Training Material: Introduction to Accounting of Transactions — With Specific Reference to MGNREGA Scheme

A JOINT INITIATIVE OF
Ministry of Rural Development, Government of India
& Professional Development Committee of the ICAI

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Foreword

The Mahatma Gandhi National Rural Employment Guarantee Act, 2005 (MGNREGA), notified in 2005, mandated to provide 100 days of guaranteed wage employment in a financial year to every household whose adult members volunteer to do unskilled manual work. Taking the forward steps, ICAI approached the Ministry of Rural Development (MoRD) to provide support in guidance for accounting and auditing of the transactions under MGNREGA. The Training Material on Accounting of the transactions under the scheme of MGNREGA has been prepared.

As you all are aware, MGNREGA is a powerful instrument for inclusive growth in rural India through its impact on social protection, livelihood security and democratic empowerment. Any shortcoming in implementation will always need to be closely looked into and rectified.

Implementation of the MGNREGA involves roles and responsibilities of a large number of stakeholders from the village to the national level. The key stakeholders are Wage seekers, Gram Sabha (GS), Three-tier Panchayati Raj Institutions (PRIs), the Gram Panchayat (GP), Block Panchayat, Zilla Panchayat, Programme Officer (PO) at the Block level, District Programme Coordinator (DPC), State Government, Civil Society, and Other stakeholders [viz. line departments, convergence departments, Self-Help Groups (SHGs), etc.].

The nodal Ministry in the Government of India for MGNREGA is Ministry of Rural Development (MoRD), who has issued the guidance to all the States to conduct the training programme. The Ministry ensures timely and adequate resource support to the States and also undertakes review, monitoring and evaluation of processes and outcomes.

I am happy to note that the Professional Development Committee (PDC) of ICAI has brought Background Training Material on accounting of the transactions under MGNREGA. After training on accounting, the accounts under the said scheme could be prepared more systematically to facilitate the audit of the accounts by the members of ICAI and various reporting requirement to the sanction/disbursing authorities.

I would like to thank Chairman, PDC, CA. Shyam Lal Agarwal and his dynamic team for bringing out Background training material on accounting of transactions under MGNREGA. I am sure this background material would of great value addition and use for all the participants.

Date: 1st July, 2014 CA. K. Raghu

Place: New Delhi *President, ICAI*

PREFACE

A meeting with the Ministry of Rural Development, Government of India with representatives of State Governments was held at Krishi Bhawan, New Delhi in June, 2012 to discuss the arrangement for engaging CA firms for audit of MGNREGA Accounts at Gram Panchayat (GP) Level.

A circular on Framework for Certification of Accounts and Financial Audit of MGNREGA accounts at GP Level by Chartered Accountants was released by Ministry of Rural Development in June 2012,wherein, they had mentioned that pursuant to the provisions of 24(1) of MGNREGA Act and with the objective of bringing in more transparency and accountability in management and deployment of MGNREGA funds at the GP level, Ministry of Rural Development, Government of India proposed to get GP accounts of the schemes formulated by the States under Section 4 of MGNREGA and to be audited and certified by the Chartered Accountants in accordance with the guidelines.

Various meetings were held with the officials of the MoRD, GoI for having the proper accounting and reporting of the transactions under MGNREGA and therefore to have the training programmes in the States.

In the last meeting held on 4th March,2014 with the officials of MoRD, it was discussed to direct the States to conduct the training programmes under the guidance and programmes of accountants at Gram Panchayat level to be organised through ICAI and in the matter to incur/bear expenses on such training programs it was approved that such expenses may be incurred out of 6% administrative cost allowed out of MGNREGA funds. The letter bearing such sanction has also been issued by MoRD.

The PDC of ICAI has already issued the letters to all the State Governments for conducting the training programmes and the meetings are also being held from time to time. It is expected that the first training program of its kind would be held shortly.

It was precise that Professional Development Committee comes out with a training module for such programs. I am thankful to CA Dinesh Kumar Garg and CA. Ravi Mansaka for preparation and their valuable contribution by providing deep insight into the intricacies of the same. I am also thankful to the Secretary PDC and PDC secretariat and particularly CA. Anuj Kaushik for putting all efforts for the same.

I hope this training material will provide the basic guidance for accounting the transaction in a manner to facilitate not only smooth audit but also to the various reporting requirements to control and monitor the scheme.

Date: 1st July, 2014 — (CA. Shyam Lal Agarwal)

Place: New Delhi — *Chairman, Professional Development Committee*

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Chapter 1
Introduction to Accounting

“Accounting is as old as money itself”. Since in early ages commercial activities were based on barter system, record keeping was not a necessity. The Industrial Revolution of 19th century along with rapid rise in population, paved way for the development of commercial activities, mass production and credit terms. Thus recording of business transaction has become an important feature. In recent years with the change of technologies and marketing along with stiff competition, accounting system has undergone remarkable changes.

