तत् त्वं पूषन् अपावृणु
केन्द्रीय विद्यालय संगठन

INTERACTIVE STUDY MATERIAL

CLASS 11 COMMERCE

SESSION 2022-23

INSERVICE COURSE FOR PGT COMMERCE (2ND SPELL)

KVS ZIET CHANDIGARH

स्नातकोत्तर शिक्षक (वाणिज्य) हेतु सेवाकालीन प्रशिक्षण (द्वितीय चरण)

INSERVICE COURSE FOR PGT COMMERCE (SECOND SPELL)

23.12.2022-01.01.2023

श्री मुकेश कुमार / **SH. MUKESH KUMAR**

उपायुक्त एवं निदेशक जीट चंडीगढ़/

DC & DIRECTOR , ZIET CHANDIGARH

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पीजीटी वाणिज्य, / के वि बददोवाल छावनी

PGT COMMERCE KV BADDOWAL CANTT

संसाधिका / **RESOURCE PERSON**

श्रीमती अंशु सिंगला / **SMT ANSHU SINGLA**

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PGT COMM,KV SEC 47 CHD

संसधिका/ **RESOURCE PERSON**

प्रतिभागियों की सूची

क्रमांक	प्रतिभागी का नाम	पुरुष/ महिला	पद	विषय	केंद्रीय विद्यालय
1	श्री डी पी तिवारी	पुरुष	पीजीटी	वाणिज्य	क्रमांक 1 धनबाद
2	श्रीमती मोनिदीपा देब	महिला	पीजीटी	वाणिज्य	एन ऍफ़ आर मालीगांव
3	श्रीमती सुमन सिंह	महिला	पीजीटी	वाणिज्य	ए ऍफ़ एस मनौरी प्रयागराज
4	श्री रूम सिंह यादव	पुरुष	पीजीटी	वाणिज्य	क्रमांक 2 ओ सी ऍफ़ शाहजहांपुर
5	श्री आर के नागपाल	पुरुष	पीजीटी	वाणिज्य	ओक ग्रोव स्कूल , देहरादून

LIST OF PARTICIPANTS

S.No.	NAME OE THE PARTICIPANT	MALE / FEMALE	CADRE	SUBJECT	KENDRIYA VIDYALAYA
1	MR. D P TEWARY	Male	PGT	COMMERCE	DHANBAD NO.1
2	MRS. MONIDIPA DEB	FEMALE	PGT	COMMERCE	NFR MALIGAON
3	MRS. SUMAN SINGH	FEMALE	PGT	COMMERCE	AFS MANAURI PRAYAGRAJ
4	MR. ROOM SINGH YADAV	MALE	PGT	COMMERCE	NO.2 OCF SHAHJAHANPUR
5	MR. RK NAGPAL	MALE	PGT	COMMERCE	OAK GROVE SCHOOL, DEHRADUN

ACCOUNTANCY (Code No. 055)

Rationale

The course in accountancy is introduced at plus two stage of senior second of school education,
as the formal commerce education is provided after ten years of schooling. With the fast-changing economic scenario, accounting as a source of financial information has carved out a place for itself at the senior secondary stage. Its syllabus content provides students a firm foundation in basic accounting concepts and methodology and also acquaint them with the changes taking place in the preparation and presentation of financial statements in accordance to the applicable accounting standards and the Companies Act 2013. The course in accounting put emphasis on developing basic understanding about accounting as an information system. The emphasis in Class XI is placed on basic concepts and process of accounting leading to the preparation of accounts for a sole proprietorship firm. The students are also familiarized with basic calculations of Goods and Services Tax (GST) in recording the business transactions. The accounting treatment of GST is confined to the syllabus of class XI. The increased role of ICT in all walks of life cannot be overemphasized and is becoming an integral part of business operations. The learners of accounting are introduced to Computerized Accounting System at class XI and XII. Computerized Accounting System is a compulsory component which is to be studied by all students of commerce in class XI; whereas in class XII it is offered as an optional subject to Company Accounts and Analysis of Financial Statements. This course is developed to impart skills for designing need-based accounting database for maintaining book of accounts. The complete course of Accountancy at the senior secondary stage introduces the learners to the world of business and emphasize on strengthening the fundamentals of the subject.

Objectives:

1. To familiarize students with new and emerging areas in the preparation and presentation
of financial statements.
2. To acquaint students with basic accounting concepts and accounting standards.
3. To develop the skills of designing need-based accounting database.
4. To appreciate the role of ICT in business operations.
5. To develop an understanding about recording of business transactions and preparation of financial statements.
6. To enable students with accounting for Not-for-Profit organizations, accounting for Partnership Firms and company accounts.

Accountancy (Code No.055)

Course Structure

Class-XI (2022-23)

Theory: 80 Marks **3 Hours**

Project: 20 Marks

Units		Periods	Marks
Part A: Financial Accounting-1			
	Unit-1: Theoretical Framework	**25**	**12**
	Unit-2: Accounting Process	**115**	**44**
Part B: Financial Accounting-II			
	Unit-3: Financial Statements of Sole Proprietorship	**60**	**24**
Part C: Project Work		**20**	**20**

PART A: FINANCIAL ACCOUNTING - I

Unit-1: Theoretical Frame Work

Units/Topics	Learning Outcomes
Introduction to Accounting • Accounting- concept, meaning, as a source of information, objectives, advantages and limitations, types of accounting information; users of accounting information and their needs. Qualitative Characteristics of Accounting Information. Role of Accounting in Business. • Basic Accounting Terms- Entity, Business Transaction, Capital, Drawings. Liabilities (Non Current and Current). Assets (Non Current, Current); Expenditure (Capital and Revenue), Expense, Revenue, Income, Profit, Gain, Loss, Purchase, Sales, Goods, Stock, Debtor, Creditor, Voucher, Discount (Trade discount and Cash Discount) **Theory Base of Accounting** • Fundamental accounting assumptions: GAAP: Concept • Basic accounting concept : Business Entity,	**After going through this Unit, the students will be able to:** • describe the meaning, significance, objectives, advantages and limitations of accounting in the modem economic environment with varied types of business and non-business economic entities. • identify / recognise the individual(s) and entities that use accounting information for serving their needs of decision making. • explain the various terms used in accounting and differentiate between different related terms like current and non-current, capital and revenue. • give examples of terms like business transaction, liabilities, assets, expenditure and purchases. • explain that sales/purchases include both cash and credit sales/purchases relating to the accounting year.

Money Measurement, Going Concern, Accounting Period, Cost Concept, Dual Aspect, Revenue Recognition, Matching, Full Disclosure, Consistency, Conservatism, Materiality and Objectivity • System of Accounting. Basis of Accounting: cash basis and accrual basis • Accounting Standards: Applicability in IndAS • Goods and Services Tax (GST): Characteristics and Advantages.	• differentiate among income, profits and gains. • state the meaning of fundamental accounting assumptions and their relevance in accounting. • describe the meaning of accounting assumptions and the situation in which an assumption is applied during the accounting process. • explain the meaning, applicability, objectives, advantages and limitations of accounting standards. • appreciate that various accounting standards developed nationally and globally are in practice for bringing parity in the accounting treatment of different items. • acknowledge the fact that recording of accounting transactions follows double entry system. • explain the bases of recording accounting transaction and to appreciate that accrual basis is a better basis for depicting the correct financial position of an enterprise. • Explain the meaning, advantages and characteristic of GST.

Unit-2: Accounting Process

Units/Topics	Learning Outcomes
Recording of Business Transactions • Voucher and Transactions: Source documents and Vouchers, Preparation of Vouchers, Accounting Equation Approach: Meaning and Analysis, Rules of Debit and Credit. • Recording of Transactions: Books of Original Entry- Journal • Special Purpose books: • Cash Book: Simple, cash book with bank column and petty cashbook	**After going through this Unit, the students will be able to:** • explain the concept of accounting equation and appreciate that every transaction affects either both the sides of the equation or a positive effect on one item and a negative effect on another item on the same side of accounting equation. • explain the effect of a transaction (increase or decrease) on the assets, liabilities, capital, revenue and expenses.

• Purchases book • Sales book • Purchases return book • Sales return book • Journal proper ***Note: Including trade discount, freight and cartage expenses for simple GST calculation.*** • Ledger: Format, Posting from journal and subsidiary books, Balancing of accounts **Bank Reconciliation Statement:** • Need and preparation, Bank Reconciliation Statement **Depreciation, Provisions and Reserves** • Depreciation: Meaning, Features, Need, Causes, factors • Other similar terms: Depletion and Amortisation • Methods of Depreciation: i. Straight Line Method (SLM) ii. Written Down Value Method (WDV) ***Note: Excluding change of method*** • Difference between SLM and WDV; Advantages of SLM and WDV • Method of recoding depreciation i. Charging to asset account ii. Creating provision for depreciation/accumulated depreciation account • Treatment of disposal of asset • Provisions, Reserves, Difference Between Provisions and Reserves. • Types of Reserves: i. Revenue reserve ii. Capital reserve iii. General reserve iv. Specific reserve v. Secret Reserve • Difference between capital and revenue reserve	• appreciate that on the basis of source documents, accounting vouchers are prepared for recording transaction in the books of accounts. • develop the understanding of recording of transactions in journal and the skill of calculating GST. • explain the purpose of maintaining a Cash Book and develop the skill of preparing the format of different types of cash books and the method of recording cash transactions in Cash book. • describe the method of recording transactions other than cash transactions as per their nature in different subsidiary books . • appreciate that at times bank balance as indicated by cash book is different from the bank balance as shown by the pass book / bank statement and to reconcile both the balances, bank reconciliation statement is prepared. • develop understanding of preparing bank reconciliation statement. • appreciate that for ascertaining the position of individual accounts, transactions are posted from subsidiary books and journal proper into the concerned accounts in the ledger and develop the skill of ledger posting. • explain the necessity of providing depreciation and develop the skill of using different methods for computing depreciation. • understand the accounting treatment of providing depreciation directly to the concerned asset account or by creating provision for depreciation account. • appreciate the method of asset disposal through the concerned asset account or by preparing asset disposal account. • appreciate the need for creating reserves and

Trial balance and Rectification of Errors • Trial balance: objectives, meaning and preparation **(Scope:** *Trial balance with balance method only*) • Errors: classification-errors of omission, commission, principles, and compensating; their effect on Trial Balance. • Detection and rectification of errors; (i) Errors which do not affect trial balance (ii) Errors which affect trial balance • preparation of suspense account.	also making provisions for events which may belong to the current year but may happen in next year. • appreciate the difference between reserve and reserve fund. • state the need and objectives of preparing trial balance and develop the skill of preparing trial balance. • appreciate that errors may be committed during the process of accounting. • understand the meaning of different types of errors and their effect on trial balance. • develop the skill of identification and location of errors and their rectification and preparation of suspense account.

Part B: Financial Accounting - II

Unit 3: Financial Statements of Sole Proprietorship

Units/Topics	Learning Outcomes
Financial Statements Meaning, objectives and importance; Revenue and Capital Receipts; Revenue and Capital Expenditure; Deferred Revenue expenditure. Opening journal entry. Trading and Profit and Loss Account: Gross Profit, Operating profit and Net profit. Preparation. Balance Sheet: need, grouping and marshalling of assets and liabilities. Preparation. Adjustments in preparation of financial statements with respect to closing stock, outstanding expenses, prepaid expenses, accrued income, income received in advance, depreciation, bad debts, provision for doubtful debts, provision for discount on debtors, Abnormal loss, Goods taken for personal use/staff welfare, interest on capital and managers commission. Preparation of Trading and Profit and Loss account and Balance Sheet of a sole proprietorship with adjustments.	**After going through this Unit, the students will be able to:** • state the meaning of financial statements the • purpose of preparing financial statements. • state the meaning of gross profit, operating profit and net profit and develop the skill of preparing trading and profit and loss account. • explain the need for preparing balance sheet. • understand the technique of grouping and marshalling of assets and liabilities. • appreciate that there may be certain items other than those shown in trial balance which may need adjustments while preparing financial statements. • develop the understanding and skill to do adjustments for items and their presentation in financial statements like depreciation, closing stock, provisions, abnormal loss etc. • develop the skill of preparation of trading and profit and loss account and balance sheet.

PROJECT WORK

It is suggested to undertake this project after completing the unit on preparation of financial statements. The student(s) will be allowed to select any business of their choice or develop the transaction of imaginary business. The project is to run through the chapters and make the project an interesting process. The amounts should emerge as more realistic and closer to reality.

Specific Guidelines for Teachers

Give a list of options to the students to select a business form. You can add to the given list:

1. A beauty parlour
2. Men's saloon
3. A tailoring shop
4. A canteen
5. A cake shop
6. A confectionery shop
7. A chocolate shop
8. A dry cleaner
9. A stationery shop
10. Men's wear
11. Ladies wear
12. Kiddies wear
13. A Saree shop
14. Artificial jewellery shop
15. A small restaurant
16. A sweet shop
17. A grocery shop
18. A shoe shop
19. A coffee shop
20. A music shop
21. A juice shop
22. A school canteen
23. An ice cream parlour
24. A sandwich shop
25. A flower shop

After selection, advise the student(s) to visit a shop in the locality (this will help them to settle on a realistic amounts different items. The student(s) would be able to see the things as they need to invest in furniture, decor, lights, machines, computers etc.

A suggested list of different item is given below.

1. Rent
2. Advance rent [approximately three months]
3. Electricity deposit
4. Electricity bill
5. Electricity fitting
6. Water bill
7. Water connection security deposit
8. Water fittings
9. Telephone bill
10. Telephone security deposit
11. Telephone instrument
12. Furniture
13. Computers
14. Internet connection
15. Stationery
16. Advertisements
17. Glow sign
18. Rates and Taxes
19. Wages and Salary
20. Newspaper and magazines
21. Petty expenses
22. Tea expenses
23. Packaging expenses
24. Transport
25. Delivery cycle or a vehicle purchased
26. Registration
27. Insurance
28. Auditors fee
29. Repairs & Maintenance
30. Depreciations
31. Air conditioners
32. Fans and lights
33. Interior decorations
34. Refrigerators
35. Purchase and sales

At this stage, performas of bulk of originality and ledger may be provided to the students and they may be asked to complete the same.

In the next step the students are expected to prepare the trial balance and the financial statements.

Suggested Question Paper Design
Accountancy (Code No. 055)
Class XI (2022-23)

Theory: 80 Marks **3 hrs.**
Project: 20 Marks

S N	Typology of Questions	Marks	Percentage
1	**Remembering and Understanding**: Exhibit memory of previously learned material by recalling facts, terms, basic concepts, and answers. Demonstrate understanding of facts and ideas by organizing, comparing, translating, interpreting, giving descriptions, and stating main ideas	44	55%
3	**Applying**: Solve problems to new situations by applying acquired knowledge, facts, techniques and rules in a different way.	19	23.75%
4	**Analysing, Evaluating and Creating:** Examine and break information into parts by identifying motives or causes. Make inferences and find evidence to support generalizations. Present and defend opinions by making judgments about information, validity of ideas, or quality of work based on a set of criteria. Compile information together in a different way by combining elements in a new pattern or proposing alternative solutions.	17	21.25%
	TOTAL	**80**	**100%**

UNIT - I

THEORETICAL FRAME WORK

LEARNING OBJECTIVES:

The students will be able to:

1. describe the meaning, significance, objectives, advantages and limitations of accounting in the modem economic environment with varied types of business and non-business economic entities.
2. identify / recognise the individual(s) and entities that use accounting information for serving their needs of decision making.
3. explain the various terms used in accounting
4. differentiate between different related terms like current and non-current, capital and revenue.
5. give examples of terms like business transaction, liabilities, assets, expenditure and purchases.
6. explain that sales/purchases include both cash and credit sales/purchases relating to the accounting year.
7. differentiate among income, profits and gains.
8. state the meaning of fundamental accounting assumptions and their relevance in accounting.
9. describe the meaning of accounting assumptions and the situation in which an assumption is applied during the accounting process.
10. explain the meaning, applicability, objectives, advantages and limitations of accounting standards.
11. Double entry system
12. Explain the meaning, advantages and characteristic of GST.

INTRODUCTION TO ACCOUNTING

MEANING OF ACCOUNTING

The American Institute of Certified Public Accountants (AICPA) had defined accounting as the art of recording, classifying, and summarising in a significant manner and in terms of money, transactions and events which are, in part at least, of financial character, and interpreting the results thereof'.

Accounting as a Source of Information

accounting is a definite process of interlinked activities, that begins with the identification of transactions and ends with the preparation of financial statements. Every step in the process of accounting generates information. To be useful, the accounting information should ensure to:

• provide information for making economic decisions;
• serve the users who rely on financial statements as their principal source of information;
• provide information useful for predicting and evaluating the amount, timing and uncertainty of potential cash-flows;

• provide information for judging management's ability to utilise resources effectively in meeting goals
• provide factual and interpretative information by disclosing underlying assumptions on matters subject to interpretation, evaluation, prediction, or estimation; and
• provide information on activities affecting the society.

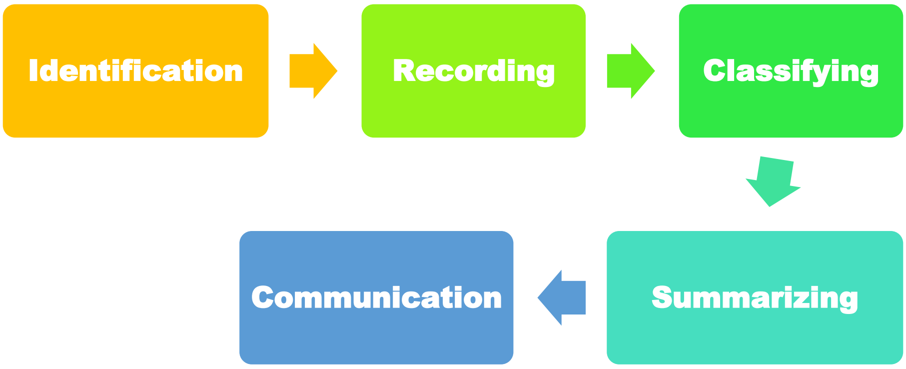
Branches of Accounting

The economic development and technological advancements have resulted in an increase in the scale of operations and the advent of the company form of business organisation. This has made the management function more and more complex and increased the importance of accounting information. This gave rise to special branches of accounting. These are :
Financial accounting: The purpose of this branch of accounting is to keep a record of all financial transactions so that:
(a) the profit earned or loss sustained by the business during an accounting period can be worked out,
(b) the financial position of the business as at the end of the accounting period can be ascertained, and
(c) the financial information required by the management and other interested parties can be provided.
Cost Accounting:
The purpose of cost accounting is to analyse the expenditure so as to ascertain the cost of various products manufactured by the firm and fix the prices. It also helps in controlling the costs and providing necessary costing information to management for decision-making.
Management Accounting:
The purpose of management accounting is to assist the management in taking rational policy decisions and to evaluate the impact of its decisions and actions.
Tax accounting
(GST and income tax). The purpose of this accounting is to calculate the tax liabilities of business.
Social responsibility: It involves the recording of transactions related to expenditure on social benefits.

