pay the amount in full or part. However, if not paid in full, the interest is charged.

### ACCOUNTING FOR CREDIT/DEBIT CARD SALE

From the seller's point of view, this type of sale is equivalent to a cash sale. Commission charged by the bank will be treated as selling expenses. The following journal entries will be made in the seller's books of accounts.

1. Bank A/c Dr.  
    To Sales Account  
(Sales made through Credit/Debit Card)
2. Commission Account Dr.  
    To Bank Account  
(Commission charged by bank)

## SUMMARY

- ◆ Cash book contains cash transactions and also bank transactions, if it has a separate book column. It is both a subsidiary book and a principal book.
- ◆ Cash book can be prepared with discount column also.
- ◆ For small payments, petty cash book is maintained separately for recording the particulars of payment and its amount. The fixed amount is given to the petty cashier for making small payments in the beginning of the period. The amount spent is replenished so that he will have again the fixed sum in the beginning of the next period. This system is known as imprest system of petty cash book.

## TEST YOUR KNOWLEDGE

### True and False

1. *Cash book is a subsidiary book as well as a principal book.*
2. *Two column cash book consists of two columns cash column & bank column.*
3. *Discount column of cash book is never balanced.*
4. *Contra entry is passed in a two column cash book.*
5. *If the bank column is showing the opening balance on credit side, it is an overdraft.*
6. *A cash book records cash transactions as well as credit transactions.*
7. *Discount column of cash book records the trade discount.*

### Multiple Choice Questions

1. *The total of discounts column on the debit side of the cash book, recording cash discount deducted by customers when paying their accounts, is posted to the \_\_\_\_\_*
  - (a) *Credit of the discount allowed account.*
  - (b) *Debit of the discount allowed account*
  - (c) *Credit of the discount received account.*
2. *Cash book is a type of \_\_\_\_\_ but treated as a \_\_\_\_\_ of accounts.*
  - (a) *Subsidiary book, principal book*
  - (b) *Principal book, subsidiary book*
  - (c) *Subsidiary book, subsidiary book*

3. Which of the following is not a column of a three-column cash book?
- (a) Cash column
  - (b) Bank column
  - (c) Petty cash column
4. Contra entries are passed only when \_\_\_\_\_
- (a) Double-column cash book is prepared
  - (b) Three-column cash book is prepared
  - (c) Simple cash book is prepared
5. The Cash Book records \_\_\_\_\_
- (a) All cash receipts
  - (b) All cash payments
  - (c) All cash receipts and payments
6. The balance in the petty cash book is \_\_\_\_\_
- (a) An expense
  - (b) A profit
  - (c) An asset
7. If Ram has sold goods for cash, the entry will be recorded \_\_\_\_\_
- (a) In the Cash Book
  - (b) In the Sales Book
  - (c) In the Journal

### Theory Questions

1. Is cash book a subsidiary book or a principal book? Explain.
2. What are the various kinds of cash book?
3. What are the advantages of a three column cash book?

### Practical Questions

1. Shri Ramaswamy maintains a Columnar Petty Cash Book on the Imprest System. The imprest amount is ₹500. From the following information, show how his Petty Cash Book would appear for the week ended 12th September, 2022:

₹

7-9-2022	Balance in hand	134.90
	Received Cash reimbursement to make up the imprest	365.10
	Stationery	49.80
8-9-2022	Miscellaneous Expenses	20.90
9-9-2022	Repairs	156.70
10-9-2022	Travelling	68.50
11-9-2022	Stationery	71.40
12-9-2022	Miscellaneous Expenses	6.30
13-9-2022	Repairs	48.30

## ANSWERS/HINTS

### True and False

1. True: Since the balance is directly taken to the Trial balance from cash book. Hence, it is a subsidiary book as well as principal book.
2. False: Two column cash book consists of two columns either cash column & discount column or cash column & bank column.
3. True: Discount column is totalled and transferred to the discount allowed or received account.
4. True: Contra entry can be passed in a two column cash book which includes bank and cash columns.
5. True: The debit side of opening balance shows a favourable balance, whereas the credit balance is an unfavourable balance and treated as overdraft.
6. False: A cash book records only cash transactions.
7. False: Discount column of cash book records the cash discount. Trade discount is not shown in the books of accounts.

### Multiple Choice Questions

1.	(b)	2.	(a)	3.	(c)	4.	(b)	5.	(c)	6.	(c)
7.	(a)										

## Theoretical Questions

- Cash transactions are straightaway recorded in the Cash Book and on the basis of such a record, ledger accounts are prepared. Therefore, the Cash Book is a subsidiary book. But the Cash Book itself serves as the cash account and the bank account, if bank column is also included; the balances are entered in the trial balance directly. The Cash Book, therefore, is part of the ledger also. Hence, it is also treated as the principal book. The Cash Book is thus both a subsidiary book and a principal book.
- The main Cash Book may be of the three types:
  - Simple Cash Book;
  - Two-column Cash Book;
  - Three-column Cash Book.

In addition to the main Cash Book, firms also generally maintain a petty cash book but that is purely a subsidiary book.

- The advantages of three column Cash Book are that -
  - the Cash Account and the Bank Account are prepared simultaneously, therefore the double entry is completed in the Cash Book itself. Thus the contra entries can be easily cross-checked in Cash column in one side and the Bank column in the other side of the Cash Book. The chances of error are also reduced.
  - the information regarding Cash in Hand and the Bank Balance can be obtained very easily and quickly as there is no need to prepare Ledger of the Cash and Bank Account.

## Practical Problems

### 1. Petty Cash Book

Date 2022	Receipts	Amount ₹	Date 2022	Payments	Total Amount ₹	Stationery ₹	Travelling ₹	Misc Exps. ₹	Repairs ₹
Sept. 7	To Balance b/d	134.90	7	By Stationery	49.80	49.80			
	To Reimbursement	365.10	8	By Misc. Expenses	20.90			20.90	
			9	By Repairs	156.70				156.70
			10	By Travelling	68.50		68.50		
			11	By Stationery	71.40	71.40			
			12	By Misc. Expenses	6.30			6.30	
			13	By Repairs	48.30				48.30
					421.90	121.20	68.50	27.20	205.00
				By Balance c/d	78.10				
		500.00			500.00				
	To Balance b/d	78.10							

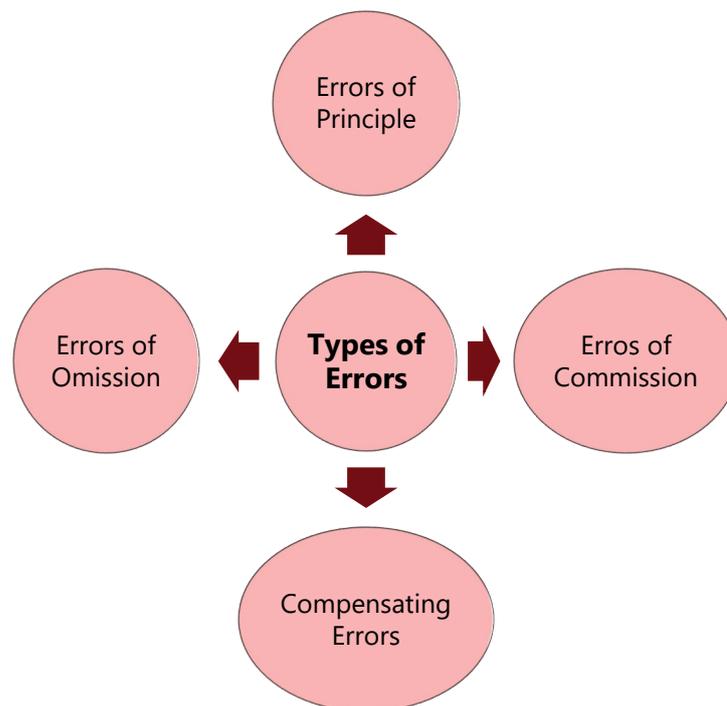
## UNIT 6 : RECTIFICATION OF ERRORS

### LEARNING OUTCOMES

After studying this unit, you will be able to:

- ◆ Understand different types of errors which may occur in the course of recording transactions and events.
- ◆ Be familiar with the steps involved in locating errors.
- ◆ Learn the nature of one-sided errors and two-sided errors.
- ◆ Understand why suspense account is opened for rectification of errors.
- ◆ Understand the technique of correcting errors of one period in the next accounting period.