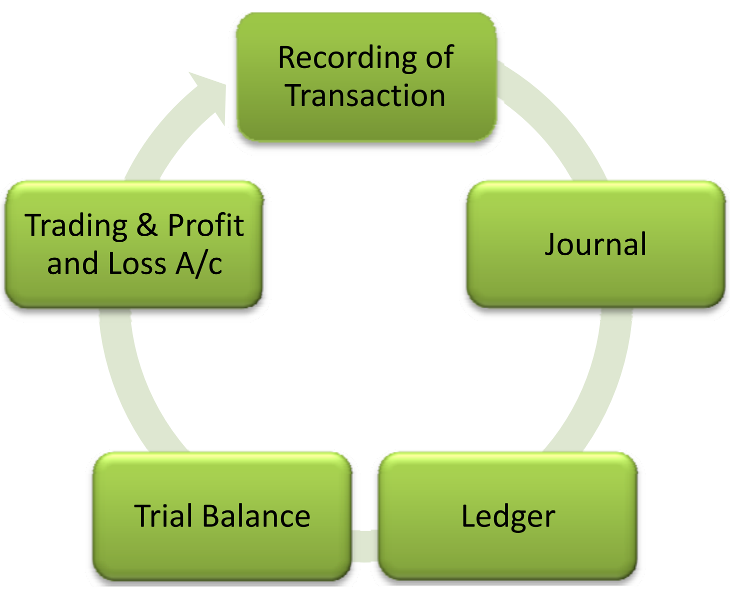
Over the years accountancy has made tremendous progress in the field of commerce and industry. Accounting can be described as being concerned with measurement and management. Measurement of recording transactions and management with the use of data for making decisions are the two fundamental aspects.

Definition of Accounting:-

> “Accounting is the art of recording, classifying and summarising in a significant manner and in terms of money, transactions and events, which are, in part atleast, of a financial character, and interpreting the result thereof.” — American Institute of Certified Public Accountants

Accounting Process starts with recording of business transactions in the journal or subsidiary books and passing through the ledger and trial balance. It results in the preparation of finals accounts i.e., Trading & Profit and Loss A/c and Balance Sheet.

ACCOUNTING CYCLE/ACCOUNTING PROCESS



Book-keeping

Book-keeping is that branch of knowledge which tells us how to keep a record of business transactions. It is often routine and clerical in nature. It is important to note that only those transactions related to business which can be expressed in terms of money are recorded. The activities of book-keeping include recording in the journal, posting to the ledger and balancing of accounts.

Accounting

Book-keeping does not present a clear financial picture of the state of affairs of a business. When one has to make a judgement regarding the financial position of the firm, the information contained in these books of accounts has to be analysed and interpreted. It is with the purpose of giving such information that accounting came into being.

Accounting is considered as a system which collects and processes financial information of a business. These information are reported to the users to enable them to make appropriate decisions.

Accounting, as an information system is the process of identifying, measuring and communicating the economic information of an organization to its users who need the information for decision making. It identifies transactions and events of a specific entity. A transaction is an exchange in which each participant receives or sacrifices value. An event (whether internal or external) is a happening of consequence to an entity. An entity means an economic unit that performs economic activities.

For example: Sachin started business with a capital of ₹ 500000. He purchases goods of ₹ 400000 for cash and sells ¾ goods for ₹ 380000. He also pays a rent of ₹ 20000.The following results can be drawn from the above:

1. Transaction are :
   - Investment of ₹ 500000
   - Purchasing of goods ₹ 400000
   - Cash Sales of ₹ 380000
   - Rent Paid ₹ 20000
2. Events are :
   - Profit of ₹ 60000 computed as under :

Particular	Amount
Sales	380000
Cost of Purchase (3/4 of ₹ 400000) 300000	
Add: Rent 20000	(320000)
Profit	60000

   - Closing Inventory of ₹ 100000 computed as under :

Particular	Amount
¼ of ₹ 400000	100000

- Cash Balance of ₹ 460000 computed as under :

Particular	Amount
Capital Invested	500000
Add : Cash Sales	380000
Less : Cash Purchase 400000	
Rent Paid 20000	(420000)
	460000

- Capital of ₹ 560000 computed as under :

Particular	Amount
Initial Capital Invested	500000
Add : Profit	60000
	560000

Objective of Accounting

The objectives of accounting may differ from business to business depending upon their specific requirements. However, the following are the general objectives of accounting.

(i) **To keep systematic record:** It is very difficult to remember all the business transactions that take place. Accounting serves this purpose of record keeping by promptly recording all the business transactions in the books of account.

(ii) **To ascertain the results of the operation**: Accounting helps in ascertaining results i.e., profit earned or loss suffered in business during a particular period. For this purpose, a business entity prepares either a Trading and Profit and Loss account or an Income and Expenditure account which shows the profit or loss of the business by matching the items of revenue and expenditure of the same period.

(iii) **To ascertain the financial position of the business:** In addition to profit, a businessman must know his financial position i.e., availability of cash, position of assets and liabilities etc. This helps the businessman to know his financial strength. Financial statements are barometers of health of a business entity.