Functions of Accounting

Identification:
It involves observing all business activities and selecting those events or transactions which can be considered as financial transactions.
Measurement: In Accounting we record only those transactions which can be measured in terms of money or which are of financial nature. If a transactions or event cannot be measured in monetary terms, it is not considered for recording in financial accounts.
Recording: Once the economic events are identified and measured in financial terms, these are recorded in books of account in monetary terms and in a chronological order. Recording should be done in a systematic manner so that the information can be made available when required.
Classifying: Once the financial transactions are recorded in journal or subsidiary books, all the financial transactions are classified by grouping the transactions of one nature at one place in a separate account. This is known as preparation of Ledger.

Summarizing: It is concerned with presentation of data and it begins with balance of ledger accounts and the preparation of trial balance with the help of such balances. Trial balance is required to prepare the financial statements i.e. Trading Account, Profit & Loss Account and Balance Sheet.
Communication: The main purpose of accounting is to communicate the financial information the users who analyse them as per their individual requirements. Providing financial information to its users is a regular process.



Objectives of Accounting

(i) The main objective of the accounting is to keep systematic record of business transactions. That is why, all financial transactions are first recorded in journal and then posted into ledger.

(ii) Accounting is helpful in preventing and detecting the errors and frauds.

(iii) Accounting plays important role in calculating the profit or loss during a particular period by preparing Trading account and Profit and Loss Account.

(iv) Accounting is helpful in ascertaining the financial position of the business.

(v) Accounting provides useful information to its users.

Qualitative Characteristics of Accounting

(i) **Reliability:** Accounting information should be reliable, verifiable and based on facts.

(ii) **Relevance**: Only Relevant information should be disclosed. Information which is irrelevant and useless should be not be the part of financial statements.

(iii) **Understandability**: Accounting information should be presented in a very simple way so that it is easy to understand by its users.

(iv) **Comparability**: Financial Statements should contains the figures of current year as well as figures of previous year so that the current performance of the business can be compared with the performance of previous year.

Advantages of Accounting

1. Financial Information about Business

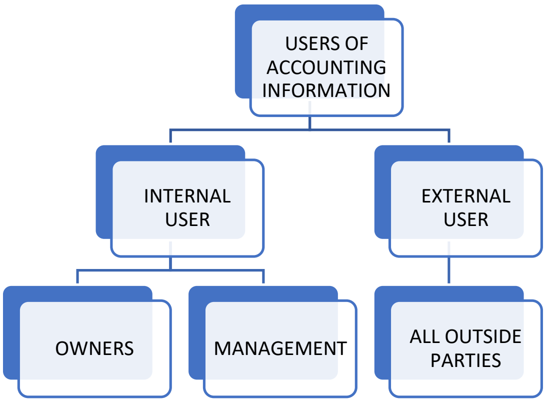
2. Assistance to Management
3. Replaces Memory
4. Facilitates Comparative Study
5. Facilitates Settlement of Tax Liabilities
6. Facilitates Loans
7. Evidence in Court

Limitations of Accounting

1. Accounting is not Fully Exact
2. Accounting does not Indicate the Realisable Value
3. Accounting Ignores the Qualitative Elements
4. Accounting Ignores the Effect of Price Level Change
5. Accounting may Lead to Window Dressing

Interested Users of Information

Many users need financial information in order to make important decisions. These users can be divided into two broad categories: *internal users and external users.*



Internal users include: Chief Executive, Financial Officer, Vice President, Business Unit Managers, Plant Managers, Store Managers, Line Supervisors, etc.
External users include: present and potential Investors (shareholders), Creditors (Banks and other Financial Institutions, Debenture holders and other Lenders), Tax Authorities, Regulatory Agencies (Department of Company Affairs, Registrar of Companies, Securities Exchange Board of India, Labour Unions, Trade Associations, Stock Exchange and Customers, etc.

• The owners/shareholders use them to see if they are getting a satisfactory return on their investment, and to assess the financial health of their company/business.

• The directors/managers use them for making both internal and external comparisons in their attempts to evaluate the performance. They may compare the financial analysis of their company with the industry figures in order to ascertain the company's strengths and weaknesses. Management is also concerned with ensuring that the money invested in the company/organisation is generating an adequate return and that the company/organisation is able to pay its debts and remain solvent.

• The creditors (lenders) want to know if they are likely to get paid and look particularly at liquidity, which is the ability of the company/organisation to pay its debts as they become due.

• The prospective investors use them to assess whether or not to invest their money in the company/organisation.

• The government and regulatory agencies such as Registrar of companies, Custom departments IRDA, RBI, etc. require information for the payment of various taxes such as

Income Tax (IT), Customs and Excise duties for protecting the interests of investors, creditors(lenders), and also to satisfy the legal obligations imposed by The Companies Act 2013 and SEBI from time-to time.

Different Roles of Accounting

(i) As a language – it is perceived as the language of business which is used to communicate information on enterprises;
(ii) As a historical record- it is viewed as chronological record of financial transactions of an organisation at actual amounts involved;
(iii) As current economic reality- it is viewed as the means of determining the true income of an entity namely the change of wealth over time;
(iv) As an information system – it is viewed as a process that links an information source (the accountant) to a set of receivers (external users) by means of a channel of communication;
(v) As a commodity- specialised information is viewed as a service which is in demand in society, with accountants being willing to and capable of providing it.

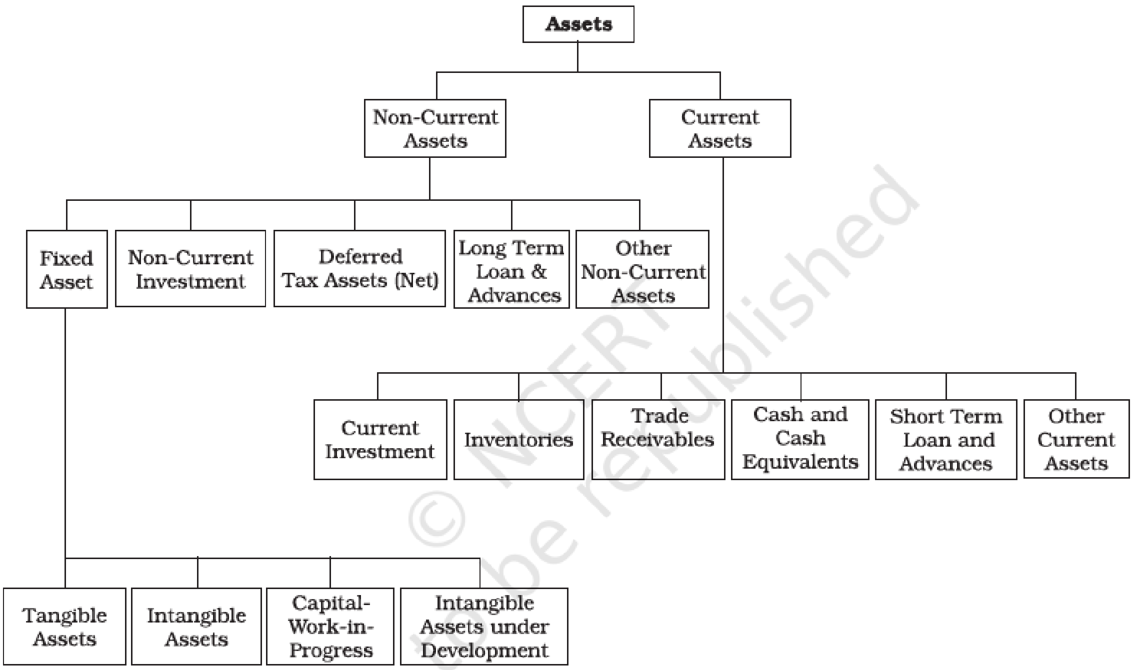
Basic Accounting Terms

Business Entity: It means a specifically identifiable business enterprise like Super Bazar, ITC Limited, Hira & Co. etc.

Transactions: An event involving some value between two or more entities.

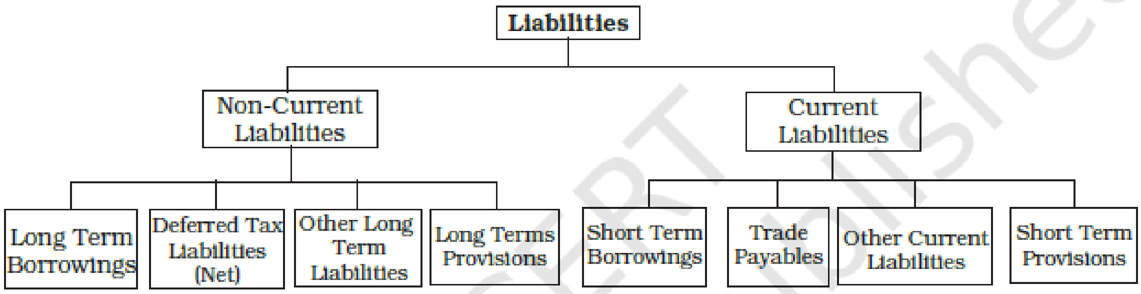
Assets: - These are properties or economic resources of an enterprises which can be expressed in monetary terms it can be divided in two parts

1.Non current assets(more than 1 year period) 2. Current assets (less than 1 year period)



Liabilities: These are certain obligations or dues which business has to pay to outsiders. These are of two types: 1. Noncurrent liabilities(payable in more than 1 year)

2 current liabilities (payable in one year)



Capital: It is amount invested by the owner of business.

Sales: It can be credit or cash, in which goods are sold and delivered to customers.

Revenues: It is the amount which is earned by selling of products and services.

Expenses: It is known as cost of assets consumed or services which used.

Expenditure: It means spending money for some benefit.

Profit: Excess of revenues over expenses is called profit.

Gain: It generates from incidental transaction such as sales of fixed asset, winning of court case.

Loss: Excess of expenses over income is termed as loss.

Discount: It is defined as concession or deduction in price of goods sold.

Voucher: It is known as evidence in support of a transaction.

Goods: It refers all the tangible goods in which a business deals. (Raw material, work in progress, finished goods.)

Drawings: Amount of goods or cash which is withdrawn from business for personal use by the proprietor.

Purchases: It means of procurement of goods on credit or cash.

Stock: It is a part of unsold goods. It can be divided into two categories.

a. Opening stock
b. Closing stock.

Debtors: There are persons who owe to an enterprise an amount for buying goods and services on credit.

Creditors: These are persons who have to be paid by an enterprise an amount for providing the enterprise goods and services on credit.

Discount it is the reduction in the price of goods. It is of two types: cash discount and trade discount. Trade discount is given to increase sales while cash discount is given for early or prompt payment.

Questions for practice

1. Define accounting.
2. State the end product of financial accounting.
3. Enumerate main objectives of accounting.

4. Who are the users of accounting information.
5. State the nature of accounting information required by long-term lenders.
6. Who are the external users of information?
7. Enumerate information needs of management.
8. Give any three examples of revenues.
9. Distinguish between debtors and creditors; profit and gain
10. ‘Accounting information should be comparable’. Do you agree with this statement. Give two reasons.

THEORY BASE OF ACCOUNTING

The principles are generally accepted by the accountants as general guidelines for preparing accounting records. These are classified as:

(i) Basic Assumptions/Concepts

(ii) Basic Principles

(iii) Modifying Principles/Conventions

BASIC ASSUMPTION/CONCEPTS

In order to make the accounting statements convey the same meaning to all people and to make them more meaningful, accountants have agreed on a number of assumptions/concepts, which are usually followed in preparing accounting records. These are following:

1. **Going Concern Assumption:** According to this assumption, it is assumed that business will continue to exist for a long period in future. All transactions are recorded assuming that enterprise will continue in future for a long time. That is why fixed assets are recorded at their cost price and depreciated during its useful life, irrespective of its market value, because fixed asset are not meant for resale in business. Also without this assumption, the classification of fixed and current assets, current and long term liabilities is impossible.

2. **Accrual Concept:** Accrual concept holds the recognition of transactions as they occur, whether receipt or payment for the same is made or not. The accrual concept recognizes revenue when it earned rather than when it is collected and recognizes expense when they occur rather than when these are paid.

3. **Concept of Consistency:** This principle states that accounting principles and methods followed for preparing accounting statements should remain consistent year after year. If this concept is not followed, different results can be drawn from the same accounting data. E.g. if method of calculation of depreciation is changed, the profit figure will distort and no longer comparable.

BASIC PRINCIPLES:

On the basis of accounting assumptions, certain principles have been developed that guide how transactions should be recorded and reported. Following are some of basic principles:

1. **Accounting Entity Concept:** According to this concept, a business is treated as an entity distinct from its owners. Business has its separate books of accounts and all business transactions are recorded from firm’s point of view and not from owner’s point of view. It this assumption is not followed, the operating results and financial position of the business entity can’t be ascertained correctly.

2. **Money Measurement Principle:** According to this principle, only those transactions and events are recorded in books of accounts, which can be measured and expressed in terms of money. Also, accounting records are made simple, understandable and homogeneous by expressing all the items in a common unit of measurement i.e. money.

3. **Accounting Period Principle:** According to this principle, the entire life of the business is divided into small time intervals for calculation of profits and losses of the business and for ascertaining its financial position. Each time interval, for which results are calculated, is known as an ***Accounting Period.*** Twelve months is usually adopted for this purpose. This accounting period can be of two types i.e. calendar year (from 1st Jan. - 31st Dec.) or financial year (from 1st Apr. – 31st Mar.). In India, financial year is adopted as accounting year.

4. Dual Aspect Principle: According to this principle, every transaction has two aspects i.e. debit and credit, and both are recorded at the time of occurrence of a transaction. Each transaction affects at least two accounts, one is debited and other is credited. This system is based on dual aspect and is called ***Double Entry System of Book Keeping.***

5. **Historical Cost Principle:** According to this principle, an asset is recorded in the books of accounts at the price at which it is acquired. Market value of assets and price level changes (inflation and deflation) are ignored and not recorded.
The cost of the asset relates to the past, it is referred to as ***Historical Cost.*** If nothing is paid to acquire assets of company, it is not recorded as an asset like increasing goodwill. 19
6. **Principle of Full Disclosure:** According to this principle, all significant financial information of an entity should be completely disclosed in financial statements. It means disclosing sufficient information, which is material to the interests of users of financial statements e.g. while reporting sales during the year, sales returns should be disclosed separately as deduction from the amount of sales, rather than showing the net sales for the year. As the huge amount of sales return can raise the inquiry and may lead to corrective action.
7. **The Revenue Recognition Concept:** This concept holds that revenue is considered to have been realized when a transaction has been entered into and the obligation to receive the amount has been established. In other words, revenue is considered as being earned when goods are sold or services rendered and not when cash is received.
8. **The Matching Concept:** This principle holds that the cost incurred to earn the revenue should be set out against the revenue in the period during which it is recognized as earned. For matching expenses with revenue, first revenue is recognized and the costs associated with this revenue are recognized.
9. **Verifiable Objective Evidence/Objectivity Concept:** All transactions, which are recorded in books of accounts, must be supported by relevant vouchers e.g. invoices, bills, passbook etc. Personal bias has no place in preparation and presentation of financial records.

MODIFYING PRINCIPLES/CONVENTIONS:

These are certain accounting principles, which can be modified by different accountants according to the situations and requirements of business. Some of these are following:
1. Principle of Conservatism/Prudence: This principle tells us that all anticipated losses should be recorded in books of accounts, but all anticipated and unrealized gains should be ignored. Provision is made for all known liabilities and losses even though the amount can't be determined with certainty. It is the policy of playing safe. E.g. closing stock is valued at cost or market price whichever lower and making provision for doubtful debts etc.
2. Principle of Materiality: According to this principle, only those items are to be disclosed separately in financial statements which are material for decision making for the users of financial statements of the business. Insignificant items or items which are not relevant to the users need not to be disclosed separately in books of accounts. These can be merged with other items. Here materiality based on both information and amount.
An information is considered material if this could change the decisions of a person to whom this information is communicated. This principle is an exception to the principle of full disclosure.

ACCOUNTING STANDARDS

Accounting standards may be defined as written statements issued from time to time by institutions of accounting professionals e.g ICAI, specifying uniform rules or practices for preparing ad presenting financial statements. Some of accounting standards are as follows:
(i) AS-1: Disclosure of Accounting Policies

(ii) AS-2: Valuation of Inventories

(iii) AS-3: Cash Flow Statement

Need or Utility or Advantages of Accounting Standards:

(i) Accounting standards bring uniformity in preparation and presentation of financial statements.

(ii) They ensure the consistency and comparability of different financial statements.

(iii) They significantly reduce the chances of manipulations and frauds.

(iv) To improve the reliability and credibility of financial statements.

Nature of accounting standards:

(i) These are based on applicable law, customs and business environment.

(ii) These are intended to apply only on material items.

(iv) Mostly accounting standards are mandatory in nature.

Limitations of Accounting Standards

1. Accounting standard makes choice between different alternate accounting treatments difficult to apply.

2. It is rigidly followed and fails to extend flexibility in applying accounting standards.

3. Accounting standard cannot override the statue. The standards are required to be farmed within the ambit of prevailing status.

Meaning of IFRS: IFRS is a principle-based accounting standard. IFRS are a single set of high-quality accounting Standards developed by IASB, recommended to be used by the enterprises globally to produce financial statements.