### UNIT OVERVIEW





## 6.1 INTRODUCTION

Unintentional omission or commission of amounts and accounts in the process of recording the transactions are commonly known as errors. These various unintentional errors can be committed at the stage of collecting financial information/data on the basis of which financial statements are drawn or at the stage of recording this information. Also errors may occur as a result of mathematical mistakes, mistakes in applying accounting policies, misinterpretation of facts, or oversight. To check the arithmetic accuracy of the journal and ledger accounts, trial balance is prepared. If the trial balance does not tally, then it can be said that there are errors in the accounts which require rectification thereof. Some of these errors may affect the Trial Balance and some of these do not have any impact on the Trial Balance although such errors may affect the determination of profit or loss, assets and liabilities of the business.

### Illustrative Case of Errors and their Nature

We have seen that after preparing ledger accounts a trial balance is taken out where debit and credit balances are separately listed and totalled. If the totals of debit and credit do not agree, it is definite that there are some errors. We shall now study the types of errors which may be committed and how they may be rectified. For this purpose, the working of the following illustrative cases should be carefully seen.

### Illustrative Cases of Errors

- (a) **Wrong Entry:** Let us start from the first phase of the accounting process. Where wrong amount of transactions and events are recorded in the subsidiary books, Journal Proper and Cash Book.

**Example 1:** Credit purchases ₹17,270 are entered in the Purchases Day Book as ₹17,720. Credit sales of ₹15,000 gross less 1% trade discount are wrongly entered in Sales Day Book at ₹15,000. Cheque issued ₹19,920 are wrongly entered in the credit of bank column in the Cash Book as ₹19,290.

- (b) **Wrong casting of subsidiary books:** Subsidiary books are totalled periodically and posted to the appropriate ledger accounts. There may be totalling errors. Totalling errors may arise due to wrong entry or simply these may be independent errors.

**Example 2:** For the month of January, 2022 total of credit sales are ₹1,75,700, this is wrongly totalled as ₹1,76,700 and posted to sales account as ₹1,76,700.

- (c) **In case of cash book,** wrong castings will result in wrong calculation of the balance c/d.

**Example 3:** The following cash transactions of M/s. Tularam & Co. occurred:

**2023**

Jan. 1	Balance - cash ₹1,200 bank ₹16,000;
Jan. 2	Cheque issued to M/s. Bholaram & Co., a supplier, for ₹22,500;
Jan. 6	Cheque collected from M/s. Scindia & Bros. ₹42,240 and deposited for clearance;
Jan. 7	Cash sales ₹27,200 and paid wages ₹12,400;
Jan. 8	Cash sales ₹ 37,730 and cash deposited to bank ₹ 35,000.

The following Cash Book entries are passed:

Dr.		<b>Cash Book</b>				Cr.	
Date	Particulars	Cash	Bank	Date	Particulars	Cash	Bank
2023		₹	₹	2023		₹	₹
Jan. 1	To Balance b/d	1,200	16,000	Jan. 2	By M/s Bholaram & Co. A/c		22,500
Jan. 6	To M/s. Scindia & Bros. A/c		<b>42,420</b>		By Wages A/c	<b>12,200</b>	
Jan. 7	To Sales A/c	27,200			By Bank A/c	<b>34,500</b>	
Jan. 8	To Sales A/c	<b>37,370</b>			By Balance c/d	19,070	71,420
Jan. 8	To Cash A/c		<b>34,500</b>				
		65,770	<b>93,920</b>			65,770	<b>93,920</b>

Wrong entries and wrong casting are shown in bold prints. However, errors of cash entries generally are not carried. Usually cash balances are tallied daily. So errors are identified at an early stage. But bank balance cannot be checked daily and thus errors may be carried until bank reconciliation is done. In the above example, there are four wrong entries and one wrong casting. Bank and cash balances are affected by these errors.

- (d) **Wrong posting from subsidiary books:** In this case, the wrong amount may be posted to the ledger account or the amount may be posted to the wrong side or to the wrong account. For example, purchases from A may be posted to B's account.
- (e) **Wrong casting of ledger balances:** Likewise Cash Book, any ledger account balance may be casted wrongly. Obviously wrong postings make the balance wrong; but that is not wrong casting of balances. Whenever there arises independent casting error as

in the case of bank column in the Cash Book of example (4), that is called wrong casting to ledger balances.

**Example 4:** The following are the credit purchases of M/s. Ballav Bros.:

2023

Jan. 1 Purchases from M/s. Saurabh & Co.- gross ₹1,00,000 less 1% trade discount.

Jan. 3 Purchases from M/s. Netai & Co.- gross ₹ 70,000 less 1% trade discount.

Jan. 6 Purchases from M/s. Saurabh & Co.- gross ₹ 60,000 less 1% trade discount

Let us cast M/s. Saurabh & Co.'s Account:

Dr. **M/s Saurabh & Co. Account** Cr.

Date	Particulars	Amount ₹	Date	Particulars	Amount ₹
2023			2023		
Jan. 1	To Balance c/d	1,55,400	Jan. 1	By Purchases A/c	99,000
			Jan. 6	By Purchases A/c	59,400
		<b>1,55,400</b>			<b>*1,55,400</b>

\*While casting the credit side, an error has been committed and so the account is wrongly balanced.

**Example 5:** Goods are purchased on credit from M/s. Saurabh & Co. for ₹ 27,030 and from M/s. Karnataka Suppliers for ₹ 28,050. The following Purchase Day Book is prepared:

#### Purchases Day Book

Date	Particulars	Amount
		₹
	M/s. Saurabh & Co.	27,050
	M/s. Karnataka Suppliers	28,030
		55,080

In the above Purchase Day Book, both the transactions are entered wrongly but the first error has been compensated by the second. Even if these errors are not rectified Trial Balance would tally.

## Trial Balance

Particulars	Dr. ₹	Cr. ₹
M/s. Saurabh & Co.		27,050
M/s. Karnataka Suppliers		28,030
Purchases Account	55,080	
	55,080	55,080



## 6.2 STAGES OF ERRORS

Errors may occur at any of the following stages of the accounting process:

### AT THE STAGE OF RECORDING THE TRANSACTIONS IN JOURNAL

Following types of errors may happen at this stage:

- (i) Errors of principle,
- (ii) Errors of omission,
- (iii) Errors of commission.

### AT THE STAGE OF POSTING THE ENTRIES IN LEDGER

- (i) Errors of omission:
  - (a) Partial omission,
  - (b) Complete omission.
- (ii) Errors of commission:
  - (a) Posting to wrong account,
  - (b) Posting on the wrong side,
  - (c) Posting of wrong amount.

### AT THE STAGE OF BALANCING THE LEDGER ACCOUNTS

- (i) Wrong Totalling of accounts,
- (ii) Wrong Balancing of accounts.

**AT THE STAGE OF PREPARING THE TRIAL BALANCE**

- (i) Errors of omission,
- (ii) Errors of commission:
  - (a) Taking wrong account,
  - (b) Taking wrong amount,
  - (c) Taking to the wrong side.

On the above basis, we can classify the errors in four broad categories:

Errors of Principle	Errors of Omission	Errors of Commission	Compensating Errors
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**6.3 TYPES OF ERRORS**