(iv) **To portray the liquidity position:** Financial reporting should provide information about how an enterprise obtains and spends cash, about its borrowing and repayment of borrowing, about its capital transactions, cash dividends and other distributions of resources by the enterprise to owners and about other factors that may affect an enterprise's liquidity and solvency.

(v) **To protect business properties**: Accounting provides up to date information about the various assets that the firm possesses and the liabilities the firm owes, so that nobody can claim a payment which is not due to him.

Functions of Accounting

In order to accomplish its main objective of communicating information to the users, accounting embraces the following functions.

1. **Identifying:** Identifying the business transactions from the source documents.
2. **Recording**: The next function of accounting is to keep a systematic record of all business transactions, which are identified in an orderly manner, soon after their occurrence in the journal or subsidiary books.
3. **Classifying**: This is concerned with the classification of the recorded business transactions so as to group the transactions of similar type at one place. i.e., in ledger accounts. In order to verify the arithmetical accuracy of the accounts, trial balance is prepared.
4. **Summarising**: The classified information available from the trial balance is used to prepare profit and loss account and balance sheet in a manner useful to the users of accounting information.
5. **Analysing**: It establishes the relationship between the items of the profit and loss account and the balance sheet. The purpose of analysing is to identify the financial strength and weakness of the business. It provides the basis for interpretation.
6. **Interpreting**: It is concerned with explaining the meaning and significance of the relationship so established by the analysis. Interpretation should be useful to the users, so as to enable them to take correct decisions.
7. **Communicating:** The results obtained from the summarised, analysed and interpreted information are communicated to the interested parties.

Importance of Accounting: The "users" of accounting information

We have been talking about accounting and its purpose of providing information to users for decision-making. But, who exactly are these "users of financial statements"? Also, what information do they need and what decisions do they make?

The following are the different users of accounting information and their specific information needs:

1. Owners and Investors

Stockholders of corporations need financial information to help them make decisions on what to do with their investments (shares of stock), i.e. hold, sell, or buy more. Prospective investors need information to assess the company's potential for success and profitability. In the same way, small business owners need financial information to determine if the business is profitable and whether to continue, improve or drop it.

2. Management

In small businesses, management may include the owners. In huge organizations, however, management is usually made up of hired professionals who are entrusted with the responsibility of operating the business or a part of the business. They act as agents of the owners. The managers, whether owners or hired, regularly face economic decisions –

How much supplies will we purchase?

Do we have enough cash?

How much did we make last year?

Did we meet our targets?

All those, and many other decisions, require analysis of accounting information.

3. Lenders

Lenders of funds such as banks and other financial institutions are interested in the company's ability to pay liabilities upon maturity (solvency).

4. Trade creditors or suppliers

Like lenders, trade creditors or suppliers are interested in the company's ability to pay obligations when they become due. They are nonetheless especially interested in the company's liquidity -- its ability to pay short-term obligations.

5. Government

Governing bodies of the state, especially the tax authorities, are interested in an entity's financial information for taxation and regulatory purposes. Taxes are computed based on the results of operations and other tax bases. In general, the state would like to know how much the taxpayer is making to determine the tax due thereon.

6. Employees

Employees are interested in the company's profitability and stability. They are after the ability of the company to pay salaries and provide employee benefits. They may also be interested in its financial position and performance to assess the possibility of company expansion and career opportunities.

7. Customers

When there is a long-term involvement or contract between the company and its customers, the customers may be interested in the company's ability to continue its existence and its stability of operations. This need is also heightened in cases where the customers depend upon the entity. For example, a distributor (reseller), the customer in this case, is dependent upon the manufacturing company from which it purchases the items it resells.

8. General Public

Anyone outside the company such as researchers, students, analysts and others are interested in the financial statements of a company for some valid reason.

9. Research Scholars

Accounting information, being a mirror of the financial performance of a business organization, is of immense value to the research scholar who wants to make a study into the financial operations of a particular firm. To make a study into the financial operations of a particular firm, the research scholar needs detailed accounting information relating to purchases, sales, expenses, cost of materials used, current assets, current liabilities, fixed assets, long-term liabilities and share-holders funds which is available in the accounting records maintained by the firm.

Internal and External Users

The users may be classified into internal and external users.

Internal users refer to managers who use accounting information in making decisions related to the company's operations.

External users, on the other hand, are not involved in the operations of the company but hold some financial interest. The external users may be classified further into users withdirect financial interest – owners, investors, creditors; and users with indirect financial interest – government, employees, customers and the others.

Advantages of Accounting

The following are the advantages of accounting to a business:

1. It helps in having complete record of business transactions.
2. It gives information about the profit or loss made by the business at the end of a financial year and its financial conditions. The basic function of accounting is to supply meaningful information about the financial activities of the business to the owners and the managers.
3. It provides useful information for taking economic decisions.
4. It facilitates comparative study of current year's profit, sales, expenses etc., with those of the previous years.
5. It supplies information useful in judging the management's ability to utilise enterprise resources effectively in achieving primary enterprise goals.
6. It provides users with factual and interpretive information about transactions and other events which are useful for predicting, comparing and evaluation the enterprise's earning power.
7. It helps in complying with certain legal formalities like filing of income- tax and sales-tax returns etc.. If the accounts are properly maintained, the assessment of taxes is greatly facilitated.