Benefits of IFRS:

(1) Global comparison of financial statements of any companies is possible

(2) Financial statements prepared by using IFRS shall be better understood with financial statements prepared by the country specific accounting standards. So the investors can make better decision about their investments.

(3) Industry can raise or invest their funds by better understanding if financial statements are there with IFRS.

(4) Accountants and auditors are in a position to render their services in countries adopting IFRS.

(5) By implementation of IFRS accountants and auditors can save the time and money.

(6) Firm using IFRS can have better planning and execution. It will help the management to execute their plans globally.

Basis of Accounting:

(1) Cash basis

Under this entry in the books of accounts are made when cash received or paid and not when the receipt or payment becomes due. For example, if salary Rs. 7,000 of January 2010 paid in February 2010 it would be recorded in the books of accounts only in February, 2010.

(2) Accrual basis

Under this however, revenues and costs are recognized in the period in which they occur rather when they are paid. It means it record the effect of transaction is taken into book when they are earned rather than in the period in which cash is actually received or paid by the enterprise. It is more appropriate basis for calculation of profits as expenses are matched against revenue earned in the relation thereto. For example, raw materials consumed are matched against the cost of goods sold for the accounting period.

Goods and Services Tax

(One Country One Tax)

GST is a destination-based tax on consumption of goods and services. It is proposed to be levied at all stages right from manufacture up to final consumption with credit of taxes paid at previous stages available as setoff.

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 CGST, SGST, IGST

CGST means Central Goods and Services Tax. Taxes collected under CGST will constitute the revenues of the Central Government.

SGST means State Good and Services Tax. A collection of SGST is the revenue of the State Government.

For example, Ramesh a dealer in Punjab sell goods to Seema in Punjab worth ` 10,000. If the GST rate is 18%, i.e., 9% CGST and 9% SGST, ` 900 will go to Central Government and 900 will go to Punjab Government.

IGST means Integrated Goods and Services Tax. Revenue collected under IGST is divided between Central and State Government as per the rates specified by the Government. IGST is charged on transfer of goods and services from one state to another. Import of goods and services are also covered under IGST.

Characteristics of Goods and Services Tax

1. GST is a common law and procedure throughout the country under single administration.
2. GST is a destination-based tax and levied at a single point at the time of consumption of goods and services by the end consumer.
3. GST is a comprehensive levy and collection on both goods and services at the same rate with benefit of input tax credit or subtraction of value.
4. Minimum number of rates of tax does not exceed two.
5. There is no scope for levy of cess, resale tax, additional tax, turnover tax etc.
6. There is no multiple levy of tax on goods and services, such as sales tax, entry tax, octroi, entertainment tax or luxury tax etc.

Advantages

1. Introduction of GST has resulted in the abolition of multiple types of taxes in goods and services.
2. GST widens the tax base and increased revenue to Centre and State thereby reducing administrative cost for the Government.
3. GST has reduced compliance cost and increases voluntary compliance.
4. GST has affected rates of tax to the maximum of two floor rates.
5. GST has removed the cascading effect on taxation.
6. GST will result in enhancing manufacturing and distribution system affecting the cost of production of goods and services and consequently the demand and production of goods and services will increase.
7. It will eventually promote economic efficiency and sustainable long-term economic growth as GST is neutral to business processes, business models, organisational structure and geographical location.
8. GST would help to extend competitive edge in international market for goods and services produced in the country leading to increased exports.

Questions for Practice

1. Why is it necessary for accountants to assume that business entity will remain a going concern?
2. When should revenue be recognised? Are there exceptions to the general rule?
3. What is the basic accounting equation?
4. The realisation concept determines when goods sent on credit to customers are to be included in the sales figure for the purpose of computing the profit or loss for the accounting period. Which of the following tends to be used in practice to determine when to include a transaction in the sales figure for the period. When the goods have been:
a. dispatched b. invoiced c. delivered d. paid for

Give reasons for your answer.
5. Complete the following worksheet:
(i) If a firm believes that some of its debtors may 'default', it should act on this by making sure that all possible losses are recorded in the books. This is an example of the ___________ concept.
(ii) The fact that a business is separate and distinguishable from its owner is best exemplified by the ___________ concept.
(iii) Everything a firm owns, it also owns out to somebody. This co-incidence is explained by the ___________ concept.
(iv) The ___________ concept states that if straight line method of depreciation is used in one year, then it should also be used in the next year.
(v) A firm may hold stock which is heavily in demand. Consequently, the market value of this stock may be increased. Normal accounting procedure is to ignore this because of the ___________.
(vi) If a firm receives an order for goods, it would not be included in the sales figure owing to the ___________.
(vii) The management of a firm is remarkably incompetent, but the firms accountants can not take this into account while preparing book of accounts because of ___________ concept.
6. Explain Cost concept.
7. What is mean by accounting standard? What is the main objective of accounting standard?
8. Explain the following concepts.
a. Business entity concept
b. Going concern concept
c. Revenue recognition concept
9. Explain the utility of Accounting Standards.
10.Which principle assumes that a business enterprise will not be liquidated in near future?
Ans. Going concern concept.
11. "Closing stock is valued lower than the market price" which concept of accounting is applied here?
Ans. Conservatism (Prudence) concept.
12.An asset may define as a bundle of services" – explain with an example.
13.Under which accounting principle, quality of manpower is not recommended in the books of accounts?
Ans. Money measurement concept.

ACCOUNTING EQUATION

LEARNING OBJECTIVES

- *Meaning of Accounting Equation*
- *Analysis of effect of transactions on assets, liabilities, capital, revenues & expenses*
- *Preparation of Accounting Equation*

MEANING OF ACCOUNTING EQUATION

Accounting equation signifies that the assets of a business are always equal to the total of its liabilities and capital. The equation reads as follows:

$$A = L + C$$

Where,

A = Assets

L = Liabilities

C = Capital

The above equation can also be presented in the following forms as its derivatives to enable the determination of missing figures of Capital(C) or Liabilities (L).

(i) A – L = C

(ii) A – C = L

Since, the accounting equation depicts the fundamental relationship among the components of the balance sheet, it is also called the Balance Sheet Equation. As the name suggests, the balance sheet is a statement of assets, liabilities and capital.

Example 1.

Find the capital of the business if total assets are ₹1,70,000 and its liabilities are ₹70,000.

Solution:

Assets = Liabilities + Capital

So, Capital = Assets – Liabilities

Capital = 1,70,000 – 70,000 = **₹1,00,000**

Example 2.

X commenced business on 1st April, 2016 with a capital of ₹50,000. On 31st March, 2017, his assets were worth ₹95,000 and liabilities of ₹30,000. Find the capital at the end of the year and profit earned during the year.

Solution:

Assets = Liabilities + Capital

So, Capital = Assets – Liabilities

Capital = 95,000 – 30,000 = **₹65,000**

Profit = Closing Capital – Opening Capital

Profit = 65,000 – 50,000 = **₹15,000**

Example 3.

Show effect of following transaction on the accounting equation:

(a) Manoj started business with Cash ₹2,30,000, Goods ₹1,00,000, Building ₹2,00,000

(b) He purchased goods for cash ₹50,000

(c) He sold goods (costing ₹20,000) ₹35,000

(d) He purchased goods from Rahul ₹55,000

(e) He sold goods to Varun (Costing ₹52,000) ₹60,000

(f) He paid cash to Rahul in full settlement ₹53,000

(g) Salary paid by him ₹20,000

(h) Received cash from Varun in full settlement ₹59,000

(i) Rent outstanding ₹3,000

(j) Prepaid Insurance ₹2,000

(k) Commission received by him ₹13, 000

(l) Amount withdrawn by him for personal use ₹20,000

(m) Depreciation charge on building ₹10,000

(n) Fresh capital invested ₹50,000

(o) Purchased goods from Rakhi ₹10,000

Solution:

S. N.	TRANSACTION				ASSETS =		LIABILITIES	+ CAPITAL	
		CASH	STOCK	BUILDING	DEBTORS	PREPAID INSURANCE	CREDITORS	O/S RENT	CAPITAL
a	Started business	2,30,000	1,00,000	2,00,000					5,30,000
b	Purchased goods for cash	2,30,000 (50,000)	1,00,000 50,000	2,00,000					5,30,000
c	Sold goods for cash	1,80,000 35,000	1,50,000 (20,000)	2,00,000					5,30,000 15,000
d	Purchased goods from Rahul	2,15,000	1,30,000 55,000	2,00,000			55,000		5,45,000
		2,15,000	1,85,000	2,00,000			55,000		5,45,000

e	Sold goods to Varun		(52,000)		60,000				8,000
f	Paid cash to Rahul	2,15,000 (53,000)	1,33,000	2,00,000	60,000		55,000 (55,000)		5,53,000 2,000
g	Paid salary	1,62,000 (20,000)	1,33,000	2,00,000	60,000				5,55,000 (20,000)
h	Received cash from Varun	142,000 59,000	1,33,000	2,00,000	60,000 (60,000)				5,35,000 (1,000)
i	O/S Rent	2,01,000	1,33,000	2,00,000				3,000	5,34,000 (3,000)
j	Prepaid Insurance	2,01,000 (2,000)	1,33,000	2,00,000		2,000		3,000	5,31,000
k	Commission received	1,99,000 13,000	1,33,000	2,00,000		2,000		3,000	5,31,000 13,000
l	Drawings	2,12,000 (20,000)	1,33,000	2,00,000		2,000		3,000	5,44,000 (20,000)
m	Depreciation on building	1,92,000	1,33,000	2,00,000 (10,000)		2,000		3,000	5,24,000 (10,000)
n	Fresh capital	1,92,000 50,000	1,33,000	1,90,000		2,000		3,000	5,14,000 50,000
o	Purchased goods from Rakhi	2,42,000	1,33,000 10,000	1,90,000		2,000	10,000	3,000	5,64,000
		2,42,000	1,43,000	1,90,000		2,000	10,000	3,000	5,64,000
						5,77,000	5,77,000		

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SELF ASSESSMENT

1. Prepare accounting equation for the following transactions:

(i) Introduced ₹8,00,000 as cash and ₹50,000 by stock.

(ii) Purchased plant for ₹3,00,000 by paying ₹15,000 in cash and balance at a later date.

(iii) Deposited ₹6,00,000 into the bank.

(iv) Purchased office furniture for ₹1,00,000 & paid by cheque.

(v) Purchased goods worth ₹80,000 for cash and for ₹35,000 in credit.

(vi) Goods amounting to ₹45,000 was sold for ₹60,000 on cash basis.

(vii) Goods costing ₹80,000 were sold for ₹1,25,000 on credit.

(viii) Cheque issued to the supplier of goods worth ₹35,000.

(ix) Cheque received from customer amounting to ₹75,000.

(x) Withdrawn by owner for personal use ₹25,000.

2. Prepare accounting equation for the following transactions:

(i) Started business with cash ₹2,00,000 & stock ₹1,50,000.

(ii) Purchased goods for cash ₹15,000 & on credit ₹20,000.

(iii) Sold goods for cash ₹20,000 & on credit ₹10,000.

(iv) Purchased goods of the value of ₹12,000 for ₹15,000.

(v) Sold goods for ₹20,000 (cost price ₹17,500).

3. Find the total assets of the firm if the capital is ₹60,000 & liabilities ₹39,000.

4. A started business on 1st April, 2017 with a capital of ₹1,10,000 & took loan from bank ₹40,000. At the end of the year on 31st March, 2018, his assets were for ₹2,50,000, creditors for ₹70,000. Bank loan has not been paid so far, however, interest on loan has been paid. Find the closing capital and profit earned during the year.

5. Find the opening capital of the firm from the following information given at the end of the year:

Total assets: ₹1,30,000 External liabilities: ₹40,000

Additional capital: ₹20,000 Drawings: ₹15,000

Profit: ₹25,000

---**END OF CHAPTER**---------------------------------

RECORDING OF TRANSACTIONS I

Meaning of Debit and Credit

All accounts are divided into two sides. The left side of an account is traditionally called Debit side and the right side of an account is called Credit side. Normally account is prepared in 'T' shape. Double entry system is the most progressive, scientific and complete system of recording the financial transaction of a business. According to this system there are **two accounts** involved in every business transaction. One of them is debited and the other is credited.

Types of accounts:

There are 5 types of accounts as per Modern approach

1. **Assets**
2. **Liabilities**
3. **Expenses and losses**
4. **Incomes and gains**
5. **Capital**

Debit is written as **Dr.** and credit is written as **Cr.** An account is abbreviated as A/c.

Rule for Debit and Credit

1. **Asset Accounts** (Land and Building, Plant and machinery, furniture, stock, debtors, cash & bank etc.)
Debit the increases and Credit the decreases.
2. **Liability Accounts** (Creditors, bank loan, outstanding expenses, bills payable etc.)
Debit the decreases and credit the increases.
3. **Capital Account** (Capital account and drawings account)
Debit the decreases and credit the increases.
4. **Income/ Revenue account** (sales, discount received, interest received, commission received, discount received, bad debts recovered etc.)
Debit the decreases and credit the increases.
5. **Expenses/ loss Accounts** (purchases, wages, salary, depreciation, bad debts, rent, discount allowed etc.)
Debit the increases and Credit the decreases

On which side will increase in following accounts be recorded? Also, mention the nature of accounts are debited and credited?

1. Cash 2. Creditors 3. Bank loan 4. Stock 5. Rent received 6. Salary paid 7. Salary payable 8. Rajan (owner) 9. Soman (debtor) 10. Sharan (Customer) 11. Purchase 12. Sales 13. Interest Payable 14. Accrued Commission 15. Drawings 16. Discount received 17. Depreciation

Name of the Account	**Nature of the account**	**Side in which Increase will be recorded**
1.Cash	Asset	**Debit**
2. Creditors	Liability	**Credit**
3. Bank loan	Liability	**Credit**
4. Stock	Asset	**Debit**
5. Rent Received	Income/ Revenue	**Credit**

6. Salary Paid	Expenses/ losses	**Debit**
7. Salary Payable	Liability	**Credit**
8. Rajan (Owner)	Capital	**Credit**
9. Soman (Debtor)	Asset	**Debit**
10. Sharan (Customer)	Asset	**Debit**
11.Purchase	Expenses/ losses	**Debit**
12. Sales	Income/ Revenue	**Credit**
13. Interest Payable	Liability	**Credit**
14. Accrued Commission	Asset	**Debit**
15. Drawings	**Capital**	**Credit**
16. Discount received	Income/ Revenue	**Credit**
17.Depreciation	Expenses/ losses	**Debit**

JOURNAL

MEANING OF JOURNAL

A journal is a detailed account that records all of a company's financial activities and is used for future reconciliations and information transfer to other formal accounting records, such as the general ledger. In a double-entry bookkeeping system, a journal records the date of a transaction, which accounts were affected, and the balances.

A journal is a book of accounts that records every transaction that occurs in a business with precise explanation for it. It is maintained day to day, hence the chances of mistakes occurring are greatly reduced. There are generally six types of journal entries namely, opening entries, transfer entries, closing entries, compound entries, adjusting entries, reversing entries, and each represent a specific purpose for which such entries are made

Formate of journal

Date	Particulars	LF	**Amount DR.**	**Amount**. CR

Transactions related to Goods:

1. Goods purchased for cash:

    Purchase A/c Dr.

    To Cash A/c

    (Being goods purchased for cash)

2. Goods purchased from ram on Credit:

    Purchase A/c Dr.

    To Ram

    (Being goods purchased from Ram on credit)

3. Goods sold for cash:

Cash A/C Dr.
To Sales A/c
(Being goods sold for cash)

4. Goods sold on credit to Mohan:
   Mohan Dr.
   To Sales A/c
   (Being goods sold to Mohan on credit)
5. Withdrawal of goods by owner for personal use:
   Drawings A/c Dr.
   To Purchase A/c
   (Being goods withdrew by owner for personal use)

6. Goods distributed as free samples:
Advertisement A/c Dr.
To Purchase A/c
(Being goods distributed as free samples)

7. Goods given as charity:
Charity A/c Dr
. To Purchases A/c
(Being goods given as charity)

8. Goods lost by fire/flood/theft etc.:
Loss by fire/theft A/c Dr.
To Purchase A/c

Transactions related to Bank:-

1. Cash deposited into the bank:
   Bank A/c...... Dr.
   To Cash A/c
   (Being cash deposited to bank)
2. Cash withdrawn for office use:
   Cash A/c...... Dr.
   To Bank A/c
   (Being cash withdrew from bank for office use)
3. When cheque is received from customer and deposited into bank same day:
   Bank A/c..... Dr.
   To Customer's personal A/c
   (Being cheques deposited into bank)
4. Cash withdrawn for personal use by owner:

Cash A/c...... Dr

. To Bank A/c

(Being cash withdrew for personal use)

5. When cheque is received from customer and not deposited into bank same day:

   Cheque-in-hand A/c.... Dr.

   To customer's personal A/c

6. When above cheque (Point 5) is deposited later into bank:

   Bank A/c ......Dr.

   To cheque-in-hand A/c

   (Being cheques deposited into bank received from …………….. On ………)

7. When payment is made through cheque:

   Personal A/c ....Dr.

   To Bank A/c

   (being payment made to …….. by cheque)

8. When expense is paid through cheque:

   Expense A/c ....Dr.

   To Bank A/c

   (Being expense paid by cheque)

9. When interest is allowed by the bank:

   Bank A/c........ Dr.

   To Interest A/c

   (Being interest allowed by bank)

10. When Bank charges for the services provided:

    Bank Charges A/c...... Dr.

    To Bank A/c

    (Being Bank charges deducted)

Fixed Asset Related Transactions

Example:

1. When furniture purchased for Cash Rs. 20,000

Furniture A/c Dr.

To Cash A/c

2. When furniture purchased from A Ltd on credit Rs.10,000

Furniture A/c Dr.

To A Ltd A/c

3. Depreciation charged on furniture Rs.2,000

Depreciation A/c Dr. 2,000

To Furniture A/c 2,000

4. When furniture sold for Rs.18,000

Cash A/c Dr.