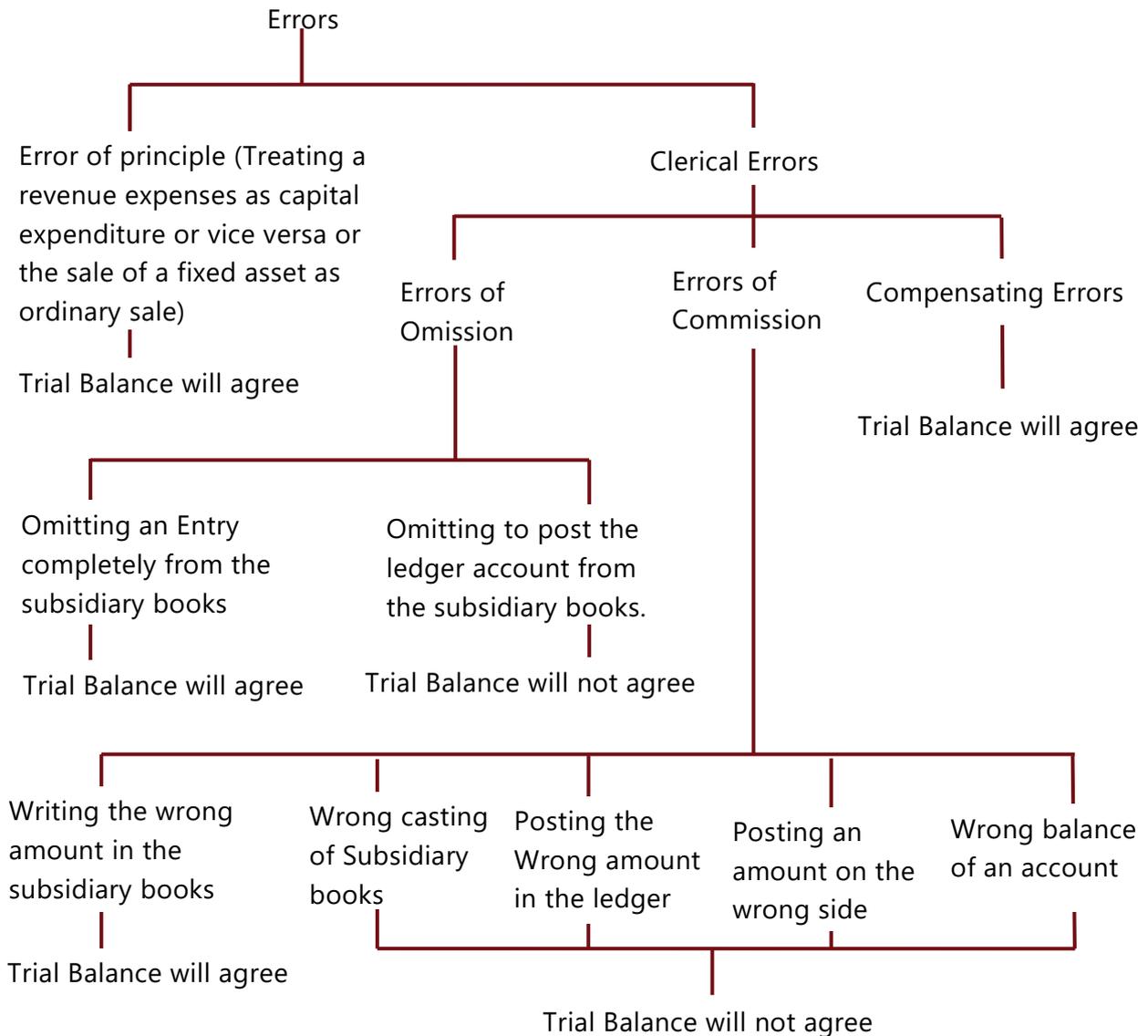
Basically errors are of two types:

- (a) **Errors of principle:** When a transaction is recorded in contravention of accounting principles, like treating the purchase of an asset as an expense, it is an error of principle. In this case, there is no effect on the trial balance since the amounts are placed on the correct side, though in a wrong account. Suppose on the purchase of a computer, the office expenses account is debited; the trial balance will still agree.
- (b) **Clerical errors:** These errors arise because of mistake committed in the ordinary course of the accounting process. These are of three types:
  - (i) *Errors of Omission:* If a transaction is completely or partially omitted from the books of account, it will be a case of omission. Examples would be: not recording a credit purchase of furniture or not posting an entry into the ledger.
  - (ii) *Errors of Commission:* If an amount is posted in the wrong account or it is written on the wrong side or the totals are wrong or a wrong balance is struck, it will be a case of "errors of commission."

- (iii) *Compensating Errors*: If the effect of errors committed cancel out, the errors will be called compensating errors. The trial balance will agree. Suppose an amount of ₹10 received from A is not credited to his account and the total of the sales book is ₹10 in excess. The omission of credit to A's account will be made up by the increased credit to the Sales Account.

From another point of view, error may be divided into two categories:

- (a) Those that affect the trial balance - because of these errors, trial balance does not agree; these are the following:
- (i) Wrong casting of the subsidiary books.
  - (ii) Wrong balancing of an account.
  - (iii) Posting an amount on the wrong side.
  - (iv) Posting the wrong amount.
  - (v) Omitting to post an amount from a subsidiary book.
  - (vi) Omitting to post the totals of subsidiary book.
  - (vii) Omitting to write the cash book balances in the trial balance.
  - (viii) Omitting to write the balance of an account in the trial balance.
  - (ix) Writing a balance in wrong column of the trial balance.
  - (x) Totalling the trial balance wrongly.
- (b) The errors that do not affect the trial balance are the following:
- (i) Omitting an entry altogether from the subsidiary book.
  - (ii) Making an entry with the wrong amount in the subsidiary book.
  - (iii) Posting an amount in a wrong account but on the correct side, e.g., an amount to be debited to A is debited to B, the trial balance will still agree.



 **6.4 STEPS TO LOCATE ERRORS**

Even if there is only a very small difference in the trial balance, the errors leading to it must be located and rectified. A small difference may be the result of a number of errors. The following steps will be useful in locating errors :

- (i) The two columns of the trial balance should be totalled again. If in place of a number of accounts, only one amount has been written in the trial balance the list of such accounts should be checked and totalled again. List of Trade receivables is the example from which Trade receivable balance is derived.

- (ii) It should be seen that the cash and bank balances have been written in the trial balance.
- (iii) The exact difference in the trial balance should be established. The ledger should be gone through again; it is possible that a balance equal to the difference has been omitted from the trial balance. The difference should also be halved; it is possible that balance equal to half the difference has been written in the wrong column.
- (iv) The ledger accounts should be balanced again.
- (v) The casting of subsidiary books should be checked again, especially if the difference is ₹ 1, ₹ 100 etc.
- (vi) If the difference is very big, the balance in various accounts should be compared with the corresponding accounts in the previous period. If the figures differ materially, those cases should be further scrutinised; it is possible that an error has been committed. Suppose the sales account for the current year shows a balance of ₹ 32,53,000 whereas it was ₹ 36,45,000 last year; it is possible that there is an error in the Sales Account.
- (vii) Postings of the amounts equal to the difference or half the difference should be checked. It is possible that an amount has been omitted to be posted or has been posted on the wrong side.
- (viii) If there is still a difference in the trial balance, a complete checking will be necessary. The posting of all the entries including the opening entry should be checked. It may be better to begin with the nominal accounts.



## 6.5 RECTIFICATION OF ERRORS

Errors should never be corrected by overwriting. The correction should be made by making another suitable entry, called as rectification entry. In fact the rectification of an error depends on at which stage it is detected. An error can be detected at any one of the following stages:

- (a) Before preparation of Trial Balance.
- (b) After Trial Balance but before the final accounts are drawn.
- (c) After final accounts, i.e., in the next accounting period.

### 6.5.1 Before preparation of Trial Balance

There are some errors which affect one side of an account or which affect more than one account in such a way that it is not possible to pass a complete rectification entry. In other words, there are some errors which can be corrected, if detected at this stage, by making rectification statement in the appropriate side(s) of concerned account(s). It is important to

note here that such errors may involve only one account or more than one account. Read the following illustrations:

- (i) The sales book for November is undercast by ₹ 200. The effect of this error is that the Sales Account has been credited short by ₹ 200. Since the account is posted by the total of the sales book, there is no error in the accounts of the customers since they are posted with amounts of individual sales. Hence only the Sales Accounts is to be corrected. This will be done by making an entry for ₹ 200 on the credit side: "By undercasting of Sales Book for November ₹ 200".
- (ii) While posting the discount column on the debit side of the cash book the discount of ₹ 10 allowed to Ramesh has not been posted. There is no error in the cash book, the total of discount column presumably has been posted to the discount account on the debit side. The error is in not crediting Ramesh by ₹ 10. This should now be done by the entry "By omission of posting of discount on ----- ₹10".
- (iii) ₹ 200 received from Ram has been entered by mistake on the debit side of his account. Since the cash book seems to have been correctly written, the error is only in the account of Ram - he should have been credited and not debited by ₹ 200. Not only the wrong debit is to be removed but also a credit of ₹ 200 is to be given. This can be done now by entering ₹ 400 on the credit side of his account. The entry will be "By Posting on the wrong side - ₹ 400".
- (iv) ₹ 50 was received from Mahesh and entered on the debit side of the cash book but was not posted to his account. By the error, which affects only the account of Mahesh, ₹ 50 has been omitted from the credit side of his account. The rectification will be by the entry. "By Omission of posting on the ₹ 50."
- (v) ₹ 51 paid to Mohan has been posted as ₹15 to the debit of his account. Mohan has been debited short by ₹ 36. The rectifying entry is "To mistake in posting on ₹ 36".
- (vi) Goods sold to Ram for ₹1,000 was wrongly posted from sales day book to the debit of purchase account. Ram has however been correctly debited. Here the error affects two accounts, viz., purchases account and sales account but we cannot pass a journal entry for its rectification because both the accounts need to be credited. The rectification will be done by the entry "By wrong posting on ₹ 1,000" in the credit of purchases account and also "By omission of posting on - ₹ 1,000" in the credit sales account.
- (vii) Bills receivable from Mr. A of ₹ 500 was posted to the credit of Bills payable Account and also credited to A account. Here also although two accounts are involved we cannot pass a complete journal entry for rectification. The rectification will be done by the entry "To wrong posting on ₹ 500" in debit of Bills payable Account and also "To omission of posting on ₹ 500" in the debit of Bills Receivable Account.