Limitations of Accounting

1. Accounting is historical in nature. It does not reflect the current financial position or worth of a business.
2. Transactions of non-monetary nature do not find place in accounting. Accounting is limited to monetary transactions only. It excludes qualitative elements like management, reputation, employee morale, labour strike etc.
3. Facts recorded in financial statements are greatly influenced by accounting conventions and personal judgements of the Accountant or Management. Valuation of inventory, provision for doubtful debts and assumption about useful life of an asset may, therefore, differ from one business house to another.
4. Accounting principles are not static or unchanging-alternative accounting procedures are often equally acceptable. Therefore, accounting statements do not always present comparable data.
5. Cost concept is found in accounting. Price changes are not considered. Money value is bound to change often from time to time. This is a strong limitation of accounting.

Distinction between Book-keeping and Accounting

In general the following are the differences between book-keeping and accounting.

S. No.	Basis of Distinction	Book-keeping	Accounting
1	Scope	Recording and maintenance of books of accounts.	It is not only recording and maintenance of books of accounts but also includes analysis, interpreting and communicating the information.
2	Stage	Primary stage.	Secondary stage.
3	Objective	To maintain systematic records of business transactions.	To ascertain the net result of the business operation.
4	Nature	Often routine and clerical in nature.	Analytical and executive in nature.
5	Responsibility	A book-keeper is responsible for recording business transactions.	An accountant is also responsible for the work of a book-keeper.
6	Supervision	The book-keeper does not supervise and check the work of an Accountant.	An accountant supervises and checks the work of the book-keeper.
7	Staff involved	Work is done by the junior staff of the organisation.	Senior staff performs the accounting work.

Relationship between Accountancy, Accounting and Book-keeping

Book-keeping provides the basis for accounting and it is complementary to accounting process. Accounting begins where book-keeping ends. Accountancy includes accounting and book-keeping. The terms Accounting and Accountancy are used synonymously.

USERS OF ACCOUNTING INFORMATION

Chapter 2

Financial Statements – Classification & Terminology

Terminology Used in Accounting System

Account – A formal record of a particular type of transaction expressed in money or other unit of measurement and kept in a recorded form. In accounting separate record of each individual, asset, liability, expenses or income is kept. The place where such a record is maintained is termed as 'Account'. Such as the Account of Ranbir, the Account of Ram, the Account of Machinery, the Account of Salary, the Account of Rent and likewise. All transactions entered into with Ranbir will be recorded in the Account of Ranbir.

All accounts are divided into two sides.

The left side of an account is arbitrarily or traditionally called Debit side and the right side of an account is called Credit side.

In the abbreviated form, Debit is written as Dr. and Credit is written as Cr.

Accounting Entry – A record of financial transaction in the books of account like journal, ledger, cash book, etc.

Account Payable – Amount owed by an enterprise on account of goods purchased or services received or in respect of contractual obligations. Also termed as Creditor.

Accounting Period – The period of time for which financial statements are customarily prepared.

Accounting Principle – The principles and procedures under which the accounts of an organization are maintained/ to be maintained are called accounting principles. An accounting principle is an adaptation or special application of a principle necessary to meet the peculiarities of an organization or the needs of its management. Thus, principles are required for the computation of depreciation, the recognition of capital expenditures etc.

Account Receivable – Persons from whom amounts are due for goods sold or services rendered or in respect of contractual obligations. Also termed as debtor. The words 'Receivables' and 'Debtors' are used interchangeably.

Accounting Unit – An accounting unit shall be defined as a department, branch, office identified by the enterprise/as a unit for maintenance of separate accounting records.

Accounting Year – Accounting year means a year commencing on the first day of the accounting period. Generally, in case of a business enterprise /educational body, it would refer to the period from 1st April of a year to 31st March next year.

Accrual – Recognition of revenues and costs as they are earned or incurred (and not as money is received or paid). It includes recognition of transactions relating to assets and liabilities as they occur irrespective of the actual receipts or payments.

Accrual Basis of Accounting – The basis of accounting under which transactions and other events are recognized when they occur (and not only when cash or its equivalent is received or paid). Therefore, the transactions and events are recorded in the accounting records and recognized in the financial statements of the periods to which they relate. The elements recognized under accrual accounting are assets, liabilities, revenue and expenses.

Accrued & Due – In respect to an asset (or a liability) it means a claim which has become enforceable, which arises from the sale/ rendering (purchase) of goods/ services or otherwise and has become receivable (payable). In respect to an income (or an expense) it means the amount earned (incurred) in an accounting period, for which a claim has become enforceable, and it arises from the sale/rendering (purchase) of goods/services or otherwise and has become receivable (payable).