To Furniture A/c
5. Bricks worth Rs.10,000 purchased for the construction of building
Building A/c Dr.
To Cash
6. Paid installation charges of machinery Rs.2,000
Machinery A/c Dr.
To Cash A/c
7. Purchased Furniture for Rs.10,000 and spent Rs.100 for its carriage
Furniture A/c Dr. 10,100
To Cash 10,100

Practice Questions

Q1 Enter the following transactions in the Journal of Manohar Lal & Sons.:-

2022		**₹**
March 1	Manohar Lal & Sons started business with cash	60,000
2	Purchased furniture for cash	10,000
4	Purchased goods for cash	25,000
5	Bought goods from Kamlesh	15,000
10	Paid cash to Kamlesh	15,000
16	Purchased goods from Sohan	6,000
18	Purchased goods from Sohan *for cash*	8,000
20	Paid rent for the office	1,000

Q2 Enter the following transactions in the Journal of M/s Tripathi Bros. :-

2022		**₹**
Jan. 6	Sold goods for cash	36,000
8	Sold goods to Hari	30,000
14	Received cash from Hari	18,000
26	Received Commission	750
27	Paid Salary to Gopal	1,200
28	Received cash from Hari	12,000
29	Withdrew cash from office for personal use	4,000
30	Wages paid	7,200
30	Bought Machinery for Cash	8,000

1. Trade Discount: Trade discount is an allowance given by the seller of goods out of the selling price (list price or catalogue price). It is usually allowed by the wholesaler to the retailer, when goods are purchased in large quantity. Trade discount is allowed on both on cash as well as credit transactions. Trade discount is related to the purchase and not to the payment. No separate entry is passed for the trade discount, as it is deducted in the invoice from the list price and the net amount only is recorded in the books of accounts.

2. Cash Discount

Cash discount is usually allowed by the seller to the customers (creditor to the debtor) to encourage prompt or early payment. Cash discount is allowed only if the customer/debtor makes the payment within a fixed period. When cash discount is allowed, it is an expense and debited to 'Discount allowed Account' and when cash discount is received, it is a revenue and credited to 'Discount Received Account'. It is an expense for the business allowing and gain for the business availing it.

Q 3.Pass Journal entries in the books of Hari Shankar & Co. from the following:

2022		**₹**
April 1	Commenced business with cash	50,000
2	Purchased goods from Subhash	20,000
4	Sold goods to Ramnath	15,000
6	Ramnath returned defective goods	1,000
10	Received cash from Ramnath and	13,800
	Discount allowed	200
12	Gopal sold goods to us	10,000
14	Paid to Gopal in full settlement of his account after deducting 5% discount.	
15	Paid Rent	10,000
16	Paid Rent of Hari Shankar's residence	5,000
18	Purchased goods *for cash* from Govind for ₹ 6,000 at 20% trade discount.	
20	Purchased goods from Govind for ₹ 10,000 at 20% trade discount.	
24	Paid to Govind ₹ 7,850 in full settlement of his account.	
25	Paid to Subhash ₹ 4,750; discount received ₹ 250.	
30	Paid Wages ₹ 400; Salaries ₹ 4,000; Advertisement expenses ₹ 800 and Trade expenses ₹ 1,000.	

Accounting Entries under Goods and Services Tax

Record necessary Journal entries assuming CGST @ 5% and SGST @ 5% and all transactions are occurred within Delhi)

i. Shobit bought goods ₹1,00,000 on credit
ii. He sold them for ₹1,35,000 in the same state on credit
iii. He paid for Railway transport ₹8,000
iv. He bought computer printer for ₹10,000
v. Paid postal charges ₹2000

Solution

Journal

Date	*Particulars*		*L.F.*	*Debit Amount* ₹	*Credit Amount* ₹
(i)	Purchases A/c	Dr.		1,00,000	
	Input CGST A/c	Dr.		5,000	
	Input SGST A/c	Dr.		5,000	
	To Creditors A/c				
	(Being Goods bought on credit)				1,10,000
(ii)	Debtors A/c	Dr.		1,48,500	
	To Sales A/c				1,35,000
	To Output CGST A/c				6,750
	To Output SGST A/c				6,750
	(Being Goods sold on credit)				
(iii)	Transport Charges A/c	Dr.		8,000	
	Input CGST A/c	Dr.		400	
	Input SGST A/c	Dr.		400	
	To Bank A/c				8,800
	(Being tranport charges paid)				
(iv)	Computer printer A/c	Dr.		10,000	
	Input CGST A/c	Dr.		500	
	Input SGST A/c	Dr.		500	
	To Bank A/c				11,000
	(Being Computer-Printer bought)				
(v)	Postal charges A/c	Dr.		2,000	
	Input CGST A/c	Dr.		100	
	Input SGST A/c	Dr.		100	
	To Bank A/c				2,200
	(Being Paid for Portage)				
(vi)	Output CGST A/c	Dr.		6,750[3]	
	Output SGST A/c	Dr.		6,750[4]	
	To Input CGST A/c				6,000[1]
	To Input SGST A/c				6,000[2]
	To Electronic Cash Ledger A/c				1,500
	(Being GST set off and balance paid)				

Working Notes :-

Total Input CGST	=	₹ 5,000 + ₹ 400 + ₹500 + ₹100 = ₹6,000[1]
Total Input SGST	=	₹ 5,000 + ₹ 400 + ₹500 + ₹100 = ₹6,000[2]
Total Output CGST	=	₹ 6,750[3]
Total Output SGST	=	₹ 6,750[4]
Net CGST Payable	=	₹ 6,750 - ₹6,000 = ₹750
Net SGST Payable	=	₹ 6,750 - ₹6,000 = ₹750

CASH BOOK

A cash book can be defined as a financial journal which contains all the cash receipts and disbursements. Cash Book also includes bank deposits and bank withdrawals. The entries that come in the cash book are then posted into the general ledger. In the cash book entries, the daily cash receipts and cash payments are easily and smoothly analyzed. The Cash in hand at any point of time can be easily ascertained through the Cash Book balance.

Types of Cash Book

1.Simple Cash Books- This is also known as the Single Column Cash Book. This cash book will only be recorded for the purpose of cash transactions. The cash that is coming in is known as the receipts which will be on the left and the cash payments are recorded on the right.

Formate of single column cash book

Date	Particulars	Cash(Dr)	Date	Particulars	Cash (Cr)

2.Two Column Cash- Here we have an additional column for the discounts. Thus, along with the cash transactions, we are also required to have discounts in the same cash book. Hence both the discounts received and the discount which is given here is recorded.

Formate of double column cash book

Date	Particulars	Cash	Bank	Date	Particulars	Cash	Bank

3.**Three Column Cash-** This cash book has three columns, consisting of the - cash, the discount and the additional column as the bank columns in it. With the development of banking most of the firms, these days prefer to deal in cheques or with the bills of exchange

Petty Cash Book- The firm usually has cash transactions which are happening in all the departments. The cash transactions are then recorded in one of the above formats of the cash books. But there are a lot of cash transactions which are recorded for every small amount. Even the dozens of such transactions that occur in just one day are also recorded here. These are known as the petty transactions.

Date	*Details*	*Amount* ₹
2017		
Nov. 01	Cash in hand	30,000
Nov. 04	Cash received from Gurmeet	12,000
Nov. 08	Insurance paid (Annual Instalment)	6,000
Nov. 13	Purchased furniture	13,800
Nov. 16	Sold goods for cash	28,000
Nov. 17	Purchased goods from Mudit in cash	17,400
Nov. 20	Purchase stationery	1,100
Nov. 24	Cash paid to Rukmani in full settlement of account	12,500
Nov. 27	Sold goods to Kamal for cash	18,200
Nov. 30	Paid monthly rent	2,500
Nov. 30	Paid salary	3,500
Nov. 30	Deposited in bank	8,000

Date	Particulars	l.f	Amount	Date	Particulars	LF	Amount
2017 Nov.1	Balance b/d		30,000	Nov 8	Insurance		6,000
Nov 4	Gurmeet		12,000	Nov 13	Furniture		13,800
Nov 16	Sales		28,000	Nov 17	Purchases		17,400
Nov.27	Sales		18,200	Nov 20	Stationery		1,100
				Nov 24	Rukmani		12,500
				Nov 30	Rent		2,500
				Nov 30	Salary		3,500
				Nov 30	By Bank A/c		8,000
				Nov 30	Balance c/d		23,400
			88,200				88,200
Dec 1	Balance b/d		23,400				

Date	*Details*	*Amount* ₹
2017		
Sept. 01	Bank balance	42,000
Sept. 01	Cash balance	15,000
Sept. 04	Purchased goods by cheque	12,000
Sept. 08	Sales of goods for cash	6,000
Sept. 13	Purchased machinery by cheque	5,500
Sept. 16	Sold goods and received cheque (deposited same day)	4,500
Sept. 17	Purchase goods from Mriaula in cash	17,400
Sept. 20	Purchase stationery by cheque	1,100
Sept. 24	Cheque given to Rohit	1,500
Sept. 27	Cash withdrawn from bank	10,000
Sept. 30	Rent paid by cheque	2,500
Sept. 30	Paid salary	3,500

Cash Book

Dr. **Cr.**

Date	*Receipts*	*L.F.*	*Cash* ₹	*Bank* ₹	*Date*	*Payments*	*L.F.*	*Cash* ₹	*Bank* ₹
2017 Sept.					2017 Sept.				
01	Balance b/d		15,000	42,000	04	Purchases			12,000
08	Sales		6,000		13	Machine			5,500
16	Sales			4,500	17	Purchase		17,400	
27	Bank	C	10,000		20	Stationery			1,100
					24	Rohit			1,500
					27	Cash	C		10,000
					30	Rent			2,500
					30	Salary		3,500	
					30	Balance c/d		10,100	13,900
			31,000	46,500				31,000	46,500
Oct. 01	Balance b/d		10,100	13,900					

Questions for practice:

1. **Enter the following transactions in a simple cash book :**

Date	Particulars	Amount
Dec.2022		
01	Cash in hand	12000
05	Cash received from Bhanu	4000
07	Rent paid	2000
10	**Purchased goods Murari for cash**	6000
12	**Sold goods for cash**	9000
15	**Purchase stationery**	300
18	**Cash paid to Rahul on account**	2000
24	**Paid salary**	1000
29	**Paid rent**	500

2.**Record the following transactions in a bank column cash book for November 2022:**

Date	**Particulars**	**Amount**
01	**Started business with cash**	**80000**
04	**Deposited in bank**	**50000**
10	**Received cash from Rahul**	**1000**
15	**Bought goods for cash**	**8000**
22	**Bought goods by cheque**	**10000**
25	**Paid to Shyam by cash**	**20000**

30 **30**	**Drew from Bank for office use** **Rent paid by cheque**	**2000** **1000**

3. Prepare double-column cash book from the following information for September 2022

Date	Particulars	Amount
01	**Cash in hand**	7500
	Bank overdraft	3500
06	**Paid wages**	200
07	**Cash sales**	7000
10	**Cash deposited into the bank**	10000
16	**Goods purchased and paid by cheque**	2000
18	**Paid rent**	500
26	**Drew from the bank for personal use**	4000
29	**Salary paid**	1000

4. Enter the following transactions in double column cash book of M/s Ambica Traders for September 2022.

Date	Particulars	Amount
01	**Commenced business with cash**	50000
03	**Opened bank account with ICICI**	30000
05	**Purchased goods for cash**	10000
10	**Purchased office machine for cash**	5000
15	**Sales goods on credit from Rohan and received cheque**	7000
18	**Cash sales**	8000
20	**Rohan's cheque deposited into the bank**	
22	**Paid cartage by cheque**	500
25	**Cash withdrawn for personal use**	2000
30	**Paid rent by cheque**	1000

SUBSIDIARY BOOKS

The Subsidiary books are known as the books of original entry. In daily business transactions, a majority of the transactions are either related to sales, or to purchases or to cash. Thus, we record the transactions of the same or similar nature in one place, that place is a subsidiary book. We record the transactions chronologically to facilitate the accountant.

Types of Subsidiary Books

The subsidiary books are of various types which suit the needs of an organization. The types are as follows:

- Cash book
- Purchases book
- Sales book
- Purchases return or return outwards book
- Sales return or return inwards book
- Journal proper

Subsidiary Books of Accounts

The Subsidiary Books are the books of Original Entry. These books are also called Day Books or special journals. We record the transactions in this book which are of similar nature, the recordings are done in chronological manner in Subsidiary Books. Subsidiary books actually are helpful in overcoming the limitations of journal books or journal entries.

Format of Purchase Book

Date	Invoice No.	Name of the Supplier	L.F	Details	Total Amount

Format of Sales Book

Date	Invoice No.	Name of the Customers	L.F	Details	Total Amount

Format of Purchase Return Book

Date	Debit Note	Particulars	L.F	Details	Total Amount

Format of Sales Return Book

Date	Credit Note	Particulars	L.F	Details	Total Amount

Q.Enter the following transactions in the Purchase Book, Sales Book, Purchase Returns Book and Sales Returns Book of Abhishek and Co. for the month of January, 2022.

01	Purchased goods from Raj Traders Rs 16,400 at 10% trade discount.
03	Preeti enterprises invoiced goods to us Rs 17,250.
06	Sold goods to Vinita Stores Rs 19,000 at 5% trade discount.
09	Mitesh Associates invoiced goods to us Rs 17,000 at $2^{½}$ trade discount.
12	Returned goods to Raj traders Rs 1,650 (Net).
15	Vinita Traders returned goods to us as they were damaged in transit Rs 4,000 (Gross).
18	Returned goods to Preeti Rs 2,550
23	Placed an order with Novel Stores for goods worth Rs 29,000.
25	Novel Stores supplied goods worth Rs 19,000 only
26	Returned goods to Novel Stores as they were not as per specification Rs 2,550.
28	Sold goods to Deepika Rs 24,000 at 8% trade discount.
30	Deepika returned goods of Rs 4,000 (Gross).

ANSWER:

In the Books of Abhishek and Co.				
		Purchases Book		
Date	**Particulars**	**L.F.**	**Details (Rs)**	**Amount (Rs)**
Jan 2011				
1	Raj Traders		16,400	
	Less: Trade Discount @ 10%		(1,640)	14,760
3	Preeti Enterprises			17,250
9	Mitesh Associates		17,000	
	Less: Trade Discount @ 2.5%		(425)	16,575
25	Novel Stores			19,000

31	Purchases A/c Dr.			**67,585**

Sales Book

Date	Particulars	L.F.	Details (Rs)	Amount (Rs)
Jan 2011				
6	Vinita Stores		19,000	
	Less: Trade Discount @ 5%		(950)	18,050
28	Deepika		24,000	
	Less: Trade Discount @ 8%		(1,920)	22,080
31	Sales A/c Cr.			**40,130**

Purchases Return Book

Date	Particulars	L.F.	Details(Rs)	Amount(Rs)
Jan 2022	Raj Traders		**1650**	
12	Preeti Enterprises		**2550**	
18	Novel Stores		**2550**	
26	Purchases Returns A/c			**6750**

Sales Return Book

Date	Particulars	Credit Note No.	L.F.	Details (Rs)	Amount (Rs)
Jan 2011					
15	Vinita Traders			4,000	
	Less: Trade Discount @ 5%			(200)	3,800
30	Deepika			4,000	
	Less: Trade Discount @ 8%			(320)	3,680
31	Sales Returns A/c Dr.				**7,480**

Questions for practices:

1.Record the following transactions in Purchase Book, Sales Book, Purchase Returns Book and Sales Returns Book of Tushar General Stores for the month of May 2022.

May 01-Jaya invoiced goods of Rs 15,000 at 9% trade discount as per their Invoice number 231.
May 13-Purchased computer from IBM Computers worth Rs 55,000 as per their Invoice number 863.
May 23-Invoiced goods to Priya for Rs 20,000 at 4½ % trade discount as per Invoice number 341
May 25-Sold goods to Sneha for Rs 14,500 at 10% trade discount as per Invoice number 342
May 27-Sold goods to Anita for Rs 26,650 as per Invoice number 343 and purchased goods from her for Rs 12,250 as per their Invoice number 545.
May 29-Satya supplied goods to us of Rs 2,450 Invoice number 630
May 30-Returned goods worth Rs 460 to Satya and issued Debit Note No. 95

2.Enter the following transactions in the books of Ajay in Purchase Book, Sales Book, Purchase Returns Book and Sales Returns Book for the month of July 2022.

July 01-Purchased goods from Neelkamal Stroes Rs 33,000 at 5% trade discount Half the amount was paid immediately
July 05-Sonali invoiced goods of Rs 14,000 to us at 4% trade discount as per our order dated 27th June 2022.
July 14-Sold goods of Rs 30,000 on credit to Ramlal and Sons at 7% trade discount
July 19-Purchased goods from Surabhi Stores Rs 15,000 and sold the same to Prachi at a profit of 25% on cost
July 24-Purchased goods of Rs 6,600 from Seema Stores and paid for carriage Rs 340
July 26-Purchased furniture for office use Rs 23,000 from Bharat Furniture on credit.

LEDGER

Meaning of Ledger: After recording the business transactions in the Journal or special purpose Subsidiary Books, the next step is to transfer the entries to the respective accounts in the Ledger

Ledger is a book where all the transactions related to a particular account are collected at one place.

Definition: The Ledger is the main or principal book of accounts in which all the business transactions would ultimately find their place under various accounts in a duly classified form.

Utility of Ledger: To know the collective effect of all the transactions pertaining to one particular account. By this classification/collective effect, we are able to know the following-

- It provides complete information about all accounts.
- It provides position of Assets and Liabilities.
- It facilitates the preparation of Trial Balance.

The Journal and the Ledger are the most important books of the double entry mechanism of accounting and are indispensable for an accounting system.

Following points of comparison are worth noting :

1. The Journal is the book of first entry (original entry); the ledger is the book of second entry.
2. The Journal is the book for chronological record; the ledger is the book for analytical record.
3. The Journal, as a book of source entry, gets greater importance as legal evidence than the ledger.
4. Transaction is the basis of classification of data within the Journal; Account is the basis of classification of data within the ledger.
5. Process of recording in the Journal is called Journalising; the process of recording in the ledger is known as Posting.