- (viii) Goods purchased from Vinod for ₹ 1,000 was wrongly credited to Vimal account by ₹ 100. Again we cannot pass a complete journal entry for rectification even though two accounts are involved. The rectification will be done by the entry "To wrong posting on ₹100" in the debit of Vimal account and "By omission of posting on ₹ 1,000" in the credit of Vinod account.

Thus, from the above illustrations, it is clear that the general rule of errors affecting two accounts can be corrected by a journal entry does not hold true always.

### ILLUSTRATION 1

*How would you rectify the following errors in the book of Rama & Co.?*

1. *The total to the Purchases Book has been undercast by ₹ 100.*
2. *The Returns Inward Book has been undercast by ₹ 50.*
3. *A sum of ₹ 250 written off as depreciation on Machinery has not been debited to Depreciation Account.*
4. *A payment of ₹ 75 for salaries (to Mohan) has been posted twice to Salaries Account.*
5. *The total of Bills Receivable Book ₹ 1,500 has been posted to the credit of Bills Receivable Account.*
6. *An amount of ₹151 for a credit sale to Hari, although correctly entered in the Sales Book, has been posted as ₹ 115.*
7. *Discount allowed to Satish ₹ 25 has not been entered in the Discount Column of the Cash Book. the amount has been posted correctly to the credit of his personal account.*

### SOLUTION

1. The Purchases Account should receive another debit of ₹100 since it was debited short previously:  
"To Undercasting of Purchases Book for the month of --- ₹100."
2. Due to this error the Returns Inward Account has been posted short by ₹ 50 : the correct entry will be:  
"To Undercasting of Returns Inward Book for the month of --- ₹50."
3. The omission of the debit to the Depreciation Account will be rectified by the entry:  
"To Omission of posting on ₹ 250".
4. The excess debit will be removed by a credit in the Salaries Account by the entry:  
"By double posting on ₹ 75".

5. ₹1,500 should have been debited to the Bills Receivable Account and not credited. To correct the mistake, the Bills Receivable Account should be debited by ₹ 3,000 by the entry:  
"To Wrong posting of B/R received on ₹ 3,000"
6. Hari's personal A/c is debited ₹ 36 short. The rectification entry will be:  
"To Wrong posting ₹ 36".
7. Due to this error, the discount account has been debited short by ₹ 25. The required entry is :  
"To Omission of discount allowed to Satish on ₹ 25."

So far we have discussed the correction of errors which affected only one Account or more than one account but for which rectifying entries were not complete journal entries. We shall now take up the correction of errors which affect more than one account in such a way that complete journal entries are possible for their rectification. Read the following illustrations:

- (i) The purchase of machinery for ₹ 2,000 has been entered in the purchases book. The effect of the entry is that the account of the supplier Ram & Co. has been credited by ₹ 2,000 which is quite correct. But the debit to the Purchases Account is wrong : the debit should be to Machinery Account. To rectify the error, the debit in the purchases Account has to be transferred to the Machinery Account. The correcting entry will be to Credit Purchases Account and debit the Machinery Account. Please see the three entries made below: the last entry rectifies the error:

Particulars	Debits ₹	Credits ₹
<b>Wrong Entry:</b>		
Purchases Account	2,000	
To Ram & Co.		2,000
<b>Correct Entry:</b>		
Machinery Account	2,000	
To Ram & Co.		2,000
<b>Rectifying Entry:</b>		
Machinery Account	2,000	
To Purchases Account		2,000

- (ii) ₹100 received from Kamal Kishore has been credited in the account of Krishan Kishore. The error is that there is a wrong credit in the account of Krishan Kishore and omission of credit in the account of Kamal Kishore; Krishan Kishore should be debited and Kamal Kishore be credited. The following three entries make this clear:

Particulars	Debits ₹	Credits ₹
<b>Wrong Entry:</b>		
Cash Account	100	
To Krishan Kishore		100
<b>Correct Entry:</b>		
Cash Account	100	
To Kamal Kishore		100
<b>Rectifying Entry:</b>		
Krishan Kishore	100	
To Kamal Kishore		100

- (iii) The sale of old machinery, ₹1,000 has been entered in the sales book. By this entry the account of the buyer has been correctly debited by ₹1,000. But instead of crediting the Machinery Account. Sales Account has been credited. To rectify the error this account should be debited and the Machinery Account credited. See the three entries given below:

Particulars	Debits ₹	Credits ₹
<b>Wrong Entry:</b>		
Buyer's Account	1,000	
To Sales Account		1,000
<b>Correct Entry:</b>		
Buyer's Account	1,000	
To Machinery Account		1,000
<b>Rectifying Entry:</b>		
Sales Account	1,000	
To Machinery Account		1,000

**ILLUSTRATION 2**

The following errors were found in the book of Ram Prasad & Sons. Give the necessary entries to correct them.

- (1) ₹ 500 paid for furniture purchased has been charged to ordinary Purchases Account.
- (2) Repairs made were debited to Building Account for ₹ 50.
- (3) An amount of ₹100 withdrawn by the proprietor for his personal use has been debited to Trade Expenses Account.
- (4) ₹100 paid for rent debited to Landlord's Account.
- (5) Salary ₹ 125 paid to a clerk due to him has been debited to his personal account.
- (6) ₹ 100 received from Shah & Co. has been wrongly entered as from Shaw & Co.
- (7) ₹ 700 paid in cash for a typewriter was charged to Office Expenses Account.

**SOLUTION****Journal**

Sr. No.	Particulars	Dr. ₹	Cr. ₹
(1)	Furniture A/c To Purchases A/c (Correction of wrong debit to Purchases A/c for furniture purchased)	500	500
(2)	Repairs A/c To Building A/c (Correction of wrong debit to building A/c for repairs made)	50	50
(3)	Drawings A/c. To Trade Expenses A/c (Correction of wrong debit to Trade Expenses A/c for cash withdrawn by the proprietor for his personal use)	100	100
(4)	Rent A/c To Landlord's Personal A/c (Correction of wrong debit to landlord's A/c for rent paid)	100	100

(5)	Salaries A/c To Clerk's (Personal) A/c (Correction of wrong debit to Clerk's personal A/c for salaries paid)	125	125
(6)	Shaw & Co. To Shah & Co. (Correction of wrong credit to Shaw & Co. Instead of Shah & Co.)	100	100
(7)	Typewriter A/c To Office Expenses A/c (Correction of wrong debit to Office Expenses A/c for purchase of typewriter)	700	700

**ILLUSTRATION 3**

Give journal entries to rectify the following:

- (1) A purchase of goods from Ram amounting to ₹150 has been wrongly entered through the Sales Book.
- (2) A Credit sale of goods amounting ₹120 to Ramesh has been wrongly passed through the Purchase Book.
- (3) On 31st December, 2022 goods of the value of ₹ 300 were returned by Hari Saran and were taken into inventory on the same date but no entry was passed in the books.
- (4) An amount of ₹ 200 due from Mahesh Chand, which had been written off as a Bad Debt in a previous year, was unexpectedly recovered, and had been posted to the personal account of Mahesh Chand.
- (5) A Cheque for ₹ 100 received from Man Mohan was dishonoured and had been posted to the debit of Sales Returns Account.

**SOLUTION****Journal**

Sr.No.	Particulars	Dr.(₹)	Cr.(₹)
(1)	Purchases A/c Sales A/c To Ram (Correction of wrong entry in the sales Book for a purchases of goods from Ram)	150 150	300

(2)	Ramesh To Purchases A/c To Sales A/c (Correction of wrong entry in the Purchases Book of a credit sale of goods to Ram)	240	120 120
(3)	Returns Inwards A/c To Hari Saran (Entry of goods returned by him and taken in inventory omitted from records)	300	300
(4)	Mahesh Chand To Bad Debts Recovered A/c (Correction of wrong credit to Personal A/c in respect of recovery of previously written off bad debts)	200	200
(5)	Man Mohan To Sales Return A/c (Correction of wrong debit to Sales Returns A/c for dishonour of cheque received from Man Mohan)	100	100

Thus, it can be said that errors detected before the preparation of trial balance can be rectified either through rectification statements (not entries) or through rectification entries.

### 6.5.2 After Trial Balance but before Final Accounts

The method of correction of error indicated so far is appropriate when the errors have been located before the end of the accounting period. After the corrections, the trial balance will agree. Sometimes the trial balance is artificially made to agree despite of errors by opening a suspense account and putting the difference in the trial balance to the account - the suspense account will be debited if the total of the credit column in the trial balance exceeds the total of the debit column and vice versa.