Accrued But Not Due – In respect to an asset (or a liability) it means a claim which has not yet become enforceable, which accumulates with the passage of time or arises from the sale/ rendering (purchase) of goods/ services which, on the date of period-end, have been partly performed and are not yet receivable (payable). In respect to an income (or an expense) it means the amount earned (incurred) in an accounting period, but for which no enforceable claim has become due in that period. It accumulates with the passage of time or arises from the sale/ rendering (purchase) of goods/services goods which, at the date of accounting, have been partly performed and are not yet receivable (payable).

Accumulated Depreciation – The total to date of the periodic depreciation charges on depreciable assets.

Advance – Payment made on account of, but before completion of, a contract, or before acquisition of goods or receipt of services.

Amortisation – The gradual and systematic writing off of an asset or an account over an appropriate period. The amount on which amortisation is provided is referred to as amortisable amount. Depreciation accounting is a form of amortisation applied to depreciable assets. Depletion accounting is another form of amortisation applied to wasting assets. Amortisation also refers to gradual extinction or provision for extinction of a debt by gradual redemption or sinking fund payments or the gradual writing off to revenue of miscellaneous expenditure carried forward.

Annual Report – Any report prepared at yearly intervals. A statement of the financial condition and operating results of a business enterprise/institute, prepared yearly for submission to interested parties; summarising its operations for the preceding year and including a balance sheet, income & expenditure statement, often a receipts & payment statement, and the auditor's report, together with comments by the Manager/ Officer of the business enterprise / institute on the year's operations.

Assets – "Any thing which is in the possession or is the property of business enterprises including the amount due to it from others, is called an Asset." Assets are tangible objects or intangible rights owned by an business enterprise/ and carrying probable future benefits. Assets provide the means to achieve their objectives. Assets that are used to deliver goods and services in accordance with an organisation's objectives but which do not directly generate net cash inflows are often described as embodying "service potential". Assets that are used to generate net cash inflows are often described as embodying "future economic benefits".

Bad Debts – Debts owed to the business enterprises, which are considered to be irrecoverable, e.g., arrears of taxes, fees and other revenue left uncollected and considered to be irrecoverable. It is a business loss debited to Profit and Loss A/c as expense.

Balancing- It means writing of the difference that exists between the amount columns of the two sides, namely debit and credit in the smaller side so that the totals of the two sides are equalized.

Balance Sheet – A statement of the financial position of an business enterprise/ as at a given date, which exhibits its assets, liabilities, capital, reserve and other account balances at their respective book values.

Bank Reconciliation Statement – A statement, which reflects the nature and amount of transaction (s) not responded either by the business enterprise or the bank as on a particular date. Such statement may also reflect errors/ omission in the recording of transaction inter-se between the business enterprise and the Bank.

Books of Original Entry – A record book, recognised by law in which transactions are successively recorded, and which is the source of postings to ledgers; a journal. Books of original entry include general and special journals, such as cash books.

Budget – Budget is a financial plan, an expression of financial intent. It sets forth the expenditures that bodies are expected to incur during the year on various programmes and the means of financing them. A budget thus provides both, the authorization of, and limitations on, the amounts that may be spent for particular purposes.

Capitalisation – An expenditure for a fixed asset or addition thereto that has the effect of enlarging physical dimensions, increasing productivity, lengthening future life, or lowering future costs.

Capital Expenditure – An expenditure which is incurred in acquiring or increasing the value of Fixed Assets and this expenditure yields (give) benefits for more than one year. The term is generally restricted to expenditure that adds fixed asset units or that has the effect of improving the capacity, efficiency, life span or economy of operations of an existing asset. It is written in Balance Sheet on Assets Side.

Cash Book – A book of original entry maintained on daily basis for cash receipts and disbursement in its chronological order.

Chart of Accounts – A systematically arranged list of accounts applicable to a specific concern, giving account names and numbers, if any.

Contingent Liability – An obligation relating to an existing condition or situation which may arise in future depending on the occurrence or non-occurrence of one or more uncertain future events. No accounting entry needs to be passed for a contingent liability. However, disclosure is required in the Balance Sheet.

Contra Entry – An item on one side of an account which offsets fully or in part one or more items on the opposite side of the same account.

Cost – The amount of expenditure incurred on or attributable to a specified article, product or activity.

Cost of Acquisition – The cost of acquisition of a Fixed Asset comprises its purchase price and includes import duties and other non-refundable taxes or levies and any directly attributable cost of bringing the asset to its working condition for its intended use; any trade discounts and rebates are deducted in arriving at the purchase price.

Credit – A book-keeping entry recording the reduction or elimination of an asset or an expense, or the creation of or addition to a liability or item of net worth or revenue; the amount so recorded.

Current Assets – Cash and other assets that are expected to be converted into cash or consumed in rendering of services in the normal course of operations of the business enterprise/institution.

Current Liability – Liability including loans, deposits, expenses and bank overdrafts which fall due for payment in a relatively short period, normally not more than twelve months.

Debit – The goods or benefit received from a transaction; a book-keeping entry recording the creation of or addition to an asset or an expense, or the reduction or elimination of a liability, or item of net worth or revenue; the amount so recorded.

Deficit – The excess of expenditure over income for an Accounting Period under consideration.