Format of Ledger Account

Date	Particulars	JF	Amount		Particulars	JF	Amount

Q1.Journalise the following transactions of M/s Mallika Fashion House and post the entries to the Ledger:

Date 2022

June 05 Business started with cash 2,00,000

June 08 Opened a bank account with Syndicate Bank 80,000

June 12 Goods purchased on credit from M/s Gulmohar Fashion House 30,000

June 12 Purchase office machines, paid by cheque 20,000

June 18 Rent paid by cheque 5,000

June 20 Sale of goods on credit to M/s Mohit Bros 10,000

June 22 Cash sales 15,000

June 25 Cash paid to M/s Gulmohar Fashion House 30,000

June 28 Received a cheque from M/s Mohit Bros 10,000

June 30 Salary paid in cash 6,000

Date	Particulars	JF	Amount	
2022 June 05	Cash A/c Dr. To Capital A/c (Business started with cash)		2,00,000	 2,00,000
 June 08	Bank A/c Dr. To Cash A/c		 80,000	

	(Opened a current account with syndicate bank)			80,000
June 12	Purchases A/c Dr. To Gulmohar Fashion House A/c (Goods purchased on credit)		30,000	30,000
June 12	Office Machines A/c Dr. To Bank A/c (Office machine purchased)		20,000	20,000
June 18	Rent A/c Dr. To Bank A/c (Rent paid)		5,000	5,000
June 20	Mohit Bros A/c Dr. To Sales A/c (Goods sold on credit)		10,000	10,000
June 22	Cash A/c Dr. To Sales A/c (Goods sold for cash)		15,000	15,000
June 25	Gulmohar Fashion House A/c Dr. To Cash A/c (Cash paid to Gulmohar Fashion House)		30,000	30,000
June 28	Bank A/c Dr. To Mohit Bros A/c (Payment received in full and final settlement)		10,000	10,000
June 30	Salary A/c Dr. To Cash A/c (Monthly salary paid)		6,000	6,000

Cash Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
2022				June8	By bank		80000
June 5	Capital		200000	June25	By gulmohar fashion house		30000
June 22	Sales		15000	June30	By salary		6000

Capital Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
				June5	By cash		200000

Bank Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
June 8	Cash		80000	June12	Office machine		30000
June28	Mohit Bros.		10000	June18	Rent		5000

Purchases Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
June 12	Gulmohar Fashion House						

Gulmohar Fashion House Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
June 25	Cash		30,000	June 12	Purchases		30,000

Office Machines Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
June 12	Bank		20,000	June			

Rent Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
June 18	Bank		5,000	June			

Mohit Bros. Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
June 20	Sales		10,000	June 28	Cash		10,000

Sales Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
June				June 22	Mohit Bros Cash		. 10,000 15,000

Salary Account

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
June 30	Cash		6,000				

Q2. Journalise the following transactions of M/s Time Zone and post them to the ledger accounts :

Date Details Amount 2022

Dec. 01 Business started with cash 1,20,000

Dec. 02 Opened a bank account with ICICI 4,00,00

Dec. 04 Goods purchased for cash 12,000

Dec. 10 Paid cartage 500

Dec. 12 Goods sold on credit to M/s Lara India 25,000

Dec. 14 Cash received from M/s Lara India 10,000

Dec. 16 Goods returned from Lara India 3,000

Dec. 18 Paid trade expenses 700

Dec. 19 Goods purchased on credit from Taranum 32,000

Dec. 20 Cheque received from M/s Lara India for final settlement 11,500 and deposited same day into bank

Dec. 22 Goods returned to Taranum 1,500

Dec. 24 Paid for stationery 1,200

Dec. 26 Cheque given to Taranum on account 20,000

Dec. 28 Paid rent by cheque 4,000

Dec. 29 Drew cash for personal use 10,000

Dec. 30 Cash sales 12,000

Dec. 31 Goods sold to M/s Rupak Traders 11,000

Bank Reconciliation Statement

Bank Reconciliation Statement is a record book of the transactions of a bank account. This statement helps the account holders to check and keep track of their funds and update the transaction record that they have made. Bank Reconciliation statement is also known as bank passbook. The balance mentioned in the bank passbook of the statement must tally with the balance mentioned in the cash book. In the statement, all the deposit will be shown in the credit column and withdrawals will be shown in the debit column. However, if the withdrawal exceeds deposit it will show a debit balance (overdraft).

Importance

While making a comparison between the company's cash book and bank balance, the balance does not tally. Therefore, it is important to determine the cause for the difference and display them in the bank reconciliation statement and then tally the two balances. The bank reconciliation statement helps in explaining the differences in the amount between the company's cash book and bank balance. The cash book and the bank passbook differences are caused by:

The difference in timing can be caused by many factors which are:

1. Bank-issued cheque but not yet deposited for payment
2. Paid cheque in the bank but yet not cleared
3. Bank made direct debit from the customer's side
4. Cheque/ amount deposited directly to the bank account
5. Dividends and Interest collected by the bank
6. Bank made direct payment from the customer's side
7. Cheques deposited/bills discounted dishonoured

In a few occasions, the error in two balances can be made from the bank side or in the company's cash book. Few errors are as follows:

1. Errors made while registering the transaction by the company
2. Errors made while registering the transaction by the bank

Types of Bank Reconciliation Statement

The Bank Reconciliation Statement can be prepared in 2 ways:

1. Documenting of bank reconciliation statement without adjusting the cash book balance.
2. Filing of bank reconciliation statement after adjusting the cash book balance.

Steps to Prepare Bank Reconciliation Statement:

- First, the date on which the statement is recorded is mentioned.
- After which the balance displayed in the cash book is mentioned in the statement. Sometimes, the balance mentioned in the passbook can also be mentioned.
- The deposited cheques which are not collected are deducted.
- Then the cheques issued but the deposited for payment, but amount directly deposited in the bank account are recorded

- All the transactions like overdraft interest, amount debited by the bank but not recorded in the cash book, cheques and bills dishonoured are deducted.
- All the credits and profit collected by the company and directly deposited in the bank is added.
- Adjustments of errors are made
- Now the balance between the cash book and statement should be equal or the same.

Objective questions:

1. Why is the bank reconciliation statement important?

Answer : The bank reconciliation statement is important to determine the cause for the difference made on the part of the bank or customers side.

2. Which balance is caused an overdraft of cash book and passbook?

Answer: Cash book Cr. and Passbook Dr. balances.

3. Mention two items drafted in a plus column while starting with a debit balance of cash book.

Answer: The two items drafted in a plus column while starting with a debit balance of cash book are.

- Bank issued cheque but not yet presented for payment
- Interest allowed by the bank but not recorded in the cash book

4. Mention two items drafted in a minus column while starting with a debit balance of cash book.

Answer: The two items drafted in a minus column while starting with a debit balance of cash book are.

- Cheque deposited but not cleared
- Bank made direct payment from the customer's side

5. Mention two items drafted in a minus column while starting with an overdraft balance of cash book.

Answer: The two items drafted in a minus column while starting with an overdraft balance of cash book are.

- Cheque deposited but not cleared
- Bank made direct payment from the customer's side

6. Mention two items drafted in a plus column while starting with an overdraft balance of cash book.

Answer: The two items drafted in a plus column while starting with an overdraft balance of cash book are.

- Bank-issued cheque but not yet presented for payment
- Interest allowed by the bank but not recorded in the cash book

7. A bank reconciliation statement is prepared to.

(a) Reconcile Bank balance as per cash book and bank balance as per pass book

(b) Reconcile Cash balance as per cash book and bank balance as per pass book

(c) Both (a) & (b)

(d) None of the above

Answer : a

8. A Pass Book is a copy of

(a) A customer's account in the bank's book

(b) Cash book relating to bank column

(c) Cash book relating to cash column

(d) Firm's receipts and payments

Answer: a

9. A bank reconciliation statement is prepared with the balance of

(a) Cash Book

(b) Pass Book

(c) Either Cash Book or Pass Book

(d) Neither Cash Book nor Pass Book

Answer: c

10. A bank reconciliation statement is prepared by

(a) Bank

(b) Customers of the Bank

(c) Creditors

(d) Auditors

Answer: b

11. Which of the statement is not a part of the Double Entry System

(a) Cash Book

(b) Trial Balance

(c) Journal

(d) Bank Reconciliation Statement

Answer: d

12. A debit balance in passbook is defined as an overdraft. Is it true or false?

Answer: True

Practical questions

1. Prepare Bank Reconciliation Statement from the following particulars on 31st July 2022.

(a) Balance as per Pass Book ₹ 500.
(b) Three cheque for ₹60, ₹ 39.37, and ₹ 15.25 issued in July 2022 were presented her payment to the bank in August 2022.
(c) Two cheques of ₹ 50 and ₹ 65 sent to the bank for collection where not entered in the pass book by July 31st, 2022.

(d) The Bank charged ₹ 46 for its commission and allowed interest ₹10 which were not entered in the bank account.

Bank Reconciliation Statement

Particulars	Plus	Minus
Balance as per Pass Book	500.00	
Less Cheque issued but not yet presented		
(60+39.37+15.25)		114.62
Add Cheque sent to the bank but not yet collected		
(50+65)	115.00	
Add Bank charges	46.00	
Less Interest allowed by Bank		10.00
Balance as per cash Book		536.38
	661.00	661.00

2. Prepare Bank Reconciliation Statement from the following particulars on 31st December 2021. Cash book showed a balance of ₹ 15,000 on 31st December 2021. On comparing the same with the balance of Pass Book it was revealed that:
   (a) A cheque of ₹2,000 issued in the month of Dec. 2021 has not been presented for payment to the bank.
   (b) The customer deposited cheque worth ₹3,000 but they have not been collected by the bank.
   (c) The bank had allowed ₹ 200 as interest.
   (d) Bank had charged ₹20 as commission for his service.

Bank Reconciliation Statement

Particulars	Plus	Minus
Balance as per Cash Book	15000	
Cheque issued but not yet issued for payment	2000	
Interest allowed by the bank	200	
Cheque deposited but not yet collected by the bank		3000
Bank Charges		20
Balance as per pass Book		14180
	17200	17200

3. On 31st Dec. 2022 the Cash Book on Jain works showed an overdraft of ₹5,600 from the following particulars make out a bank reconciliation statement.
(a) Cheque drawn but not cashed before 31st Dec. 2022 amounted to ₹3,946.
(b) Cheque paid into bank but not collected and credited before 31st December amount to ₹4,891.
(c) A bill received for ₹520 previously discounted with the bank had been dishonoured and debited in the pass book.
(d) Bank charges debited in the pass book amounted to ₹55.
(e) Debit is made in the pass book for ₹120 on account of interest on overdraft.
(f) The bank has collected interest on investment and credited ₹760 in the pass book.

Bank Reconciliation Statement

Particulars	Plus	Minus
Overdraft as per Cash Book		5,600
Cheque issued but not yet presented for payment	3,946	
Cheque paid into bank but not yet credited		4,891
Dishonoured bills debited by the bank		520

Interest on overdraft debited in the pass book		120
Bank Charges		55
Interest on investment collected and credited by bank	760	
Overdraft as per pass book	6,480	
	11,186	11,186

4. The Bank pass book of Mr. X showed an overdraft of Rs. 33,575 on 31st March 2022.On going through the pass book the accountant found the following.

(a) A cheque of ₹ 1,080 credited in the pass book on March 28 is dishonoured and debited in the pass book on April 1, 2022. There was no entry in the cash book about the dishonour of the cheque until 15th April.

(b) Bank had credited his account with ₹ 2,800 for interest collected by them on his behalf but the same had not been entered in his pass book.

(c) Out of ₹20,500 paid in by Mr. X in cash and by the cheque on 31st March, cheque amount to ₹7,500 were collected on 7th April.

(d) Out of the cheque amount to ₹7,800 drawn by him on 27th March, a cheque for ₹ 2,500 was encashed on 3rd April.

Prepare a Bank Reconciliation Statement on March31, 2022.

Bank Reconciliation Statement

Particulars	Plus	Minus
Overdraft as per pass book		33,575
Less Interest collected and credited by the bank		2,800
Add Cheque paid into the bank but not yet collected	7,500	
Less cheque issued but not yet encashed		2,500
Overdraft as per cash book	31,375	
	38,875	38,875

<u>Practice questions</u>

Q.1 On examining the Bank Statement of Green Ltd., it is found that the balance shown on 31st March, 2019, differs from the bank balance of ₹ 23,650 shown by the Cash Book on that date. From a detailed comparison of the entries it is found that:

(i) ₹ 2,860 is entered in the Cash Book as paid into the bank on 31st March, 2019 but not credited by the bank until the following day.

(ii) Bank charges of ₹ 70 on 31st March, 2019 are not entered in the Cash Book.

(iii) A bill for ₹ 5,500 discounted with the bank is entered in the Cash Book without recording the discount charges of ₹ 270.

(iv) Cheques totalling ₹ 16,720 were issued by the company and duly recorded in the Cash Book before 31st March, 2019 but had not been presented at the Bank for payment until after that date.

(v) On 25th March, 2019, a debtor paid ₹ 1,000 into the Company's Bank in settlement of his account but no entry was made in the Cash Book of the company in respect of this.

(vi) No entry has been made in the Cash Book to record the dishonour on 15th March,

2019, of a cheque for ₹ 550 received from Ram Babu.
Prepare a Bank Reconciliation Statement as on 31st March, 2019.

Q.2 Prepare a Bank Reconciliation Statement as on 31st March, 2019 from the following:

(i) On 31st March, 2019, Cash Book of a firm showed bank balance of ₹ 36,000 (Dr.).

(ii) Cheques had been issued for ₹ 30,000, out of which cheques of ₹ 24,000 were presented for payment.

(iii) Cheques of ₹ 8,400 were deposited in the bank on 28th March, 2019 but had not been credited by the bank. Also, a cheque of ₹ 3,000 entered in the Cash Book on 30th March, 2019 was banked on 3rd April.

(iv) A cheque from Suresh for ₹ 2,400 was deposited in the bank on 26th March, 2019 was dishonoured, advice was received on 2nd April.

(v) Pass Book showed bank charges of ₹ 120 debited by the bank.

(vi) One of the Debtors deposited ₹ 3,000 in the bank account of the firm on 26th March, 2019, but the intimation in this respect was received from the bank on 2nd April.

Q.3 Prepare Bank Reconciliation Statement from the following particulars on 31st July, 2019:

(i) Balance as per the Pass Book ₹ 50,000.

(ii) Three cheques for ₹ 6,000, ₹ 3,937 and ₹ 1,525 issued in last week of July, 2019 were presented for payment to the bank in August, 2019.

(iii) Two cheques of ₹ 500 and ₹ 650 sent to the bank for collection were not entered in the Pass Book by 31st July, 2019.

(iv) The bank charged ₹ 460 for its commission and allowed interest of ₹ 100 which were not mentioned in the Bank Column of the Cash Book.

Depreciation, Provisions and Reserves.

Learning outcome:

1.Students will understand the need for providing depreciation.

2.Learn about the various methods that will help in calculating depreciation

3.Learn the accounting treatment of providing depreciation directly to asset Account or by preparing provision for depreciation Account

4.Appreciate the methods of asset disposal

5.The need for creating reserves and provisions.

Meaning of depreciation:

Fixed assets are subject to decline in value and this decline is technically referred to as depreciation. In other words, depreciation may be described as a permanent, continuing and gradual shrinkage in the book value of fixed assets.

Features of Depreciation:

1. It is decline in the book value of fixed assets.
2. It includes loss of value due to effluxion of time, usage or obsolescence.
3. It is a continuing process.
4. It is an expired cost and hence must be deducted before calculating taxable profits.
5. It is a non-cash expense. It does not involve any cash outflow.

Depletion: The term depletion is used in the context of extraction of natural resources like mines, quarries, etc. that reduces the availability of the quantity of the material or asset.

Amortisation:Amortisation refers to writing-off the cost of intangible assets like patents, copyright, trade marks, franchises, goodwill which have utility for a specified period of time.

Causes of Depreciation:

1. Wear and Tear due to Use or Passage of Time
2. Expiration of Legal Rights
3. Obsolescence
4. Abnormal factors such as accidents due to fire, earthquake, floods, etc.

Need for Depreciation:

1.Matching of Costs and Revenue

2.Consideration of Tax

3.True and Fair Financial Position

4. Compliance with Law

Factors Affecting the Amount of Depreciation:

The determination of depreciation depends on three parameters, viz. cost, estimated useful life and probable salvage value.

Methods of Calculating Depreciation Amount :

1.**Straight Line Method**- It is also called fixed instalment method because the amount of depreciation remains constant from year to year over the useful life of the asset. According to this method, a fixed and an equal amount is charged as depreciation in every accounting period during the lifetime of an asset

$$\text{Depreciation} = \frac{\text{Cost of asset - Estimated net residential value}}{\text{Estimated useful life of the asset}}$$

$$\text{Rate of Depreciation} = \frac{\text{Annual depreciation amount}}{\text{Acquisition cost}} \times 100$$

Advantages of Straight -Line Method:

Straight Line method has certain advantages which are stated below:

1.It is very simple, easy to understand and apply. Simplicity makes it a popular method in practice;

2.Asset can be depreciated up to the net scrap value or zero value.

3.Every year, same amount is charged as depreciation in profit and loss account. This makes comparison of profits for different years easy.

4.This method is suitable for those assets whose useful life can be estimated accurately and where the use of the asset is consistent from year to year.

2. **Written Down Value Method**:

Under this method, depreciation is charged on the book value of the asset. Since book value keeps on reducing by the annual charge of depreciation, it is also known as ‘reducing balance method’.

For example, the original cost of the asset is ₹ 2,00,000 and depreciation is charged @ 10% p.a. at written down value, then the amount of depreciation will be computed as follows:

(i)Depreciation (I year) = ₹20,00,000 x10/100=₹ 20,000

(ii) Written down value = ₹ 2,00,000 – ₹20,000 = ₹1,80,000 (at the end of the I year)

(iii) Depreciation (II year) =₹ 1, 80, 000 ×10/100 = ₹18,000

(iv) Written down value = ₹1,80,000 – ₹18,000 = ₹1,62,000 (at the end of the II year)

(v) Depreciation (III year) =₹ 1, 62, 000 ×10/100 = ₹16,200

(vi) Written down value = ₹ 1,62,000 – ₹16,200 = ₹1,45,800

Advantages of Written Down Value Method: Written down value method has the following advantages:

1.This method is based on a more realistic assumption that the benefits from asset go on diminishing (reducing) with the passage of time.