One must note that such agreement of the trial balance is not real. Effort must be made to locate the errors.

The rule of rectifying errors detected at this stage is simple. Those errors for which complete journal entries were not possible in the earlier stage of rectification (i.e., before trial balance) can now be rectified by way of journal entry(s) with the help of suspense account, for it these errors which gave rise to the suspense account in the trial balance. The rectification entry for other type of error i.e. error affecting more than one account in such a way that a complete

journal entry is possible for its rectification, can be rectified in the same way as in the earlier stage (i.e. before trial balance).

In a nutshell, it can be said that each and every error detected at this stage can only be corrected by a complete journal entry. Those errors for which journal entries were not possible at the earlier stage will now be rectified by a journal entry(s), the difference or the unknown side is being taken care of by suspense account. Those errors for which entries were possible even at the first stage will now be rectified in the same way.

Suppose, the sales book for November, 2022 is casted short by ₹100 ; as a consequence the trial balance will not agree. The credit column of the trial balance will be ₹100 short and a Suspense Account will be credited by ₹100. To rectify the error the Sales Account will be credited (to increase the credit to the right figure. Now one error remains, the Suspense Account must be closed by debiting the Suspense Account. The entry will be:

Suspense Account	₹100	
To Sales Account		₹100
(Correction of error of undercasting the sales Book for November 2022)		

#### ILLUSTRATION 4

Correct the following errors (i) without opening a Suspense Account and (ii) opening a Suspense Account:

- The Sales Book has been totalled ₹100 short.
- Goods worth ₹150 returned by Green & Co. have not been recorded anywhere.
- Goods purchased ₹250 have been posted to the debit of the supplier Gupta & Co.
- Furniture purchased from Gulab & Bros, ₹1,000 has been entered in Purchases Day Book.
- Discount received from Red & Black ₹15 has not been entered in the Discount Column of the Cash Book.
- Discount allowed to G. Mohan & Co. ₹18 has not been entered in the Discount Column of the Cash Book. The account of G. Mohan & Co. has, however, been correctly posted.

#### SOLUTION

If a Suspense Account is not opened.

- Since sales book has been casted ₹100 short, the Sales Account has been similarly credited ₹100 short. The correcting entry is to credit the Sales Account by ₹100 as "By wrong totalling of the Sales Book ₹100".

- (b) To rectify the omission, the Returns Inwards Account has to be debited and the account of Green & Co. credited. The entry:

Returns Inward Account To Green & Co. (Goods returned by the firm, previously omitted from the Returns Inward Book)	Dr.	₹150	₹150
---	-----	------	------

- (c) Gupta & Co. have been debited ₹250 instead of being credited. This account should now be credited by 500 to remove the wrong debit and to give the correct credit. The entry will be on the credit side... "By errors in posting ₹500".
- (d) By this error Purchases Account has to be debited by ₹1,000 whereas the debit should have been to the Furniture Account. The correcting entry will be:

Furniture Account To Purchases Account (Correction of the mistake by which of the Furniture Account)	Dr.	₹1,000	₹1,000
--	-----	--------	--------

- (e) The discount of ₹15 received from Red & Black should have been entered on the credit side of the cash book. Had this been done, the Discount Account would have been credited (through the total of the discount column) and Red & Black would have been debited. This entry should not be made:

Red & Black To Discount Account (Rectification of the error by which the discount allowed by the firm was not entered in Cash Book)	Dr.	₹15	₹15
---	-----	-----	-----

- (f) In this case the account of the customer has been correctly posted; the Discount Account has been debited ₹18 short since it has been omitted from the discount column on the debit side of the cash book. The discount account should now be debited by the entry; "To Omission of entry in the Cash Book ₹18."

***If a Suspense Account is opened :***

	Particulars	Dr.(₹)	Cr.(₹)
(a)	Suspense Account To Sales Account (Being the correction arising from under- casting of Sales Day Book)	100	100

(b)	Return Inward Account To Green & Co (Being the recording of unrecorded returns)	150	150
(c)	Suspense Account To Gupta & Co. (Being the correction of the error by which Gupta & Co. was debited instead of being credited by ₹ 250).	500	500
(d)	Furniture Account To Purchases Account (Being the correction of recording purchase of furniture as ordinary purchases)	1,000	1,000
(e)	Red & black To Discount Account (Being the recording of discount omitted to be recorded)	15	15
(f)	Discount Account To Suspense Account (Being the correction of omission of the discount allowed from Cash Book customer's account already posted correctly).	18	18

### Suspense Account

Dr. Date	Particulars	Amount ₹	Date	Particulars	Cr. Amount ₹
	To Sales A/c	100		By Difference in Trial Balance	582
	To Gupta & Co.	500		By Discount A/c	18
		600			600

#### Notes:

- (i) One should note that the opening balance in the Suspense Account will be equal to the difference in the trial balance.
- (ii) If the question is silent as to whether a Suspense Account has been opened, the student should make his assumption, state it clearly and then proceed.



(c)	Furniture Account To Purchases Account (Being the rectification of mistake by which purchase of furniture was entered in Purchases book and hence now corrected by crediting the Purchases Account)	Dr.	300	300
(d)	Furniture Account To Wages Account (Being the wages paid to workmen for making show-cases which should have been capitalised and not to be charged to Wages Account)	Dr.	375	375
(e)	Suspense Account To Creditors (personal) Account (Being the mistake in crediting the Trade payables Account less by ₹ 7, now corrected)	Dr.	7	7
(f)	P.C. Joshi To Allowances Account (Being the cheque of P.C. Joshi dishonoured, previously debited to Allowances Account)	Dr.	200	200
(g)	Drawings Account To Miscellaneous Expenses (Being the motor cycle purchased for Mr. Dutt debited to his Drawings Account instead of Miscellaneous Expenses Account as previously done by mistake)	Dr.	1,000	1,000
(h)	Returns Inward Account To Debtors (Personal) Account (Correction of the omission to record return of goods by customers)	Dr.	100	100
(i)	Singh & Co. To Suspense Account (Being the correction of mistake by which the account of Singh & Co. was credited by ₹ 200 instead of being debited)	Dr.	400	400

## Suspense Account

Dr.					Cr.
Date	Particulars	Amount	Date	Particulars	Amount
2022		₹	2022		₹
Dec.31	To Difference in Trial Balance	493	Dec. 31	By Returns Inwards A/c	100
" "	To Trade Payables A/c	<u>7</u>	" "	By Singh & Co.	<u>400</u>
		500			500

## ILLUSTRATION 6

The following errors, affecting the account for the year 2022 were detected in the books of Jain Brothers, Delhi:

- (1) Sale of old Furniture ₹ 150 treated as sale of goods.
- (2) Receipt of ₹ 500 from Ram Mohan credited to Shyam Sunder.
- (3) Goods worth ₹ 100 brought from Mohan Narain have remained unrecorded so far.
- (4) A return of ₹ 120 from Mukesh posted to his debit.
- (5) A return of ₹ 90 to Shyam Sunder posted as ₹ 9 in his account.
- (6) Rent of proprietor's residence, ₹ 600 debited to rent A/c.
- (7) A payment of ₹ 215 to Mohammad Sadiq posted to his credit as ₹ 125.
- (8) Sales Book casted short by ₹ 900 .
- (9) The total of Bills Receivable Book ₹ 1,500 left unposted.

You are required to pass the necessary rectifying entries and show how the trial balance would be affected by the errors.

## SOLUTION

## Journal

	Particulars	L.F.	Dr. Amount ₹	Cr. Amount ₹
(1)	Sales Account To Furniture Account (Rectification of sales of furniture treated as sales of goods)	Dr.	150	150

(2)	Shyam Sunder To Rama Mohan (Rectification of a receipt from Ram Mohan credited to Shyam Sunder)	Dr.		500	500
(3)	Purchases Account To Mohan Narain (Purchases of goods from Mohan Narain unrecorded, now corrected)	Dr.		100	100
(6)	Drawing Account To Rent Account (Rectification of Payment of rent of proprietor's residence treated as payment of office rent)	Dr.		600	600

**N.B. :** For 4, 5, 7, 8, 9 no journal entry can be passed as they affect a single account. The correction will be as under:

- (4) Credit Mukesh's Account with ₹ 240.
- (5) Debit the account of Shyam Sunder by ₹ 81.
- (7) Debit the account of Mohammad Sadiq by ₹ 340.
- (8) Credit Sales Account by ₹ 900.
- (9) Debit Bills Receivable Account with ₹ 1,500.