Depreciable Amount – The historical cost or other amount substituted for historical cost of a depreciable asset in the financial statements, less the estimated residual value.

Depreciation – A measure of the wearing out, consumption or other loss of value of a depreciable asset arising from use, efflux ion of time or obsolescence through technology and market changes. It is allocated so as to charge a fair proportion in each accounting period during the useful life of the asset. It includes amortisation of assets whose useful life is predetermined and depletion of wasting assets.

Depreciation Method – The arithmetic procedure followed in determining a provision for depreciation (an expense) and maintaining the accumulated balance.

Depreciation Rate – A percentage which when applied to the depreciable amount will yield depreciation expense for a year.

Disclosure – Process of divulging accounting information so that the content of Financial Statements is understood.

Discount – It is a rebate and allowance given by the seller to buyer.

Double-Entry Bookkeeping – It is a system of accounting in which both debit and credit aspects of each transaction is recorded. It affects at least two accounts.

You've probably heard the saying, "Money doesn't grow on trees." It means that money must come from somewhere---it doesn't just "appear." Double-entry accounting is a method of record-keeping that lets you track just where your money comes from and where it goes. Using double-entry means that money is neither gained nor lost---it is always transferred from somewhere (a source account) to somewhere else (a destination account). This transfer is known as a transaction, and each transaction requires at least two accounts.

Earmarked Funds – Funds representing Special Funds to be utilised for specific purposes.

Expenses – A cost relating to the operations of an accounting period or to the revenue earned during the period or the benefits of which do not extend beyond that period.

Fair Market Value – Price at which property would change hands between a buyer and a seller without any compulsion to buy or sell, and both having reasonable knowledge of the relevant facts.

Financial Statement – A balance sheet, income statement (income and expenditure), receipts & payment statement or any other supporting statement or other presentation of financial data derived from accounting records.

Fixed Asset – Asset held for the purpose of providing services and that is not held for resale in the normal course of operations of the business enterprise.

Fixed Deposit – Deposit for a specified period and at specified rate of interest.

Fund – The term fund refers to the amount set aside for a general or specific purpose, whether represented by specifically earmarked assets or not.

Grants – Grants are assistance by State Government and/ or Central Government in cash or kind to an organisation for past or future compliance with certain conditions.

Gross Block – The total cost of acquisition/ purchase of all the Fixed Assets of the business enterprise.

Income – Money or money equivalent earned or accrued during an accounting period, increasing the total of previously existing net assets, and arising from provision of any type of services and rentals.

Income and Expenditure Statement – A financial statement, prepared by institutions in double entry accounting system on accrual basis to present their revenues and expenses for an accounting period and to show the excess of revenues over expenses (or vice-versa) for that period. It is similar to Profit and Loss Statement and is also called revenue and expense statement.

Interest – The service charge for the use of money or capital, paid at agreed intervals by the user, and commonly expressed as an annual percentage of outstanding principal.

Internal Control – The plan of organization and all the methods and procedures adopted by the management of a Body to assist in achieving management's objective of ensuring, as far as practicable, the orderly and efficient conduct of its business, including adherence to management policies, the safeguarding of assets, prevention and detection of fraud and error, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information.

Investments – Assets held not for operational purposes or for rendering services, i.e., assets other than fixed assets or current assets (e.g. securities, shares, debentures, immovable properties).

Inventory – The values of those goods which are lying unsold at the end of accounting year. It also known as 'Stock.'

Inter unit transactions – Transactions between one and more accounting units of the business enterprise.

Infrastructure Assets – Those assets with the characteristics of being, a part of a system or network, specialised in nature and do not have alternative uses, immovable, and subject to constraints on disposal.

Journal Book – The book of original entry in which the 'dual aspect' of transactions other than those involving cash and/ or bank, along with explanations, is recorded in their chronological order , from which a posting is done in the relevant ledger.

Journal Entry – Recording of transaction other than those involving cash and/ or bank by dividing into its debit and credit aspects.

Ledger – A compilation of all accounts used for accounting purposes.

Performa of Ledger

LEDGER

Group – Head | Ledger Account

Date	Particulars	C.B. Folio	Debit		Credit		Dr. or Cr.	Balance	
			₹	P.	₹	P.		₹	P.

Lease – A lease is an agreement whereby the less or conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period. A lease agreement also includes a Hire Purchase agreement. A lease is classified as a finance lease if it transfers substantially the entire risks and rewards incident to ownership. All other leases are classified as operating leases.

Liability – An amount owing by one person to another, payable in money, or in goods or services: the consequence of an asset or service received or a loss incurred or accrued; particularly, any debt (a) due or past due (current liability), (b) due at a specified time in the future (e.g. funded debt, accrued liability), or (c) due only on failure to perform a future act (contingent liability).

Long term investments – Any investment falling outside the ambit of current investments are treated as long-term investments.

Mortgage – A lien on land, buildings, machinery, equipment, and other property, fixed or movable, given by a borrower to the lender as security for his loan; sometimes called a deed of trust.

Narration – A brief description written below an Accounting Entry. It explains as to why the entry has been recorded and other related aspects of the entry.