2.It results into almost equal burden of depreciation and repair expenses taken together every year on profit and loss account.

3.Income Tax Act accept this method for tax purposes.

4.As a large portion of cost is written-off in earlier years, loss due to obsolescence gets reduced.

5.This method is suitable for fixed assets which last for long and which require increased repair and maintenance expenses with passage of time.

Difference between Straight Line Method and Written Down Value method:

Basis	**Straight Line Method**	**Written Down Value Method**
1.Basis of charging depreciation	1.Original cost	1.Book Value
2. Annual depreciation charge	2.Fixed/constant	2.Declines year after year
3.Recognition by Income Tax	3.Not recognised	3.Recognised
4.Suitability	4.Suitable for assets where repair charges are less , possibility of and obsolescence is low.	4.Suitable for assets which are affected by technological changes and require more repair expenses with passage of time.

Methods of Recording Depreciation:

In the books of account, there are two types of arrangements for recording depreciation on fixed assets:

• Charging depreciation to asset account or

• Creating Provision for depreciation/Accumulated depreciation account.

Charging Depreciation to Asset account :

According to this arrangement, depreciation is deducted from the depreciable cost of the asset (credited to the asset account) and charged (or debited) to profit and loss account.

Creating Provision for Depreciation Account/Accumulated Depreciation Account:

This method is designed to accumulate the depreciation provided on an asset in a separate account generally called ‘Provision for Depreciation’ or ‘Accumulated Depreciation’ account. By such accumulation of depreciation the asset account need not be disturbed in any way and it continues to be shown at its original cost over the successive years of its useful life.

Questions:

Q1.R. Kanitkar had purchased a machinery for ₹1,00,000 on 1st October, 2016. Another machine was purchased for ₹60,000 by cheque on 1st April, 2018. Depreciation is charged @ 10% p.a. by the Straight Line Method. Accounts are closed every year on 31st March. You are required to pass necessary Journal entries for the years ended 31st March, 2017, 2018, and 2019 and show Machinery Account and Machinery in the Balance Sheet:

(1) When Provision for Depreciation Account is not maintained.

(ii) When Provision for Depreciation Account is maintained.

Solution: (i) When Provision for Depreciation Account is not maintained.

Dr Machinery Account Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
2016	To Bank Alc		1,00,000	2017	By Depreciation Alc		5,000
Oct1				Mar31	By Balance c/d		95,000
			1,00,000				1,00,000
2017	To balance b/d		95,000	2018	By Depreciation A/c		10,000
Apr1				Mar31	By balance c/d		85,000
			95,000				95,000
2018				2019			
Apr1	To balance b/d		85,000	Mar31	By Depreciation A/c		
Apr1	To bank A/c-Mach2		60,000		Mach1 ₹10,000		
					Mach2 ₹ 6,000		16,000
					By balance c/d		
					Mach1 ₹75,000		
					Mach2 ₹54,000		1,29,000

			1,45,000				1,45,000
2019 Apr1	To balance b/d		1,29,000				

Dr Depreciation Account Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
2017 Mar31	To machinery A/c		5,000	2017 Mar31	By Profit & Loss A/c		5,000
2018 Mar31	To machinery A/c		10,000	2018 Mar31	By Profit & loss A/c		10,000
2019 Mar31	To machinery A/c		16,000	2019 Mar31	By Profit & loss A/c		16,000

(ii) When Provision for Depreciation Account is maintained.

Dr Machinery Account Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
2016 Oct 1	To bank A/c		1,00,000	2017 Mar31	By balance c/d		1,00,000
2017 Apr1	To balance b/d		1,00,000	2018 Mar31	By balance c/d		1,00,000
2018 Apr1	To balance b/d		1,00,000	2019 Mar31	By balance c/d		1,60,000
Apr1	To bank A/c		60,000				
			1,60,000				1,60,000
2019 Apr1	To balance b/d		1,60,000				

Dr Provision for depreciation Account Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
2017 Mar31	To balance c/d		5,000	2017 Mar31	By depreciation A/c Mach 1 for 6 mnths		5,000
2018 Mar31	To balance c/d		15,000	2017 Apr1	By balance b/d		5,000

				2018 Mar31	By depreciation A/c Mach1		10,000
			15,000				15,000
2019 Mar31	To balance c/d		31,000	2018 Apr1	By balance b/d		15,000
				2019 Mar31	By depreciation A/c Mach1 ₹10,000 Mach2 ₹ 6,000		16,000
			31,000				31,000
				2019 Apr1	By balance b/d		31,000

Dr Depreciation Account Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
2017 Mar31	To Provision for depreciation A/c		5,000	2017 Mar31	By Profit and loss A/c		5,000
2018 Mar31	To Provision for depreciation A/c		10,000	2018 Mar31	By Profit and loss A/c		10,000
2019 Mar31	To Provision for depreciation A/c		16,000	2019 Mar31	By Profit and loss A/c		16,000

Q2.Green Ltd. purchased a machinery on 1st August, 2015 for ₹60,000. On 1st October,2016, it purchased another machine for ₹20,000. On 30th June, 2017, it sold the first machine for ₹38,500 and on the same date purchased a new machinery for ₹50,000. Depreciation is provided @ 20% p.a. on cost each year. Accounts are closed each year on 31st March. Show the Machinery Account for three years.

Solution:

Dr Machinery Account Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
2015				2016	By depreciation A/c		
Aug1	To bank A/c (Mach1)			Mar31	(8mnths on Mach1)		8,000
			60,000	Mar31	By balance c/d		52,000
			60,000				60,000
2016	To balance b/d		52,000	2017			
Apr1				Mar31	By Depreciation A/c		
Oct1	To bank A/c(Mach2)		20,000		Machine 1 ₹12,000		14,000
					Machine2 ₹ 2,000		
				Mar31	By balance c/d		
					Machine1 ₹40,000		58,000
			72,000		Machine2 ₹18,000		72,000
2017				2017			38,500
Apr1	To balance b/d			June30	By bank A/c (Sale)		3,000
	Mach1 ₹40,000		58,000	June30	By depreciation A/c		
	Mach2 ₹18,000		50,000	2018	(3mnths) Machine1		
June30	To bank A/c			Mar31	By depreciation A/c:		11,500
	Mach3		1,500		Mach2 ₹4,000		
June30	To gain on sale of				Mach3 ₹7,500		
	machinery(Profit &loss			Mar31	By balance c/d:		56,500
	A/c)		1,09,000		Machine2 ₹14,000		1,09,500
			56,500		Machine3 ₹42,500		
2018							
Apr1	To balance b/d						

Q3.On 1st October, 2015, Ram & Bros. purchased a second-hand machine for ₹1,80,000and spent ₹20,000 on its repair and installation. On 30th September, 2018, the machinery was sold for ₹1,40,000 and an amount of ₹4,000 was paid as dismantling charges. The books are closed on 31st March every year and depreciation is charged @ 10% p.a. on the written down value. Show Machinery Account from the date of purchase of machinery till the date of sale of machinery.

Solution:

Dr Machinery Account Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
2015 Oct1	To bank A/c ₹(1,80,000+20,000)		2,00,000	2016 Mar31	By depreciation A/c 10% of ₹2,00,000 for 6 mnths		10,000
				Mar31	By balance c/d		1,90,000
			2,00,000				2,00,000
2016 April1	To balance b/d		1,90,000	2017 Mar31	By depreciation A/c		19,000
				Mar31	By balance c/d		1,71,000
			1,90,000				1,90,000
2017 April1	To balance b/d		1,71,000	2018 Mar31	By depreciation A/c		17,100
				Mar31	By balance c/d		1,53,900
			1,71,000				1,71,000
2018 April1	To balance b/d		1,53,900	2018 Sep30	By bank A/c ₹(1,40,000-40,000)		1,36,000
				Sep30	By depreciation A/c for 6 mnths		7,695
				Sep30	By loss on sale of machinery A/c(Profit & Loss Account)		10,205
			1,53,900				1,53,900

Q4.On 1st April, 2016, Green Ltd. purchased machinery for ₹1,20,000 and on 30th September, 2017, it acquired additional machinery at a cost of ₹20,000. On 30th June, 2018, one of the original machines which had cost ₹5,000 was found to have become obsolete and was sold as scrap for ₹500. It was replaced on that date by a new machine costing ₹8,000. Depreciation is to be provided @ 15% p.a. on the Written Down Value. Accounts are closed on 31st March every year.

Show Machinery Account for the first three years.

Solution:

Dr Machinery Account Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
2016 April1	To bank Account		1,20,000	2017 Mar31	By depreciation A/c		18,000
				Mar31	By balance c/d		1,02,000
			1,20,000				1,20,000
2017 Apr1	To balance b/d		1,02,000	2018 Mar31	By depreciation A/c		16,800
Sep30	To bank A/c		20,000	Mar31	By balance c/d		1,05,200
			1,22,000				1,22,000
2018 Apr1	To balance b/d		1,05,200	2018 June30	By bank A/c- sale		500
June30	To bank A/c		8,000	June30	By depreciation A/c		135
				June30	By Loss on sale of machinery(Profit&Loss A/c)		2,977
				2019 Mar31	By depreciation A/c		16,138
				Mar31	By balance c/d		93,450
			1,13,200				1,13,200
2019 Apr1	To balance b/d		93,450				

Working Notes:

1. **Calculation of loss on sale of machinery:** ₹

	₹
Cost of machinery sold(1st April,2016)	5,000
Less: Depreciation for 2016-17 ₹ (5,000x15/100)	750
Book value of machinery(1st April,2017)	4,250
Less: Depreciation for 2017-18 ₹ (4250x15/100)	638
Book Value of machinery(1st April,2018)	3,612

Less: Depreciation upto 30th June,2018 ₹ (3,612x15/100x3/12) 135

Book value of machinery sold(30th June,2018)	3,477
Less: Sale Process	500
Loss on sale of machinery	2,977

2. **Calculation of depreciation after sale of machinery:**

Book Value of machinery(1st April,2018)	1,05,200
Less: Book value of machinery sold(1st April,2018)	3,612
Remaining machinery	1,01,588
Depreciation on remaining machinery ₹ (1,01,588x15/100)	15,238
Add: Depreciation on machinery purchased during 2018-19₹	900
(8000x15/100x9/12)	16,138

Disposal of Asset:

Disposal of asset can take place either-

(a) at the end of its useful life or (b) during its useful life (due to obsolescence or any other abnormal factor). If it is sold at the end of its useful life, the amount realised on account of the sale of asset as scrap should be credited to the asset account and the balance is transferred to profit and loss account.

Q5.Devinder had among other assets, machinery at a gross value of ₹ 5,00,000 on which accumulated depreciation amounted to ₹2,00,000. A machine purchased for ₹2,00,000 having accumulated depreciation ₹80,000 was sold during the year for ₹1,35,000. Prepare Asset Disposal A/c to determine the profit or loss on the machine sold.

Solution:

Dr Asset Disposal A/c Cr

Date	Particulars	JF	₹	Date	Particulars	JF	₹
	To machinery A/c		2,00,000		By provision for depreciation A/c		80,000
	To profit on sale of asset A/c (Profit & Loss A/c)		15,000		By bank A/c-sale proceeds		1,35,000
			2,15,000				2,15,000

Provision: - Provision can be described as an amount kept aside to cover a known expense/liability in the future.

This is the fund that is to be put aside by a company/organisation to cover the anticipated losses in the future. Example: - 1. Provision for depreciation. 2. Provision for bad debts. 3. Provision for discount on debtors.

Reserves: -A part of the profit which may be set aside and retained in the business to provide for certain future needs like growth and expansion or to meet future contingencies such as workmen compensation.

Examples of reserves are: • General reserve; • Workmen compensation fund; • Investment fluctuation fund; • Capital reserve; • Dividend equalisation reserve; • Reserve for redemption of debenture.

Difference between Reserve and Provision:

The points of difference between reserve and provision are explained below:

1. **Basic nature**: A provision is a charge against profit whereas reserve is an appropriation of profit.

2**. Purpose**: Provision is made for a known liability or expense pertaining to current accounting period, the amount of which is not certain. On the other hand, reserve is created for strengthening the financial position of the business.

3. **Presentation in balance sheet**: Provision is shown either (i) by way of deduction from the item on the asset side for which it is created, or (ii) on the liabilities side along with current liabilities. On the other hand, reserve is shown on the liabilities side after capital.

4. **Effect on taxable profits**: Provision is deducted before calculating taxable profits. Hence, it reduces taxable profits. A reserve is created from profit after tax and therefore it has no effect on taxable profit.

5. **Element of compulsion**: Creation of provision is necessary to ascertain true and fair profit or loss in compliance with ‘Prudence’ or ‘Conservatism’ concept. Whereas creation of a reserve is generally at the discretion of the management. However, in certain cases law has stipulated for the creation of specific reserves.

6**. Use for the payment of dividend**: Provision cannot be used for distribution as dividends while general reserve can be used for dividend distribution.

Types of Reserves:

A reserve is created by retention of profit of the business can be for either a general or a specific purpose.

1. **General reserve**: When the purpose for which reserve is created is not specified, it is called General Reserve. It is also General reserve strengthens the financial position of the business.

2. **Specific reserve**: Specific reserve is the reserve, which is created for some specific purpose and can be utilised only for that purpose.

Reserves are also classified as revenue and capital reserves.

Revenue reserves: Revenue reserves are created from revenue profits which arise out of the normal operating activities of the business.

Examples of revenue reserves are: • General reserve; • Workmen compensation fund; • Investment fluctuation fund; • Dividend equalisation reserve; • Debenture redemption reserve;

Capital reserves: Capital reserves are created out of capital profits which do not arise from the normal operating activities. Such reserves are not available for distribution as dividend.

Examples of capital profits, are: • Premium on issue of shares or debenture. • Profit on sale of fixed assets. • Profit on redemption of debentures. • Profit on revaluation of fixed asset & liabilities. • Profits prior to incorporation. • Profit on reissue of forfeited share

Difference between Revenue and Capital Reserve:

Revenue reserves and capital reserves are differentiated on the following grounds:

1. Source of creation: Revenue reserve is created out of revenue profits, which arise out of the normal operating activities of the business. On the other hand capital reserve is created primarily out of capital profit, which do not arise from the normal operating activities of the business

2. Purpose : Revenue reserve is created to strengthen the financial position, to meet unforeseen contingencies or for some specific purposes. Whereas capital reserve is created for compliance of legal requirements or accounting practices.

3. Usage : A specific revenue reserve can be utilised only for the earmarked purpose while a general reserve can be utilised for any purpose including distribution of dividend. Whereas a capital reserve can be utilised for specific purposes as provided in the law in force, e.g., to write off capital losses or issue of bonus shares.

Secret Reserve :Secret reserve is a reserve which does not appear in the balance sheet. It may also help to reduce the disclosed profits and also the tax liability. The secret reserve can be merged with the profits during the lean periods to show improved profits.

Secret reserve can be created by way of :

• Undervaluation of inventories/stock

• Charging capital expenditure to profit and loss account

• Making excessive provision for doubtful debts

• Showing contingent liabilities as actual liabilities

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Practice Questions:

1. What is ‘Depreciation’?

2. State briefly the need for providing depreciation.

3. What are the causes of depreciation?

4. Explain basic factors affecting the amount of depreciation.

5. Distinguish between straight line method and written down value method of calculating depreciation

Q6. G Ltd. Purchased Machinery for ₹ 80,000 on 1st October, 2018. Depreciation is provided @ 10% p.a. on Diminishing Balance Method. On 1st January, 2021, one-fourth of Machinery was found unsuitable and disposed-off for ₹ 12,000. On the same date, a new machinery at a cost of ₹ 30,000 was purchased. Write-up the Machinery A/c for 4 years. The Accounts are closed o 31st March every year.

Q7. The following balances appear in the books of K Ltd. as on 1st April 2021: ₹ Machinery Account 10,00,000 Provision for Depreciation Account 4,50,000 The machinery was depreciated at 10% p.a. on Fixed Instalment Method-the accounting year being April-March. On 1st October 2021, a machinery which was purchased on 1st July 2018 for ₹ 2, 00,000 was sold for ₹ 84,000 and on the same date a fresh machinery was purchased for ₹ 4, 00,000. Prepare the Machinery A/c and Provision for Depreciation A/c for the year 2021-22.

Q8. D Bros. purchased on 1st April, 2017 a second-hand machinery for ₹ 72,000 and spend ₹ 8,000 on its installation. On 1st Oct. in the same year, another machinery costing ₹ 40,000 was purchased. On 1st Oct. 2019 machinery bought on 1st April, 2017 was sold off for ₹ 24,000 and a fresh machinery was purchased for ₹ 1, 28,000 on the same date. One more machinery was purchased on 1st Sept, 2020 for ₹ 2,40,000. Depreciation is provided annually on 31st March @ 10% p.a. on the written Down Value Method. Show Machinery Account for 4 years ending 31st March, 2021.

Q9.B & Company purchased a machinery on 1st April, 2018, for ₹ 54,000 and spend ₹ 6,000on its installation. On 1st December, 2019, it purchased another machine for ₹ 30,000. On 30th June, 2020 the first machine purchased on 1st April, 2018, is sold for ₹ 36,000 and on the same date it purchased a new machinery for ₹ 80,000. On 1st Dec., 2021, the second machine (purchased on 1st Dec, 2019) was also sold off for ₹ 26,000. Depreciation was provided on machinery @ 10% p.a. on Original Cost Method annually on 31st March. Give the Machinery Account for four years

TRIAL BALANCE & RECTIFICATION OF ERRORS

Meaning of Trial Balance: When posting of all the transactions into the Ledger is completed and accounts are balanced off, then the balance of each account is put on a list called Trial Balance.

Definition: Trial Balance is the list of debit and credit balances taken out from ledger. "It also includes the balances of Cash and bank taken from the Cash Book".

Preparation : Steps (Balance Method)

1. Ledger A/c's which shows a debit balance is put on the Debit side of the trial balance.
2. The A/c Showing credit balance is put on the Credit side of Trial Balance.
3. Accounts which show no balance i.e. whose Debit and Credit totals are equal are not entered in Trial Balance.
4. Then the two sides of the Trial Balance are totalled. If they are equal it is assumed that there is no arithmetical error in the posting and balancing of Ledger A/c's.