Effect of the Errors on Trial Balance

1. No effect
2. No effect
3. No effect
4. Trial Balance credit total short by                    ₹     240.
5. Trial Balance debit total short by                    ₹     81.
6. No effect
7. Trial Balance debit total short by                    ₹     340.
8. Trial Balance credit total short by                    ₹     900.
9. Trial Balance debit total short by                    ₹    1,500.

**ILLUSTRATION 7**

Write out the Journal Entries to rectify the following errors, using a Suspense Account.

- (1) Goods of the value of ₹ 100 returned by Mr. Sharma were entered in the Sales Day Book and posted therefrom to the credit of his account;
- (2) An amount of ₹150 entered in the Sales Returns Book, has been posted to the debit of Mr. Philip, who returned the goods;
- (3) A sale of ₹ 200 made to Mr. Ghanshyam was correctly entered in the Sales Day Book but wrongly posted to the debit of Mr. Radheshyam as ₹ 20; and
- (4) The total of "Discount Allowed" column in the Cash Book for the month of September, 2022 amounting to ₹ 250 was not posted.

**SOLUTION****Journal**

	Particulars		L.F.	Dr. ₹	Cr. ₹
(1)	Sales Account Sales Returns Account To Suspense Account (The value of goods returned by Mr. Sharma wrongly posted to Sales and omission of debit to Sales Returns Account, now rectified)	Dr. Dr.		100 100	200
(2)	Suspense Account To Mr. Philip (Wrong debit to Mr. Philip for goods returned by him, now rectified)	Dr.		300	300
(3)	Mr. Ghanshyam To Mr. Radheshyam To Suspense Account (Omission of debit to Mr. Ghanshyam and wrong credit to Mr. Radhesham for sale of ₹ 200, now rectified)	Dr.		200	20 180
(4)	Discount Account To Suspense Account (The total of Discount allowed during September, 2022 not posted from the Cash Book; error now rectified)	Dr.		250	250

### 6.5.3 Correction in the next Accounting Period

Rectification of errors discussed so far assumes that it was carried out before the books were closed for the concerned year. However, sometimes, the rectification is carried out in the next year, carrying forward the balance in the Suspense Account or even transferring it to the Capital Account. Suppose, the Purchase Book was cast short by ₹1,000 in December, 2022 and a Suspense Account was opened with the difference in the trial balance. If the error is rectified next year and the entry passed is to debit Purchase Account (and credit Suspense Account), it will mean that the Purchases Account for year 2023 will be ₹1,000 more than the amount relating to year 2023 and thus the profit for year 2023 will be less than the actual for that year. Thus, correction of errors in this manner will 'falsify' the Profit and Loss Account.

To avoid this, correction of all amounts concerning nominal accounts, i.e., expenses and incomes should be through a special account styled as "Prior Period Items" or "Profit and Loss Adjustment Account". The balance in the account should be transferred to the Profit and Loss Account. However, these Prior Period Items should be charged after deriving the profit of the current year. 'Prior Period items' are material income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more prior periods. Prior Period Items should be separately disclosed in the current statement of profit and loss together with their nature and amount in a manner that their impact on current period profit or loss can be perceived.

#### ILLUSTRATION 8

*Mr. Roy was unable to agree the Trial Balance last year and wrote off the difference to the Profit and Loss Account of that year. Next Year, he appointed a Chartered Accountant who examined the old books and found the following mistakes:*

- (1) *Purchase of a scooter was debited to conveyance account ₹3,000.*
- (2) *Purchase account was over-cast by ₹10,000.*
- (3) *A credit purchase of goods from Mr. P for ₹2,000 was entered as a sale.*
- (4) *Receipt of cash from Mr. A was posted to the account of Mr. B ₹1,000.*
- (5) *Receipt of cash from Mr. C was posted to the debit of his account, ₹500.*
- (6) *₹500 due by Mr. Q was omitted to be taken to the trial balance.*
- (7) *Sale of goods to Mr. R for ₹2,000 was omitted to be recorded.*
- (8) *Amount of ₹2,395 of purchase was wrongly posted as ₹2,593.*

*Mr. Roy used 10% depreciation on vehicles. Suggest the necessary rectification entries.*

## SOLUTION

## Journal Entries in the books of Mr. Roy

Sr. No.	Particulars	Dr.(₹)	Cr.(₹)
(1)	Motor Vehicles Account To Profit and Loss Adjustment A/c (Purchase of scooter wrongly debited to conveyance account now rectified-capitalisation of ₹ 2,700, i.e., ₹ 3,000 less 10% depreciation)	2,700	2,700
(2)	Suspense Account To Profit & Loss Adjustment A/c (Purchase Account overcast in the previous year; error now rectified).	10,000	10,000
(3)	Profit & Loss Adjustment A/c To P's Account (Credit purchase from P ₹ 2,000, entered as sales last year; now rectified)	4,000	4,000
(4)	B's Account To A's Account (Amount received from A wrongly posted to the account of B; now rectified)	1,000	1,000
(5)	Suspense Account To C's Account (₹ 500 received from C wrongly debited to his account; now rectified)	1,000	1,000
(6)	Trade receivables To Suspense Account (₹ 500 due by Q not taken into trial balance; now rectified)	500	500
(7)	R's Account To Profit & Loss Adjustment A/c (Sales to R omitted last year; now recorded)	2,000	2,000

(8)	Suspense Account To Profit & Loss Adjustment A/c (Excess posting to purchase account last year, ₹ 2,593, instead of ₹ 2,395, now adjusted)	198	198
(9)	Profit & Loss Adjustment A/c To Roy's Capital Account (Balance of Profit & Loss Adjustment A/c transferred to Capital Account)	10,898	10,898
(10)	Roy's Capital Account To Suspense Account (Balance of Suspense Account transferred to the Capital Account)	10,698	10,698

**Note :** Entries No. (2) and (8) may even be omitted; but this is not advocated.

### Profit and Loss Adjustment Account

(Prior Period Items)

	₹		₹
To P	4,000	By Motor Vehicles A/c	2,700
To Roy's Capital (transfer)	10,898	By Suspense A/c	10,000
		By R	2,000
		By Suspense Account	198
	14,898		14,898

### Suspense Account

	₹		₹
To Profit & Loss Adjustment A/c	10,000	By Trade Receivables (Q)	500
To C	1,000	By Roy's Capital A/c (Transfer)	10,698
To Profit & Loss Adjustment A/c	198		
	11,198		11,198

## SUMMARY

- ◆ Unintentional omission or commission of amounts and accounts in the process of recording the transactions are commonly known as errors.
- ◆ Accounting errors are generally of four types-
  - (a) Errors of Principle;
  - (b) Errors of Omission;
  - (c) Errors of Commission;
  - (d) Compensating Errors.
- ◆ Some errors may affect the Trial Balance and some of these do not.
- ◆ The method of rectification of errors depends on the stage at which the errors are detected. If the error is detected before the preparation of trial balance, rectification is carried out by making the statement in the appropriate side of the concerned account.
- ◆ In case of the errors detected after the preparation of the trial balance, we open a suspense account with the amount of difference in the trial balance. Then complete journal entries can be passed for rectifying the errors.
- ◆ For rectifying the errors detected in the next accounting period, a special account 'Profit and Loss Adjustment Account' is opened for correction of amounts relating to expenses and incomes.

## TEST YOUR KNOWLEDGE

### True and False

1. *The method of rectification of errors depends on the stage at which the errors are detected.*
2. *In case of error of complete omission, the trial balance does not tally.*
3. *When errors are detected after preparation of trial balance, suspense account is opened.*
4. *When purchase of an asset is treated as an expense, it is known as error of principle.*
5. *Trial balance agrees in case of compensating errors.*
6. *When amount is written on wrong side, it is known as an error of principle.*
7. *On purchase of old furniture, the amount spent on repairs should be debited to repairs account.*

8. *'Profit & Loss adjustment account' is opened to rectify the errors detected in the current accounting period.*
9. *Rent paid to landlord of the proprietors house, must be debited to 'Rent account'.*
10. *If the errors are detected after preparing trial balance, then all the errors are rectified through suspense account.*

### Multiple Choice Questions

1. *Goods purchased from A for ₹10,000 passed through the sales book. The error will result in*
  - (a) *Increase in gross profit.*
  - (b) *Decrease in gross profit.*
  - (c) *No effect on gross profit.*
2. *If a purchase return of ₹1,000 has been wrongly posted to the debit of the sales returns account, but has been correctly entered in the suppliers' account, the total of the*
  - (a) *Trial balance would show the debit side to be ₹1,000 more than the credit.*
  - (b) *Trial balance would show the credit side to be ₹ 1,000 more than the debit.*
  - (c) *The debit side of the trial balance will be ₹ 2,000 more than the credit side.*
3. *If the amount is posted in the wrong account or it is written on the wrong side of the account, it is called*
  - (a) *Error of omission.*
  - (b) *Error of commission.*
  - (c) *Error of principle.*
4. *₹ 200 paid as wages for erecting a machine should be debited to*
  - (a) *Repair account.*
  - (b) *Machine account.*
  - (c) *Capital account.*
5. *On purchase of old furniture, the amount of ₹1,000 spent on its repair should be debited to*
  - (a) *Repair account.*
  - (b) *Furniture account.*
  - (c) *Cash account.*