Net Assets – The excess of the book value of the assets of a Body over its external liabilities.

Net Block – Gross Block less Accumulated Depreciation of all the Fixed Assets of the business enterprise.

Period End – The last day of any Accounting Period, e.g., quarter, half-year or year-end.

Prepaid Expense – Payment for expense in an accounting period, the benefit for which will accrue in the subsequent accounting period(s).

Purchase – The goods which are purchased in which business deals or for resale purpose are known as 'Purchase.'

Purchase Return – When purchase goods are returned to suppliers these are known as 'Purchase Return' or ' Return Outward.'

Ratio Analysis – Analysis of relationship worked out among various accounting data which are mutually interdependent and which influence each other in a significant manner, arises from the fact that often absolute figures standing alone convey no meaning. They become significant only when considered with other figures. It also helps in comparing the actual or projected data for a particular business enterprise to the data of that business enterprise or any other business enterprises in order to analyse trends or relationship.

Receipt – A written acknowledgement of something acquired; hence, an accounting document recording the physical receipt of cash/ cheques.

Receipts & Payments Statement – A financial statement prepared for an accounting period to depict the changes in the financial position and to present the cash received in and paid out in whatever form (cash, cheques, etc.) under certain headings. All non-cash related transactions are ignored while preparing this Statement.

Reconciliation – It means identifying the difference between two items (i.e. amounts, balances, accounts or statements) so that the figures agree.

Revenue Expenditure – It means outlay benefiting only the current year. It is treated as an expense to be matched against revenue.

Sale – It means transfer of ownership of goods and services to customer. The term 'sales' is used only for the sales of those goods which are purchased for resale purpose. It includes both cash sales and credit sales.

Sales Return – When sold goods are received back from customers then it is known as 'Sales Return' or 'return outward.'

Special Fund – An amount set aside for a specific purpose represented by specifically earmarked assets.

Straight Line Method (SLM) – The method under which the periodic charge for depreciation is computed by dividing the depreciable amount of a depreciable asset by the estimated number of years of its useful life. It also known as Fixed Installment Method or Original Cost Method.

Surplus – The excess of income over expenditure of the business enterprise for an Accounting Period under consideration.

Trial Balance – A list or abstract of the balances or of total debits and total credits of the accounts in a ledger, the purpose being to determine the equality of posted debits and credits and to establish a basic summary for financial statements. Its main objective is to check the Arithmetical Accuracy of the business transactions.

Useful Life – The period over which a depreciable asset is expected to be used by the enterprise; or (ii) the number of production or similar units expected to be obtained from the use of the asset by the enterprise.

Voucher – A document which serves as an authorisation for any financial transaction and forms the basis for recording the accounting entry for the transaction in the books of original entry, e.g., Cash Receipt Voucher, Bank Receipt Voucher, Journal Voucher, Payment Voucher, etc.

Written Down Value (WDV) – Written Down Value in respect of an asset, means its cost of acquisition or substituted value less accumulated depreciation.

Written Down Value (WDV) **Method** – A method under which the periodic charge for depreciation of an asset is computed by applying a fixed percentage to its historical cost or substituted amount less accumulated depreciation (net book value). This is also referred to as “Diminishing Balance Method”.

Chapter 3
Fundamentals and Principles of Accounting

Accounting is the language of business. It records business transactions taking place during the accounting period. Accounting communicates the result of the business transactions in the form of final accounts. With a view to make the accounting results understood in the same sense by all interested parties, certain accounting assumptions, concepts and principles have been developed over a course of period.

Accounting principles may be defined as those rules of action or conduct which are adopted by the accountants internationally while recording accounting transactions.

"Accounting principles are a body of doctrine commonly associated with the theories and procedure of accounting, serving as an explanation of current practices and a guide for selection of convention or procedure where alternatives exist."

Accounting Concepts

Accounting Concepts are the necessary assumptions, conditions or postulates upon which the accounting is based. They are developed to facilitate communication of the accounting and financial information to all the readers of the Financial Statements, so that all readers interpret the statements in the same meaning and context.

(a) Entity Concept

For accounting purposes, an "organisation" is treated as a separate entity from the "owners" or "stakeholders". This concept helps in keeping private affairs of the owners and stakeholders separate from the business affairs. For example, an educational institutions is a separate, independent and autonomous entity and is governed by a separate legislation and the regulations formed by it. The various stakeholders of the educational institutions, including citizens, state government, environmentalists, etc., do not own the educational institutions. Thus, a separate balance sheet and income & Expenditure Statement are prepared in respect of the operations of the educational institutions. This concept is applicable to all forms of organisations.