Objectives or Functions of Trial Balance:

- It helps in ascertaining the arithmetic accuracy of ledger accounts.
- Helps in locating errors.
- Provides the summary of Ledger A/c's.
- Helps in the preparation of Final A/c's

TRIAL BALANCE as at _______

Account Title	Debit Balance	Credit Balance
• Capital		xxxx
• Land and Buildings	xxxx	
• Plant and Machinery	xxxx	
• Equipment	xxxx	
• Furniture and Fixtures	xxxx	
• Cash in Hand	xxxx	
• Cash at Bank	xxxx	
• Debtors	xxxx	
• Bills Receivable	xxxx	
• Stock of Raw Materials	xxxx	
• Stock of Finished Goods	xxxx	
• Purchases	xxxx	
• Carriage Inwards	xxxx	
• Carriage Outwards		xxxx
• Sales	xxxx	
• Sales Return		xxxx
• Purchases Return	xxxx	
• Interest Paid		xxxx
• Commission/Discount Received	xxxx	
• Salaries		xxxx
• Long Term Loan		xxxx
• Bills Payable		xxxx
• Creditors	xxxx	xxxx
• Advances from Customers		
• Drawings		

Q1 Prepare the trial balance from the following information

PARTICULARS	L.F	Dr.	Cr.
Sundry Debtors		4,10,000	
Sundry Creditors			80.000
Rent &Taxes		48,000	
Purchase		34,00,000	
Sales			56,00,000
Trade Expenses		12,000	
Return Inwards		1,20,000	
Return Outwards			80,000
Expenses		4,000	
Motor Vehicles		6,50,000	
Electricity		25,000	
Opening Stock(1/4/2019)		2,30,000	
Premises		12,00,000	
Fixtures& Fittings		3,10,000	
Bad Debts Written Off		8,000	
Loan From Gopal			1,50,000
Interest On Gopal's Loan		15,000	
Drawing		40,000	
Cash in Hand		75,000	
Rent Received			30,000
Capital			6,07,000
TOTAL		65,47,000	65,47,000

Q2 Prepare the trial balance from the following information-:

Sno.	NAME OF ACCOUNTS	AMOUNT
(I)	Capital	2,00,000
(II)	Cash	1,80,000
(III)	Creditors	1,00,000
(IV)	Sales	3,00,000
(V)	Stock	70,000
(VI)	Debtors	5,000
(VII)	Bank Loan	12,00,000
(VIII)	Purchases	50,00,000

Q3 .Prepare the TRIAL BALANCE from the given information.
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S.no	NAME OF THE ACCOUNT	AMOUNT

1	Cash	2,00,000
2	Purchases	1,200
3	Sales	20,000
4	Purchase Return	5,000
5	Sales Return	6,00,000
6	Transportation	80,000
7	Discount Allowed	1,00,00
8	Printing	9,000
9	Sundry Debtors	1,800
10	Sundry Creditors	700
11	Investments	60,000
12	Plant and Machinery	4,00
13	Building	800
14	Furniture	3,100
15	Electricity	1,00,000
16	Postage	50,000
17	Drawings	2,000
18	Salary	10,000
19	Travelling Expenses	500
20	Bank Loan	1,000

MCQ

1) Agreement of trial balance is affected by:
(a) One sided errors only. (b) Two sided errors only.
(c) Both (a) and (b). (*d*) None of the above

2) If the trial balance agrees, it implies that:
(a) There is no error in the books. (b) There may be two sided errors in the book.
(c) There may be one sided error in the books. (d) There may be both two sided and one sided errors in the books.

3)Trial balance is:
(a) An account. (b) A statement.
(c) A subsidiary book. (d) A principal book

4) A Trial balance is prepared:
(a)After preparation of financial statements
(b)After recording transaction in subsidiary books
(c) After posting in ledger
(d) After posting to ledger is complete and accounts have been balanced.

5)Assets are shown in the trial balance on the
(a) Debit Side (b)Credit Side
(c)Neither debit nor credit (d)Outside the trial balance

6)Most commonly method of preparing trial balance is
(a) Balance method
(b)Totals method
(c)Total-cum- method
(d)None

RECTIFICATION OF ERRORS

Classification of Errors

Keeping in view the nature of errors, all the errors can be classified into the following in four categories:

- Errors of Commission
- Errors of Omission
- Errors of Principle
- Compensating Errors

ERRORS OF COMMISSION

These are the errors which are committed due to wrong posting of transactions, wrong totalling or wrong balancing of the accounts, wrong casting of the subsidiary books, or wrong recording of amount in the books of original entry, etc. For example: Raj Hans Traders paid Rs. 25,000 to Preetpal Traders (a supplier of goods). This transaction was correctly recorded in the cashbook But while posting to the ledger, Preetpal's account was debited with Rs. 2,500. only. This constitutes an error of commission. Such an error by definition is of clerical nature and most of the errors of commission affect in the trial balance.

ERRORS OF OMISSION

The errors of omission may be committed at the time of recording the transaction in the books of original entry or while posting to the ledger. These can be of two types:

(i) errors of complete omission

(ii) errors of partial omission

ERRORS OF COMPLETE OMISSION – When a transaction is completely omitted from recording in the books of original record, it is an error of complete omission.

FOR EXAMPLE- Credit sales to Mohan ₹. 10,000, not entered in the sales book.

ERRORS OF PARTIAL OMISSION - When the recording of transaction s is partly omitted from the books, in the above EXAMPLE, credit sales had been duly recorded in the sales book but the posting from sales book to Mohan's account has not been made, it would be an error of partial omission.

ERRORS OF PRINCIPLE –

Accounting entries are recorded as per the generally accepted accounting principles. If any of these principles are violated or ignored, errors resulting from such violation are known as errors of principle. An error of principle may occur due to incorrect classification of expenditure or receipt between capital and revenue. This is very important because it will have an impact on financial statements. It may lead to under/over stating of income or assets or liabilities, etc.

ERROR OF COMPENSATING

When two or more errors are committed in such a way that the net effect of these errors on the debits and credits of accounts is nil, such errors are called compensating errors. Such errors do not affect the tallying of the trial balance.

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RECTIFICATION OF ERRORS

From the point of view of rectification, the errors may be classified into the Following into two categories:

(a) errors which do not affect the trial balance.

(b) errors which affect the trial balance.

This distinction is relevant because the errors which do not affect the trial balance usually take place in two accounts in such a manner that it can be Easily rectified through a journal entry whereas the errors which affect the trial balance usually affects one account and a journal entry is not possible for Rectification unless a suspense account has been opened.

RECTIFICATION OF ERROR WHICH DO NOT AFFECT THE TRIAL BALANCE-

These errors are committed in two or more accounts. Such errors are also known As two sided errors. They can be rectified by recording a journal entry giving the Correct debit and credit to the concerned accounts.

The rectification process essentially involves:
• Cancelling the effect of wrong debit or credit by reversing it; and
• Restoring the effect of correct debit or credit.
For this purpose, we need to analyse the error in terms of its effect on the Accounts involved which may be:
(i) Short debit or credit in an account; and/or
(ii) Excess debit or credit in an account.
Therefore, rectification entry can be done by:
(i) Debiting the account with short debit or with excess credit,
(ii) Crediting the account with excess debit or with short credit.
The procedure for rectification for such errors is explained with the help of Following examples:
(a) Credit sales to Mohan ₹. 10,000 were not recorded in the sales book. This is an error of complete omission. Its affect is that Mohan's account has not been debited and Sales account has not been credited. Accordingly, recording usual entry for credit sales will rectify the error.

MOHAN's A/C	Dr.	10,000	
TO SALE's A/C			10,000

RECTIFICATION OF ERROR WHICH AFFECT THE TRIAL BALANCE –

The errors which affect only one account can be rectified by giving an explanatory note in the account affected or by recording a journal entry with the help of the Suspense Account. such errors are error of casting; error of carrying forward; error of balancing; error of posting to correct account but with wrong amount ; error of posting to the correct account but on the wrong side ; posting to the wrong side with the wrong amount; omitting to show an account in the trial balance . Take for example a case where Shyam's account was credited short by Rs.

190. This will be rectified by an additional entry for ₹.190 on the credit side of his account as follows

Date	Particulars	J.f	Amount	Date	Particular	J.f	Amount
					Difference in amount posted short on.....		190

Take another example, purchases book was under cast by ₹. 1,000. The effect of this entry is on purchases account (debit side) where the total of purchases book is posted

Date	Particulars	J.F	Amount	Date	Particulars	J.F	Amount
	Under casting purchases book for the month of....		1,000				

SUSPENSE ACCOUNT

Even if the trial balance does not tally due to the existence of one sided errors, accountant has to carry forward his accounting process prepare financial statements. The accountant tallies his trial balance by putting the difference on shorter side as 'suspense account'.

EXAMPLE OF SUSPENSE ACCOUNT

Q1) Rectify the following errors assuming that a suspense account was opened ascertain the difference in trial balance

(i) Credit sales to Arun ₹. 7,000 were posted to credit of his account

(ii) Credit purchase from Brij ₹. 9,000 were posted to the debit of his account as ₹.6,000

(iii) Goods returned to Charu ₹.8000 were posted to the credit of her account

(iv) Goods retuned from Deepika ₹. 1,000 were posted to the debit of her account as ₹. 2,000

(v) Cash sales ₹. 2,000 were posted to the debit of sales account as ₹.5,000

ANS 1)

Date	Particulars	L.F	Amount Dr.	Amount Cr.
(i)	Arun A/c Dr. TO Suspense A/c (Credit sales to arun wrongly credited to his account ,NOW RECTIFIED)		14,000	14,000
(ii)	Suspense A/c Dr. TO Brij A/c (Credit purchase from brij Rs. 9,000 wrongly debited to his account as Rs.6,000, NOW RECTIFIED)		15,000	15,000
(iii)	Charu A/c Dr. TO Suspense A/c (Goods returned to charu wrongly credited to her account , NOW RECTIFIED		8,000	8,000
(iv)	Suspense A/c Dr. TO Deepika A/c (Goods returned from deepika Rs. 1,000 wrongly debited to her account as Rs. 2,000 ,NOW RECTIFIED)		3,000	3,000
(v)	Suspense A/c Dr. TO Sales A/c (Cash sales Rs. 2,000 wrongly debited to sales account as Rs. 5,000,NOW RECTIFIED)		7,000	7,000

SUSPENSE A/C

Dr. Cr.

PARTICULARS	L.F	AMOUNT	PARTICULARS	L.F	AMOUNT
TO Brij TO Deepika TO Sales		15,000 3,000 7,000	By Charu By Arun		14,000 8,000
		25,000			22,000
			By balance c/d		3,000
					25,000
TO balance b/d		3,000			

SOME QUESTIONS FOR PRACTICE

Q1) Rectify the following errors:

Credit purchases from Raghu   Rs. 20,000

(i) Were not recorded.
(ii) Were recorded as Rs. 10,000.
(iii) Were recorded as Rs 25,000.
(iv) Were not posted to his account.
(v) Were posted to his account as 2,000
(vi) Were posted to Raghav's account.
(vii) Were posted to the debit of Raghu's account.
(viii) Were posted to the debit of Raghav.
(ix) Were recorded through sales book.

Q2) Trial balance of Anurag did not agree. It showed an excess credit Rs. 10,000. Anurag put the difference to suspense account. He located the following errors:

(i) Sales return book over cast by Rs.1, 000.
(ii) Purchases book was undercast by Rs. 6,00
(iii) Goods returned to Ram Rs. 1,000 were recorded through sales book.
(iv) Credit purchases from M & Co. Rs. 8,000 were recorded through sales book.
(v) Salary paid Rs. 2,000 was debited to employee's personal account.

Q3) TICK THE CORRECT

I) Agreement of trial balance is affected by:

(a) One sided errors only.
(b) Two sided errors only.
(c) Both (a) and (b).
(d) None of the above.

II) Which of the following is not an error of principle

(a) Purchase of furniture debited to purchases account.
(b) Repairs on the overhauling of second hand machinery purchased debited to repair account
(c) Cash received from Manoj posted to Saroj.
(d) Sale of old car credited to sales account.

III) Which of the following is not an error of commission:

(a) Over casting of sales book.
(b) Credit sales to Ramesh Rs. 5,000 credited to his account.
(c) Wrong balancing of machinery account.
(d) Cash sales not recorded in cash book.

VI) If suspense account does not balance off even after rectification of errors it implies that

(a) There are some one sided errors only in the books yet to be located.
(b) There are no more errors yet to be located.
(c) There are some two sided errors only yet to be located.

(d) There may be both one sided errors and two sided errors yet to be located.

Q4) Give two examples of errors of principle?

Q5) Give two examples of errors of commission?

Q6) what is a suspense account? Is it necessary that is suspense account will? Balance off after rectification of the errors detected by the accountant? If Not, then what happens to the balance still remaining in suspense account?

Q7) Rectify the following errors:

(i) Credit sales to Mohan Rs.7,000 were not recorded

(ii) Credit purchases from Rohan Rs. 9,000 were not recorded.

(iii) Goods returned to Rakesh Rs. 4,000 were not recorded.

(iv) Goods returned from Mahesh Rs. 1,000 were not recorded.

Q8) Rectify the following errors:

(i) Salary paid Rs. 5,000 was debited to employee's personal account.

(ii) Rent Paid Rs. 4,000 was posted to landlord's personal account.

(iii) Cash received from Kohli Rs.2,000 was posted to Kapur's account.

(iv) Cash paid to Babu Rs. 1,500 was posted to Sabu's account.

Q9) Rectify the following errors and ascertain the amount of difference in trial balance by preparing suspense account:

(i) Credit sales to Mohan Rs. 7,000 were posted as Rs. 9,000.

(ii) Credit purchases from Rohan Rs.9,000 were posted as Rs.6,000.

(iii) Goods returned to Rakesh Rs. 4,000 were posted as Rs. 5,000.

(iv) Goods returned from Mahesh Rs.1,000 were posted as Rs. 3,000.

(v) Cash sales Rs. 2,000 were posted as Rs. 200

Q10) Rectify the following errors assuming that suspension account was opened. Ascertain the difference in trial balance.

(I) Furniture purchased for ₹ 10,000 wrongly debited to purchase account as ₹ 4,000

(II) Repairs on machinery ₹ 1,400 debited to Machinery account as ₹ 2,400

(III) . Repairs on overhauling of second hand machinery purchased ₹ 2,000 was debited to Repairs account as ₹ 200.

(IV) Sale of old machinery at book value ₹ 3,000 was credited to sales account as Rs.5,000

Q11) Trial balance of Anuj did not agree. It showed an excess credit of ₹ 6,000. He put the difference to suspense account. He discovered the following error

(I) Cash received from Ravish ₹ 8,000 posted to his account as ₹ 6,000.

(II) Returns inwards book overcast by ₹ 1,000.

(III) Total of sales book ₹ 10,000 was not posted to Sales account.

(IV) Credit purchases from Nanak ₹ 7,000 were recorded in sales Book. However, Nanak's account was correctly credited

(V) Machinery purchased for ₹ 10,000 was posted to purchases account as ₹ 5,000. Rectify the errors and prepare suspense account

Rectify the errors and prepare suspense account to ascertain the difference in trial balance.

FINANCIAL STATEMENTS OF SOLE PROPRIETORSHIP

"Financial Statements of a company shows its financial position for the current year"

Meaning :

The financial statements provide a summary of the accounts of a business enterprise.

Financial statements include two statements include two statements:

i) 'Trading and Profit and Loss Account' or Income Statement' (To Know Profit or loss)

ii) Balance Sheet (To know value of assets and liabilities on the closing date of an accounting period)

The basic objectives of preparing financial statements are :

(a) To present a true and fair view of the financial performance of the business;

(b) To present a true and fair view of the financial position of the business; and

For this purpose, the firm usually prepares the following financial statements:

1. Trading and Profit and Loss Account 2. Balance Sheet

Capital Nature Items:

Capital Expenditure: Those expenditures which are incurred in acquiring and increasing the value of fixed assets. Ex.

1. Purchase of fixed assets or bringing into existence of fixed assets
2. Expenditure incurred on erection of a fixed asset
3. Payment of goodwill
4. Decrease in long term debts.
5. Capital Receipts: Any receipt from the sale of fixed assets is known as capital receipt.

Revenue Nature items :

Revenue Receipts: Receipts in the business of recurring nature are called as Revenue receipts ex: rent received, discount received, commission received

Revenue Expenditures: Recurring nature of expenditure done in the business which are done in order to earn profit are known as revenue expenditure ex.:

1. Purchase of goods during the year
2. Money spent in acquiring or manufacturing goods like freight, carriage, wages etc.

Any expenses for meeting day to day business like wages, salaries, postage etc.

Distinction between Capital Expenditure and Revenue Expenditure

S.No	Basis	Capital expenditure	Revenue expenditure
1	Purpose	Money spent for purchasing a fixed asset for business.	Money spent for the conduct of the business.
2	Benefit duration	For several years	For one accounting period only.
3	Presentation	Shown in the Balance sheet.	Shown either in Trading A/c or in Profit and Loss A/c.
4	Nature of account	Real account	Nominal account

Trading Account: Trading account is prepared to know the result of manufacturing and trading activities:

FORMAT OF TRADING ACCOUNT

Trading Account

Dr. **for the year ended ………………**Cr.

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Opening Stock	…………	By Sales	
To Purchases	……..	………..	……………
Less : Purchases returns		Less : Sales return	………….
To wages	…………	……….	……………
To wages & salaries	…….	By closing stock	
To carriage/carriage inwards/carriage	…………	By Gross loss	
on purchases	…….	transferred TO Profit	
To Direct expenses	…………	and loss A/c	
To Gas, fuel and power	…….	(balancing figure)	
To Freight, octroi and cartage	…………		
To manufacturing expenses	………		
To custom/import duty	…………		
To Dock and clearing charges	…….		
To Excise duty	…………		
To Factory rent and lighting	………		
To Royalty	…………		
To Gross profit Transferred to Profit	……..		
and loss A/c(balancing figure)	…………		
	……….		