6. Goods worth ₹50 given as charity should be credited to
  - (a) Charity account.
  - (b) Sales account.
  - (c) Purchase account.
7. Goods worth ₹100 taken by proprietor for domestic use should be credited to
  - (a) Sales account.
  - (b) Proprietor's personal expenses.
  - (c) Purchases account.
8. Sales of office furniture should be credited to
  - (a) Sales Account.
  - (b) Furniture Account.
  - (c) Purchase Account.
9. The preparation of a trial balance is for:
  - (a) Locating errors of commission.
  - (b) Locating errors of principle.
  - (c) Locating clerical errors.
10. ₹ 200 received from Smith whose account, was written off as a bad debt should be credited to:
  - (a) Bad Debts Recovered account.
  - (b) Smith's account.
  - (c) Cash account.
11. Purchase of office furniture ₹1,200 has been debited to General Expense Account. It is:
  - (a) A clerical error.
  - (b) An error of principle.
  - (c) An error of omission.

### Theory Questions

1. How does errors of omission differ from errors of commission?
2. What is error of principle and how does it affect Trial Balance?
3. When and how is Suspense account used to rectify errors?

### Practical Questions

1. The trial balance of Mr. W & H failed to agree and the difference ₹20,570 was put into suspense account pending the investigation which disclosed that:
- (i) Purchase returns day book had been correctly entered and totalled at ₹6,160, but had not been posted to the ledger.
  - (ii) Discounts received ₹1,320 had been debited to discounts allowed.
  - (iii) The Sales account had been under added by ₹10,000.
  - (iv) A credit sale of ₹1,470 had been debited to a customer account at ₹1,740.
  - (v) A vehicle bought originally for ₹7,000 four years ago and depreciated to ₹1,200 had been sold for ₹1,500 in the beginning of the year but no entries, other than in the bank account had been passed through the books.
  - (vi) An accrual of ₹560 for telephone charges had been completely omitted.
  - (vii) A bad debt of ₹1,560 had not been written off and provision for doubtful debts should have been maintained at 10% of Trade receivables which are shown in the trial balance at ₹23,390 with a credit provision for bad debts at ₹2,320.
  - (viii) Tools bought for ₹1,200 had been inadvertently debited to purchases.
  - (ix) The proprietor had withdrawn, for personal use, goods worth ₹1,960. No entries had been made in the books.

You are required to give rectification entries without narration to correct the above errors before preparing annual accounts and also prepare suspense account.

2. On going through the Trial balance of Ball Bearings Co. Ltd. you find that the debit is in excess by ₹150. This was credited to "Suspense Account". On a close scrutiny of the books, the following mistakes were noticed:
- (1) The totals of debit side of "Expenses Account" have been casted in excess by ₹50.
  - (2) The "Sales Account" has been totalled in short by ₹100.
  - (3) Supplier account has been overcast by 225.
  - (4) The sale return of ₹100 from a party has not been posted to that account though the Party's account has been credited.
  - (5) A cheque of ₹500 issued to the Suppliers' account (shown under Trade payables) towards his dues has been wrongly debited to the purchases.
  - (6) A credit sale of ₹50 has been credited to the Sales and also to the Trade receivables Account.

You are required to

- (i) Pass necessary journal entries for correcting the above;
  - (ii) Show how they affect the Profits; and
  - (iii) Prepare the "Suspense Account" as it would appear in the ledger.
3. Mr. A closed his books of account on September 30, 2021 in spite of a difference in the trial balance. The difference was ₹830 the credits being short; it was carried forward in a Suspense Account. In 2022 following errors were located:
- (i) A sale of ₹2,300 to Mr. Lala was posted to the credit of Mrs. Mala.
  - (ii) The total of the Returns Inward Book for July, 2021 ₹1,240 was not posted in the ledger.
  - (iii) Freight paid on a machine ₹5,600 was posted to the Freight Account as ₹6,500. 10% Depreciation is charge on this machines.
  - (iv) While carrying forward the total in the Purchases Account to the next page, ₹65,590 was written instead of ₹56,950.
  - (v) A sale of machine on credit to Mr. Mehta for ₹9,000 on 30th sept. 2021 was not entered in the books at all. The book value of the machine was ₹6,750.

Pass journal entries to rectify the errors. Have you any comments to make?

4. A merchant's trial balance as on June 30, 2022 did not agree. The difference was put to a Suspense Account. During the next trading period, the following errors were discovered:
- (i) The total of the Purchases Book of one page, ₹4,539 was carried forward to the next page as ₹4,593.
  - (ii) A sale of ₹573 was entered in the Sales Book as ₹753 and posted to the credit of the customer.
  - (iii) A return to a creditor, ₹510 was entered in the Returns Inward Book; however, the creditor's account was correctly posted.
  - (iv) Cash received from C. Dass, ₹620 was posted to the debit of G. Dass.
  - (v) Goods worth ₹840 were despatched to a customer before the close of the year but no invoice was made out.
  - (vi) Goods worth ₹1,000 were sent on sale or return basis to a customer and entered in the Sales Book. At the close of the year, the customer still had the option to return the goods. The sale price was 25% above cost.

You are required to give journal entries to rectify the errors in a way so as to show the current year's profit or loss correctly.

5. The following errors were committed by the Accountant of Geete Dye-Chem.
- (i) Credit sale of ₹ 400 to Trivedi & Co. was posted to the credit of their account.
  - (ii) Purchase of ₹ 420 from Mantri & Co. passed through Sales Day Book as ₹ 240
- How would you rectify the errors assuming that :
- (a) they were detected before preparation of Trial Balance.
  - (b) they were detected after preparation of Trial Balance but before preparing Final Accounts, the difference was taken to Suspense A/c.
  - (c) they were detected after preparing Final Accounts

## ANSWERS/HINTS

### True and False

1. True: There are 3 different stages when the mistakes are identified and then the rectification depends on the stage of identification of errors.
2. False: In case of error of complete omission, the trial balance tallies.
3. True: In order to balance the difference of balances in the trial balance suspense account is opened.
4. True: Where the accounts being debited is principally incorrect it is termed as error of principle.
5. True: Compensating errors cancel out each other when Trial balance is prepared as the mistake pertains to the same amount being credited and later debited on account of two different mistakes.
6. False: When amount is written on wrong side, it is known as an error of commission.
7. False: On purchase of furniture, the amount spent on repairs should be debited to furniture account as it is a capital expense.
8. False: 'Profit & Loss adjustment account' is opened to rectify the errors detected in the next accounting period.
9. False: Rent paid to land lord of the proprietors house, must be debited to 'Drawings account'.
10. False: If the errors are detected after preparing trial balance, then all the errors are not rectified through suspense account. There may be principal errors, which can be rectified without opening a suspense account.

## Multiple Choice Questions

1.	(a)	2.	(c)	3.	(b)	4.	(b)	5.	(b)	6.	(c)
7.	(c)	8.	(b)	9.	(c)	10.	(a)	11.	(b)		

## Theoretical Questions

- Errors of Omission: If a transaction is completely or partially omitted from the books of account, it will be a case of omission. Examples would be: not recording a credit purchase of furniture or not posting an entry into the ledger.
  - Errors of Commission: If an amount is posted in the wrong account or it is written on the wrong side or the totals are wrong or a wrong balance is struck, it will be a case of "errors of commission."
- Errors of principle:** When a transaction is recorded in contravention of accounting principles, like treating the purchase of an asset as an expense, it is an error of principle. In this case there is no effect on the trial balance since the amounts are placed on the correct side, though in a wrong account. Suppose on the purchase of a typewriter, the office expenses account is debited; the trial balance will still agree.

The method of correction of error indicated so far is appropriate when the errors have been located before the end of the accounting period. After the corrections, the trial balance will agree. Sometimes the trial balance is artificially made to agree in spite of errors by **opening a suspense account** and putting the difference in the trial balance to the account - the suspense account will be debited if the total of the credit column in the trial balance exceeds the total of the debit column; it will be credited in the other case. Each and every error detected after preparation of trial balance can only be corrected by a complete journal entry. Those errors for which journal entries were not possible at the earlier stage will now be rectified by a journal entry(s), the difference or the unknown side is being taken care of by suspense account. Those errors for which entries were possible even at the first stage will now be rectified in the same way.

