

UNIT - III

FINAL ACCOUNTS OF SOLE TRADERS

Introduction :

A Trial Balance marks a definite stage in the preparation of accounts. It indicates that all the transaction for a particular period has been duly entered, posted and balanced. But this it self is not the end of book-keeping work. Its a means to an end, the end being a. to find out the profit or loss made by the business firm in given period and b. to understand the financial position of the business as on a given date. A business man can ascertain these by preparing the final accounts, which is prepared on the basis of the trial balance. The Preparation of final accounts is the last step in the accounting circle. The final account includes manufacturing account, trading accounts, profit and loss account and balance sheet. Even though the balance sheet is a statement, for all practical purposes, it is treated as part of final accounts. We are concerned with trading and profit and loss account and balance sheet and the same are discussed in this chapter.

Trading Account :

Trading account is prepared mainly to know the profitability of goods bought or manufacture and sold by the business man. The difference between the selling price and cost price of the goods is the gross result. The term 'Goods' means the goods bought for resale. It does not include assets. If sale proceeds are more than the cost of goods sold, gross profit is made. If sale proceeds are less than the cost of the goods sold, gross loss is incurred.

Format:

Trading Account for the year ended on 31st December				
Dr.	Rs.	Cr.	Rs.	
To Opening Stock		By Sales less Return		
To Purchases less Returns		By Closing Stock		
To Wages				
To Freight Charges				
To Dock Charges				
To Excise Duty				
To Octroi				
To Import duty				
To Fuel, Power etc.				
To Store Consumed --				
To Royalty Production Basis.				
To Manufacturing expenses				
To Gross Profit				
	-----		-----	
	-----		-----	

Manufacturing Account :

A business man purchases finished goods for resale where as a manufacturer buys raw materials, converts them in to finished goods, by incurring certain expenses, and then sells them. Thus, Trading Account is splitted into two-Manufacturing Account and Trading Account.

Manufacturing account is the account to show the cost of manufacture or production. On the debit side, opening stock of raw materials, work-in-process, purchase of raw materials, carriage, manufacturing expenses and all other expenses relating to factory are entered. On the credit side, closing stock of raw materials, work-in-process, are shown and the balance, representing the cost of production of finished goods, is transferred to Trading Account. If one wants to know the cost of manufacturing, then as Manufacturing Account- will have to be prepared.

Profit and Loss Account :

By preparing the Trading Account, its possible to find out the Gross Profit or Gross Loss made during the given period. The next step is the preparation of the Profit and Loss Account to ascertain net profit earned or net lost suffered during a given period of time. The balance of Trading Account is brought down to Profit and Loss Account. Then, the Profit and Loss Account is credited with other incomes and debited with all indirect expenses. Then the Profit and Loss Account may be balance and the balance is Net Profit or Not Loss. to be transferred to capital account, in case of sole trader or partnership firms.

Profit and Loss Account for the year ended 31 st December			
Dr.	Rs.	Cr.	Rs.
To Gross Loss		By Gross Profit	
To Management expenses		By Interest Received	
Office Salaries		By Discount Received	
Rent of Office Building		By Commission	
Office Lighting		By Income from Investment	
Office, Rent and Taxes		By Apprenticeship Premium	
Printing and Stationery		By Rent from tenants	
Telephone Charges		By Reserve for Disc. on Creditors	
Postage		By Interest on Renewal of Bills	
Legal Expenses		By Miscellaneous income	
Audit Fees		By Net Loss	
Insurance -			
General expenses etc.			
To Selling expenses :			
Salesman Salaries			
Traveling expenses			
Advertising			
Bad Debts			
Selling Commission			
Brokerage			
Free Samples			
To Distribution expenses :			
Carriage out			
Warehouse Rent			
Warehouse Insurance -			
Delivery Van expenses			
Packing expenses			
To Depreciation :			

Depreciation of Assets		
Maintenance expenses		
To Finance expenses :		
Discount Allowed		
Interest on Loan -		
Interest on Capital		
Discount on Bills		
Loss by Fire		
To Net Profit		
	-----	-----
-		
	-----	-----
-		

Balance Sheet:

A Balance Sheet is a statement of the financial position at a given date. The given date is the date at which the final accounts are prepared. Transactions are first recorded in journal. Entries in the journal are posted to ledgers. Ledger accounts are balanced and the balances are recorded in a Trial Balance. Trial Balance consists of all Accounts – Personal, Real and Nominal. From the Trial Balance, nominal accounts are transferred to Trading or Profit and Loss Account and the remaining balances are taken to Balance Sheet. However, Balance Sheet is a summary of whole of the accounting record. This is because the nominal accounts are transferred to Revenue Accounts, and Revenue account is closed by shifting the balance to the Balance Sheet. Balance Sheet is also known as a Statement of Assets and Liabilities. Balance sheet is the last and the most important link in the chain of Final Accounts and Statements. It describes the financial position of a business in a systematic standard form. It is a mirror of a business. When the assets exceed the liabilities, one can conclude that the business is sound and solvent. The function of the Balance Sheet is to show the picture of the business on a particular date.

Balance Sheet as on		
Liabilities	Rs.	Assets
Rs.		
Current liabilities		Liquid assets
Bills Payable		Cash in Hand
Sundry Creditors		Cash at Bank
Bank Overdraft		Cash in Transit
Long Term Liabilities		Floating Assets
Loan from Bank		Sundry Debtors
Fixed Liabilities		Deposits Investments
		Bills Receivable
		Stock in Trade
		Capital Prepaid expenses
		Fixed Assets
		Plant and Machinery
		Buildings
		Furniture & Fixtures
		Land
		Fictitious Assets

Advertisement
Miscellaneous expenses
Profit & Loss
Intangible Assets
Goodwill
Patents
Patterns
Copyright

Adjustments :

Following are the Adjustments that are to be considered while preparing final accounts. Each and every adjustment is to be posted in two places. The following is the summary of those two places for each adjustment.

1. Closing Stock.

- i. Trading Account Credit Side, show as an item.
- ii. Balance Sheet Assets Side, show as an item.

2. Depreciation

- i. Balance Sheet Assets Side, deduct from particular asset.
- ii. Profit and Loss Account debit side, show as an item.

3. Outstanding Expenses

- i. Profit and Loss Account Debit side, add with particular expense.
- ii. Balance Sheet Liabilities side show as an item.

4. Prepaid Expenses

- i. Profit and Loss Account Debit side, deduct from particular expense.
- ii. Balance Sheet Assets side, show as an item.

5. Accrued Income or Outstanding Income

- i. Profit and Loss Account Credit side, add with particular income.
- ii. Balance Sheet Assets side, show as an item.

6. Income Received in Advance

- i. Profit and Loss Account Credit side, deduct from particular income.
- ii. Balance Sheet Liabilities side, show as an item.

7. Interest on Capital

- i. Balance Sheet Liabilities side, add with capital.
- ii. Profit and Loss Account Debit side, show as an item.

8. Interest on Drawings

- i. Balance Sheet Liabilities Side, deduct from capital.
- ii. Profit and Loss Account Credit side, show as an item.

9. Interest on Loan

- i. Balance Sheet Liabilities side, add with Loan.
- ii. Profit and Loss Account Debit side, show as an item.

10. Interest on Investment

- i. Balance Sheet Assets Side.
- ii. Profit and Loss Account Credit side, show as an item.

11. Bad Debts

- i. Balance Sheet Assets side, deduct from sundry debtors.
- ii. Profit and Loss Account Debit side, show as an item.

12. Provision for Bad debts

- i. Balance Sheet Assets side, deduct from sundry debtors.
- ii. Profit and Loss Account Debit side, show as an item.

13. Provision for Discount on debtors

- i. Balance Sheet Assets side, deduct from sundry debtors.
- ii. Profit and Loss Account Debit side, show as an item.

14. Provision for discount on creditors

- i. Balance Sheet Liabilities side, deduct from sundry creditors.
- ii. Profit and Loss Account Credit side, show as an item.

15. Drawings of Goods by proprietor

- i. Balance Sheet Liabilities side, deduct from capital.
- ii. Trading Account Credit side, show as an item.

16. Free Samples to customers

- i. Trading Account Credit side, show as an item.
- ii. Profit and Loss Account Debit side, show as an item.

17. Loss of Stock

- i. Trading Account Credit side, show as an item.
- ii. Profit and Loss Account Debit side, show as an item.

18. Manager Commission

- i. Profit and Loss Account Debit side, show as an item.
- ii. Balance Sheet Liabilities side show as an item.

Note : While calculating manager commission on Net Profit or Gross Profit due consideration is to be given whether it is based on Profit before charging such commission or after charging such commission