Ex: Prepare A Trading Account from the following particulars for the year ended March 31, 2007.

Opening Stock	56,250
Purchases	157500
Sales	405000
Wages	45000

Solution :

Trading Account for the year ended March 31, 2007

Particulars	Amount	Particulars	Amount
To Opening Stock	56,250	By Sales	4,05,000
To Purchases	1,57,500		
To Wages	45,000		
To Gross Profit	1,46,250		
	4,05,000		4,05,000

Question for Practice :

Prepare a Trading Account from the following particulars for the year ended 31st March, 2011

	Rs.		Rs.
Opening Stock	30,000	Wages	18,000
Purchases	1,00,000	Carriage on purchases	3,000
Sales	2,05,000	Manufacturing Exp.	20,000
Factory rent	10,000	Custom Duty	4,500
Purchases returns	3,000	Gas, Fuel and power	12,000
Sales returns	5,000	Dock charges	3,000

COST OF GOODS SOLD

Cost of goods sold is computed in two ways :

(i) Cost of goods sold or cost of sales = Sales – Gross profit
(ii) Cost of goods sold = Opening stock + Purchases + Direct expenses – Closing stock

Example: Find the cost of goods sold and closing stock from the following information:

Sales Rs. 4,30,000; Return inward Rs. 5,000; Gross profit Rs. 1,00,000; Opening stock Rs. 35,000 Purchases Rs. 2,85,000; Wages Rs. 27,000; Other direct expenses Rs. 16,000.

SOLUTION:

(A) Net Sales = Sales – Sales return
= 4,30,000 – 5,000 = 4,25,000

(b) Cost of goods sold = Sales – Gross profit

= 4,25,000 – 1,00,000 - = 3,25,000

(c) Cost of goods sold = Opening stock + Purchase + Direct expenses – Closing stock

3,25,000 = 35,000 +2,85,000 + (27,000 + 16,000) – closing stock

Closing stock = 3,63,000 - 3,25,000 = Rs. 38,000

OPERATING PROFIT AND NET PROFIT

After getting Gross Profit from the business. Profit may be divided into two parts :
1 Operating Profit, 2 Net Profit
Similarly, sales constitute the main item of revenue for the business. The excess of sales over purchases and direct expenses is called gross profit. If the amount of purchases including direct expenses is more than the sales revenue, the resultant figure is gross loss. The computation of gross profit can be shown in the form of equation as : Gross Profit = Sales – (Purchases + Direct Expenses)

Operating Profit: Operating profit is that profit which is earned through the normal activities of the business. It can be ascertained by deducting all operating expenses from the gross profit.

2. Net Profit: Net profit is that profit which is earned after deducting all operating as well as non-operating expenses from the Gross Profit

Profit and Loss Account :
Profit and loss account is prepared to know the result of the business in the term of net profit

FORMAT OF PROFIT AND LOSS ACCOUNT

Profit and Loss A/c

Dr. **for the year ended ………………….** Cr.

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Gross loss Office and administrative expenses: To salaries To Salaries & Wages To Rent, rates and taxes To printing and stationery To Telephone expenses To Unproductive expenses To Postage and telegrams To lighting/Electricity To Insurance premium To Travelling expenses To Establishment expenses To Audit fees To Legal charges To Trade expenses To General expenses/misc. expenses Selling and Distribution expenses : To carriage outwards/carriage on sales To Advertisement To Commission To Export duty To packing Charges To discount allowed		By Gross profit By rent received By discount received By commission received By interest on investments By dividend on shares By Apprentice premium By Bad debts recovered By profit on sale of assets By Misc. receipts By income from other sources By Net loss (if any) transferred to Capital A/c	

To Bad debts To delivery van expenses To Sales tax To conveyance expenses To Godown rent Financial and other charges : To repairs and renewals To Depreciation To Interest on loan To Donation and charity To Bank charges To loss on sale of assets To Net Profit transferred to Capital A/c			

Question for Practice:

Prepare Profit and Loss Account for the year ended 31st March, 2020 from the following particulars:

	Rs.		Rs.
Gross profit	90,500	Discount allowed	600
Trade expenses	2,400	Lighting	4,100
Rates and taxes	1,200	Interest on investment	500
Carriage outwards	7,500	Commission received	600
Salaries	13,600	Bad debts	1,000
Postage and telegram	2,400	Discount (Cr.)	600
Rent	9,000	Interest on loan	1,800
Legal charges	2,000	Stable expenses	1,600
Audit fee	2,400	Export duty	2,200
Depreciation	2,000	Miscellaneous receipts	200
Donation	500	Unproductive wages	2,100
General expenses	1,500	Travelling expenses	3,500
Selling expenses	4,000		

Solution:

Profit and Loss Account

(for the year ended 31st March 2020)

Particulars	Amount	Particulars	Amount
To Trade expenses	2,400	By Gross profit b/d	90,500
To Carriage outwards	7,500	By commission received	600
To Salaries	13,600	By Discount	600
To Postage and telegram	2,400	By Miscellaneous receipts	200
To Rent	9,000	By interest on investment	500
To Rates and taxes	1,200		
To Legal charges	2,000		
To Audit fee	2,400		

To Depreciation To Donation To General Expenses To Selling expenses To Discount allowed To Lighting To Bad Debts To Interest on loan]To Stable expenses To Export duty To Unproductive wages To Traveling expenses To Net Profit transferred to capital account	2,000 500 1,500 4,000 600 4,100 1,000 1,800 1,600 2,200 2,100 3,500 27,000		
	92,400		92,400

Question for Practice:
From the following trial balance of Raj & Co. prepare trading and profit and loss A/c for the year ending 31st March 2021 .

Debit Balance	Amount	Credit Balance	Amount
Stock	16,000	Sundry Creditors	20,000
Purchases	55,000	Purchases returns	1,000
Sales Returns	2,000	Sales	1,03,000
Carriage	3,500	Commission	4,500
Wages	12,500	Capital	56,000
Salaries	10,000	Bills Payable	8,500
Printing and stationery	3,400	Bank Loan	20,000
Trade expenses	2,000		
Cash in hand	3,500		
Bills receivables	8,000		
Sundry Debtors	22,000		
Land and buildings	30,000		
Plant and machinery	20,000		
Drawings	8,000		
Furniture and fixtures	10,600		
Rent and taxes	6,500		

Balance Sheet The Balance Sheet is a statement prepared for showing the financial position of the business summarizing its assets and liabilities at a given date.
Grouping and Marshalling of Assets and Liabilities: Grouping: The term 'Grouping' means putting together items of a similar nature under a common heading. For example, under the heading 'trade Creditors' the balances of the ledger accounts of all the suppliers from whom goods have been purchased on credit, will be shown.
Marshalling: It refers to the order in which the various assets and liabilities are shown in the Balance Sheet. The assets and liabilities can be shown either in the order of liquidity or in the order of permanence.

Order of Liquidity: 1. The assets are arranged in the order of their liquidity i.e., the most liquid asset (e.g., cash-in-hand), is shown first. The least liquid asset (e.g., goodwill) is shown last.
2. The liabilities are arranged in the order of timing i.e., the liabilities which are to be paid immediately {e.g., Creditors) are shown first and which are to be paid later are shown at last (longterm loans).

FORMAT OF BALANCE SHEET

Balance Sheet

as on………………………….

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Current Liabilities :		Current Assets :	
Bank overdraft	………….	Cash in hand	………….
Bills payable	…………	Cash at bank	………….
Sundry creditors	…………	Bills receivable	………….
Outstanding expenses	…………..	Short term investments	…………..
Unearned income	…………..	Sundry debtors	…………
Long term liabilities :	…………..	Closing stock	………..
Long term loans	…………..	Prepaid expenses	…………
		Accrued income	
Capital :			
Add : Net profit		Long term Investments:	…………..
…………..			
Less : Drawings		Fixed Assets :	
…………..	……………..	Furniture and fixtures	……………
Less : Income tax		Motor vehicles	…………..
………….		Plant and Machinery	…………..
Less : Life insurance premium		Land and building	……………
……….		Patents/Copyrights	…………..
		Goodwill	……………
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Order of Permanence: This order is exactly reverse of the liquidity order
1. The assets are arranged in the order of their permanence i.e., the least liquid asset (e.g., goodwill) is shown first and the most liquid asset (e.g., Cash-in-hand) is shown last.
2. The least urgent payment to be made (e.g., short-term creditors) is shown last.
3. A company is required to prepare the balance sheet in the order of permanence. Important

Adjustments with their treatments

S.N.	Adjustment		Treatments
1	Closing Stock	:	Credit Side of Trading and Asset Side of B/S
2	Outstanding expenses	:	Add with concerned item in trading or profit and loss a/c and Liabilities side of B/S
3	Prepaid expenses	:	Less from concerned item in trading or profit and loss a/c and assets side of B/S
4	Accrued Income	:	Add with concerned income in P&L and Asset Side of B/S
5	Income Received in advance	:	Less from concerned item in P&L A/c and Liabilities side of B/S
6	Depreciation	:	Dr.Side of P&L A/c & Deduct from concerned asset in Balance sheet
7	Bad Debts	:	Dr.Side of P&L A/c & Deduct from debtors in B/S
8	Provision for doubtful debts	:	Dr. Side of P&L A/c and Deduct from Debtors
9	Provision for Discount on debtors	:	Dr. Side of P&L A/c and Deduct from Debtors
10	Manager's Commission	:	Dr.Side of P&L and Liabilities side of B/S

METHOD FOR CALCULATION OF MANAGER'S COMMISSION

(i) On net profit before charging such commission
Manager's commission = Net profit X Rate/100

(ii) On net profit after charging such commission :
Manager's commission = Net profit X Rate/ 100+ Rate

Wasting Assets: - Assets which are exhausted during the working are called wasting assets. For exp. Mines, oil wells etc.

Contingent liabilities: - Liabilities the happening of which is uncertain are called contingent liabilities. For exp. – case of bonus pending in the court, bill discounted not yet matured. It is stated as footnote below the balance sheet.

Ex:

From the following figures prepare Trading and Profit and Loss Account for the year ended 31st March, 2020 and a Balance Sheet as on that date :

Capital	86,800
Drawing	15,000
Investments	14,000
Cash	8,000
Rent and Insurance	3,000

Opening Stock	36,600
Purchases	1,86,000
Sales	3,05,000
Sales return	5,000
Wages	22,000
Carriage	4,200
Bad debts	700
Bad debts provision	2,100
Sundry debtors	40,400
Sundry creditors	25,700
Furniture	8,000
Plant and machinery	50,000
Salaries	11,000
Advertisement	4,400
Goodwill	6,000
Freight	6,300
Commission (Cr.)	1,000

Adjustments:

1. Stock on 31st march 2020 was Rs. 31,500
2. Salary and wages for March 2020 were unpaid.
3. Rent outstanding amounted to Rs. 600 and insurance unexpired amounted to Rs. 400.
4. Commission amounting to Rs. 200 has been received in advance.
5. Write off Rs. 400 as bad debts, create provision for doubtful debts at 5% on sundry debtors and provide 2% provision for discount on debtors and creditors.
6. Depreciate furniture and plant and machinery by 10%.

Solution:

Trading and Profit and Loss Account

For the year ending 31st March 2020

Particulars		Amount	Particulars		Amount
To Opening Stock		36,600	By Sales	3,05,000	
To Purchases		1,86,000	Less : Sales Return	5,000	3,00,000
To Wages	22,000		By Closing Stock		31,500
Add : Outstanding	2,000	24,000			
To Carriage		4,200			
To Freight		6,300			
To Gross Profit c/d		74,400			
		3,31,500			3,31,500
To Bad Debts	700		By Gross Profit b/d		74,400
Add : Further Bad Debts	400		By Commission	1,000	
New Provision	2000		Less : Unearned	200	800
	3100		By Provision for Discount on		
Less : Old Provision	2100	1,000	Creditors		514
To Provision for Discount on debors		760			
To Salary	11,000				

Add:	1,000	12,000		
To Advertisement		4,400		
To Rent and Insurance	3,000			
Add : Outstanding Rent	600			
	3600			
Less :Prepaid Insurance	400	3200		
To Depreciation on				
Furniture	800			
Plant and Machinery	5,000	5,800		
To Net Profit transferred to				
Capital A/c		48,554		
		75,714		75,714

Balance Sheet (As on 31st March, 2020)

Liabilities		Amount	Assets		Amount
Salaries outstanding		1,000	Cash		8,000
Wages outstanding		2,000	Sundry Debtors	40,400	
Outstanding Rent		600	Less : Bad Debts	400	
Unearned commission		200		40,000	
Creditors	25,700		Less : New Prov. for		
Less : Prov.for discount	514	25,186	Bad Debts.	2,000	
Capital	86,800			38000	
Add : Net Profit	48,554		Less : Prov. for discount	760	37240
	1,35,354		Closing Stock		31,500
Less : Drawing	15,000	1,20,354	Insurance Prepaid		400
			Investment		14,000
			Furniture	8,000	
			Less : Depreciation	800	7,200
			Plant and Machinery	50,000	
			Less : Depreciation	5,000	45,000
			Goodwill		6,000
		1,49,340			1,49,340

Question for Practice:

Following is the Trial Balance of Rama & Co. for the year ending 31st December 2010. Prepare Trading and Profit and Loss Account and Balance Sheet:

Name of Account	Dr. Balance	Cr.Balance
Drawing and Capital	4.000	23,000
Furniture	8,000	-
Apprentice Premium	-	1,000
Machinery	20,000	-
Bad debts	350	-
Provision for bad debts	-	500

Sundry debtors and Creditors	8,200	5,000
Stock on January 1, 2010	7,400	-
Purchases and sales	75,000	1,05,000
Bank overdraft	-	2,600
Sales return and purchase returns	500	400
Advertisement	2,400	-
Interest	200	-
Commission	-	400
Cash in hand	1,650	-
Taxes and Insurance	3,200	-
Carriage and Freight	1,500	-
Salaries	5,500	-

Adjustments :

The following adjustments are to be made :

(i) Stock in hand on 31st December 2010 was value Rs. 8,250/-

(ii) Salary is paid at Rs. 500 for month.

(iii) Tax outstanding Rs. 300 and insurance is prepaid Rs 400.

(iv) Write off furniture bad debts Rs. 200 and create provision for bad debts on debtors at 5%.

(v) Apprentice Premium Rs. 300 is related to 2011.

(vi) Commission Accrued Rs. 100.

Ans. G.P. 29250, NP 18300 and B/S 46000

<u>Common mistakes by students:</u>

1- Calculation of Cost of Goods Sold

Solution : To calculate Cost of Goods Sold the following formula will be applied :

COGS = Opening Stock + Net Purchase + Direct Expenses (Carriage on purchase + wages) – Closing Stock

2- Confusion in calculating operating profit :

Solution: To calculate operating profit the following formula will be used :

Operating Profit = Net Profit + Non Operating Expenses – Non Operating Incomes

3- Marshalling and Grouping of Assets and Liabilities:

Solution: Arrangement of assets and liabilities in a particular order is known as marshalling.

4- Provision for Bad Debts:

First of all deduct bad debts given in adjustment from the debtors

Calculate provision for doubtful debts on the amount of debtors

Deduct the amount of provision for doubtful debts given in credit side of trial balance

Questions for practice:

1. What are financial statements?
2. Differentiate Capital Expenditure and Revenue Expenditure
3. Differentiate Capital Receipts and Revenue Receipts.
4. Prepare Final Accounts of Mr. Sharad for the year 31-3-21.

Trial Balance 31-3-21

Particulars	Amount	Particulars	Amount
Stock	20,000	Capital	1,60,000
Purchases	2,92,000	Sales	5,90,000
Duty and clearing charges	34,000	Rent	19,000
Rent	10,000	Creditors	1,35,000
Return inwards	16,000		
Discount	15,000		
Drawings	58,100		
Goodwill	16,000		
Furniture and Fittings	58,000		
Repairs	2,900		
Bank	24,000		
General expenses	18,000		
Salaries	1,10,000		
Debtors	2,30,000		
	9,04,000		9,04,000

Adjustments:

i. General expenses include Rs. 5,000 chargeable to furniture purchased on 1st October 2020.
ii. Create a reserve of 5% on Debtors for Bad and Doubtful debts after treating Rs. 30,000 as a Bad Debt.
iii. Balance at Bank as ascertained from the pass book is Rs. 22,500, the difference representing bank charges.
iv. Rent for 2 months is outstanding.
v. Depreciate furniture and fittings @ 10% p.a.
vi. Closing Stock was Rs. 40,000. There was a loss by fire on 20th March to the extent of Rs. 8,000. Insurance Company admitted the claim in full.
vii. Goods costing RS. 2,500 were used by the proprietor.
viii. Goods costing Rs. 1,500 were distributed as free samples.

Ans. G.P. 2,80,000, N.P. 97050 B/S 3,33,450

5. From the following Trial Balance of Mr.Sarthak for the year ended 31st March 2021.. Prepare Final Accounts.

Particulars	Amount	Amount

Capital	-	2,73,000
Furniture and fittings	48,100	-
Cash at Bank	73,230	-
Land and Building	4,94,000	-
Stock	10,530	-
Debtors and Creditors	84,890	26,780
Purchase and Sales	3,55,790	6,77,120
Carriage outwards	4,030	-
Salaries	54,210	-
General expenses	31,200	-
10% Loan "(1-4-2010)	-	2,60,000
Returns	1,690	1,430
Rent	1,820	-
Wages	71,170	-
Interest	13,000	-
Bills Payable	-	8,970
Electricity Charges (Factory)	3,640	-
	12,47,300	12,47,300

Additional Information :

1. Goods costingRs. 5,200 were taken by Sarthan for the personal use.
2. Salaries include Rs. 2,210 paid for the year ending 31-12-2021.
3. The debtors include Rohan who owned us Rs. 1,690 and has become insolvent and nothing is recoverable from his estate.
4. General expenses include Rs. 2,600 paid for wages.
5. Create a provision for doubtful debts @ 5% p.a.
6. Depreciate land and building @ 10% p.a. and furniture and fittings @ 20% p.a.
7. Closing stock was valued at Rs.20,280.

(Ans. G.P. Rs. 2,58,610 N.P. Rs. 81,290, Balance Sheet Rs.6,57,840)