## Practical Questions

1.

	Particulars	Dr.	Cr.
(i)	Suspense Account	6,160	
	To Return Outward A/c		6,160
(ii)	Suspense Account	2,640	

	To Discount Allowed Account		1,320
	To Discount Received Account		1,320
(iii)	Suspense Account	10,000	
	To Sales Account		10,000
(iv)	Suspense Account	270	
	To Trade Receivable Account		270
(v)	Suspense Account	1,500	
	To Vehicle Account		1,200
	To Profit on Sale of Vehicle Account		300
(vi)	Telephone Charges Account	560	
	To Outstanding Expenses Account		560
(vii)	Bad Debts Account (refer W.N 1)	1,560	
	To Trade Receivables Account		1,560
	Provision for Doubtful Debts Account (refer W.N. 2)	1,396	
	To Profit and Loss Account		1,396
(viii)	Loose Tools Account	1,200	
	To Purchases Account		1,200
(ix)	Drawings Account	1,960	
	To Purchases Account		1,960

### Suspense Account

	₹		₹
To Return outward Account	6,160	By balance b/d	20,570
To Discount allowed Account	1,320		
To Discount Received Account	1,320		
To Sales Account	10,000		
To Customers Account	270		
To Vehicles Account	1,200		
To Profit on Sale of Vehicle	300		
	20,570		20,570

### Working Notes :

(i)	Balance of Trail Balance for Computation of Provision for Doubtful Debts		
	Trade receivables as per books		23,390

	Deduction vide item (iv)	270	
	Bad Debts	<u>1,560</u>	<u>1,830</u>
			<u>21,560</u>
(ii)	Amount Charge to Profit & Loss on Account of Provision for Doubtful Debts		
	Opening of Provision for Doubtful Debts		2,320
	Less: Bad debts		1,560
			760
	Closing Balance of Provision for Doubtful Debts		2,156
	Charge to Profit and Loss A/c		1,396

2.

**Journal Entries**

Particulars		L.F.	Dr. ₹	Cr. ₹
Suspense Account To Expenses Account (Being the mistake in totalling of Expenses Account, rectified)	Dr.		50	50
Suspense Account To Sales Account (Being the mistake in totalling of Sales Accounts rectified)	Dr.		100	100
Supplier To Suspense Account (Being the mistake in posting from Day Book to Ledger rectified)	Dr.		225	225
Sales Returns Account To Suspense Account (Being the sales return from a party not posted to "Sales Returns" now rectified)	Dr.		100	100
Trade payables Account To Purchases Account	Dr.		500	500

(Being the payments made to supplier wrongly posted to purchases now rectified)				
Trade receivables Account	Dr.		100	
To Suspense Account				100
(Being the sales wrongly credited to Customer's Account now rectified)				

### Suspense Account

	Dr. ₹		Cr. ₹
To Expenses Account	50	By Difference in Trial Balance	150
To Sales Account	100	By Trade payables	225
To Balance c/d	425	By Sales Returns Account	100
		By Trade receivables	100
	575		575
		By Balance b/d	425

Since the Suspense Account does not balance, it is clear that all the errors have not been traced. As a result of the above corrections the Net Profit will be:

	Increased by ₹	Decreased by ₹
Mistake in totalling in "Expenses"	50	
Mistake in totalling in "Sales"	100	
Mistake in posting from day book to Ledger under "Purchases"	500	
Omission in posting under "Sales Returns"		100
	650	100
Net Increase	550	

As a result of these adjustments, the Profits will be increased by ₹550.

3.

## Journal of Mr. A

Date	Particulars	Dr.	Cr.
		₹	₹
2022 (i)	Mrs. Mala Mr. Lala To Suspense A/c (Correction of error by which a sale of ₹ 2,300 to Mr. Lala was posted to the credit of Mrs. Mala)	2,300 2,300	4,600
(ii)	Profit and Loss Adjustment A/c To Suspense A/c (Rectification of omission to post the total of Returns Inward Book for July, 2021)	1,240	1,240
(iii)	(a) Machinery A/c Suspense A/c To Profit & Loss Adjustment A/c (Correction of error by which freight paid for a machine ₹ 5,600 was posted to Freight Account at ₹ 6,500 instead of capitalising it)	5,600 900	6,500
	(b) Profit & Loss Adjustment A/c To Plant and Machinery A/c (Depreciation @ 10% charged on freight paid on a machine capitalised)	560	560
(iv)	Suspense A/c To Profit & Loss Adjustment A/c (Correction of wrong carry forward of total in the purchase Account to the next page ₹ 65,590 instead of ₹ 56,950)	8,640	8,640
(v)	Mr. Mehta To Plant & Machinery A/c To Profit & Loss Adjustment A/c (Correction of omission of a sale of machine on credit to Mr. Mehta for ₹ 9,000 )	9,000	6,750 2,250

**Comments**

The Suspense Account will now appear as shown below:

**Suspense Account**

Date	Particulars	Dr. Amount ₹	Date	Particulars	Cr. Amount ₹
2022	To Profit and Loss Adjustment A/c	900	2022 Oct. 1	By Balance b/d	830
	To Profit and Loss Adjustment A/c	8,640		By Sundries Mrs. Mala	2,300
				Mr. Lala	2,300
				By Profit and Loss Adjustment A/c	1,240
				By balance c/d	2,870
		9,540			9,540

Since the Suspense Account still shows a balance, it is obvious that there are still some errors left in the books.

**Profit & Loss Adjustment A/c****(For Prior Period Items)**

Date 2022	Particulars	Dr. Amount ₹	Date 2022	Particulars	Cr. Amount ₹
	To Suspense A/c	1,240		By Machinery A/c	5,600
	To Plant and Machinery A/c	560		By Suspense A/c	900
	To Balance c/d	15,590		By Suspense A/c	8,640
				By Mr. Mehta	2,250
		17,390			17,390

4.

## Journal Entries

	Particulars	Dr. ₹	Cr. ₹
(i)	Suspense Account Dr. To Profit and Loss Adjustment A/c (Correction of error by which Purchase Account was over debited last year- ₹4,593 carried forward instead of ₹4,539)	54	54
(ii)	Profit & Loss Adjustment A/c Dr. Customer's Account Dr. To Suspense Account (Correction of the entry by which (a) Sales A/c was over credited by ₹180 (b) customer was credited by ₹753 instead of being debited by ₹573)	180 1,326	1,506
(iii)	Suspense Account Dr. To Profit & Loss Adjustment A/c (Correction of error by which Returns Inward Account was debited by ₹510 instead of Returns Outwards Account being credited by ₹ 510)	1,020	1,020
(iv)	Suspense Account Dr. To C. Dass To G. Dass (Removal or wrong debit to G. Dass and giving credit to C. Dass from whom cash was received).	1,240	620 620
(v)	Customer's Account Dr. To Profit & Loss Adjustment A/c (Rectification of the error arising from non-preparation of invoice for goods delivered)	840	840
(vi)	Profit & Loss Adjustment A/c Dr. Inventory Account Dr.	200 800	

	To Customer's Account (The Customer's A/c credited with ₹ 1,000 for goods not yet purchased by him; cost of the goods debited to inventory and "Profit" debited to Profit & Loss Adjustment Account)		1,000
(vii)	Profit & Loss Adjustment A/c To Capital Account (Transfer of Profit & Loss Adjustment A/c balance to the Capital Account)	Dr. 1,534	1,534

5. (b) (i) This is one sided error. Trivedi & Co. account is credited instead of debit. Amount posted to the wrong side and therefore while rectifying the account, double the amount (₹ 800) will be taken.

Before Trial Balance	After Trial Balance	After Final Accounts
No Entry Debit Trivedi A/c with ₹ 800	Trivedi & Co. A/c Dr. 800 To Suspense A/c 800	Trivedi & Co. A/c Dr. 800 To Suspense A/c 800

- (ii) Purchase of ₹ 420 is wrongly recorded through sales day book as ₹ 240.

Correct Entry	Entry Made Wrongly
Purchase A/c Dr. 420 To Mantri & Co. 420	Mantri & Co. Dr. 240 To Sales 240

#### Rectification Entry

Before Trial Balance	After Trial Balance	After Final Accounts
Sales A/c Dr. 240 Purchase A/c Dr. 420 To Mantri & Co. 660	Sales A/c Dr. 240 Purchase A/c Dr. 420 To Mantri & Co. 660	Profit & Loss Adj. A/c Dr.660 To Mantri & Co. 660