(b) Dual Aspect or Accounting Equivalence Concept

This concept follows from the Entity Concept. All entities own certain assets. Such assets are acquired through contributions of those who have provided the funds for the purpose. Funds are made available either through the surpluses of the entity or loans or payables. In a sense, such providers of funds are claimants to the assets. At any point of time, the assets will be equal to the claims. Since the claims on the assets could be those of "outsiders" (i.e. liabilities) or "owners" (i.e. capital, reserves, etc.), it results in the accounting equation:

$$\text{Assets} = \text{Own Funds} + \text{Liabilities}$$

(c) Going Concern Concept

It is assumed that the organisation will continue for a long time, unless and until it has entered into a state of liquidation. It is as per this concept, that the accountant does not take into consideration the market value of the assets while valuing them, irrespective of whether the market value is higher or lower than the book value. Similarly, depreciation on fixed assets is provided on the basis of expected lives of the assets rather than on their market values. Also, the financial statements are prepared at defined period-end to measure the performance of the entity during that period and not only on the closure or liquidation of the entity.

(d) Money Measurement Concept

In accounting, every transaction is recorded in terms of money. Events or transactions that cannot be expressed in terms of money are not recorded in the books of accounts. Receipt of income, payment of expenses, purchase and sale of assets, etc., are monetary transactions that are recorded in the books of accounts. For example, the event of a machinery breakdown is not recorded as it does not have a monetary value. However, the expenditure incurred for the repair of the machinery can be measured in monetary value and hence is recorded.

(e) Cost Concept

As per this concept, an asset is ordinarily recorded at the price paid to acquire it, i.e., at its cost and this cost is the basis for all subsequent accounting for the asset. The cost concept does not mean that the asset will always be shown at cost. This basically signifies that each time the financial statements are prepared; the fixed assets need not be revised and recorded at its realisable or replacement or market value. The assets recorded at cost at the time of purchase may systematically be reduced through depreciation.

(f) Accounting Period Concept

An accounting period is the interval of time at the end of which the financial statements are prepared to ascertain the financial performance of the organisation. Although the “going concern” concept stresses the continuing nature of the entity, it is necessary for an organisation to review how it is performing. The preparation of financial statements at periodic intervals helps in taking timely corrective actions and developing appropriate strategies. The accounting period is normally considered to be of twelve months.

(g) Accrual Concept

Under the cash system of accounting, the revenues and expenses are recorded only if they are actually received or paid in cash, irrespective of the accounting period to which they belong. But under the accrual concept, occurrence of claims and obligations in respect of incomes or expenditures, assets or liabilities based on happening of any event, passage of time, rendering of services, fulfilment (partially or fully) of contracts, diminution in values, etc., are recorded even though actual receipts or payments of money may not have taken place. In respect of an accounting period, the outstanding expenses and the prepaid expenses and similarly the income receivable and the income received in advance are shown separately in the books of accounts under the accrual method.

(h) Periodic Matching of Cost and Revenue Concept

To ascertain the surplus or deficit made by the entity during an accounting period, it is necessary that the costs incurred are matched with the revenue earned by the entity during that accounting period. The matching concept is a corollary drawn from the accrual concept. To ascertain the correct surplus or deficit, it is necessary to make adjustments for all outstanding expenses, prepaid expenses, income receivable and income received in advance to correctly depict and match the income and expenditure relating to that accounting period.

(i) Realization Concept

According to this concept, revenue should be accounted for only when it is actually realised or it has become certain that the revenue will be realised. This signifies that revenue should be recognised only when the services are rendered or the sale is affected. However, in order to recognise revenue, actual receipt of cash is not necessary. What is important is that the organisation should be legally entitled to receive the amount for the services rendered or the sale affected.

Accounting Conventions

The term "accounting conventions" refer to the customs or traditions, which are used as a guide in the preparation of meaningful financial records in the form of the income statement (Profit and Loss Account) and the position statement (Balance Sheet).

(a) Convention of Disclosure

The term “disclosure” implies that there must be a sufficient revelation of information which is of material interest to owners, creditors, lenders, investors, citizens and other stakeholders. The accounts and the financial statements of an entity should disclose full and fair information to the beneficiaries in order to enable them to form a correct opinion on the performance of such entity, which in turn would allow them to take correct decisions. For example, the Accounting Principles that have been followed for preparation of the Financial Statements should be disclosed along with the Financial Statements for proper understanding and interpretation of the same.

(b) Convention of Materiality

An item should be regarded as material, if there is a sufficient reason to believe that knowledge of it would influence the decision of informed creditors, lenders, investors, citizens and other stakeholders. The accounts and the financial statements should impart importance to all material information so that true and fair view of the state of affairs of the entity is given to its beneficiaries. Hence, keeping the convention of materiality in view, unimportant items are not disclosed separately and are merged with other items. For example, the expenditure incurred on repairs and maintenance of a certain asset, which are small, may not be disclosed separately in respect of each such small item but may be grouped together and shown as a single item of expenditure.

(c) Convention of Consistency

The convention of consistency facilitates comparison of financial performance of an entity from one accounting period to another. This means that the accounting principles followed by an entity should be consistently applied by it over the years. For example, an organisation should not change its method of depreciation every year, i.e., from Straight Line Method to Written Down Value Method or vice-versa. Similarly, the method adopted for valuation of stocks, viz., First in First Out (FIFO) or Weighted Average should be consistently followed. In case a change is made, it should be disclosed.

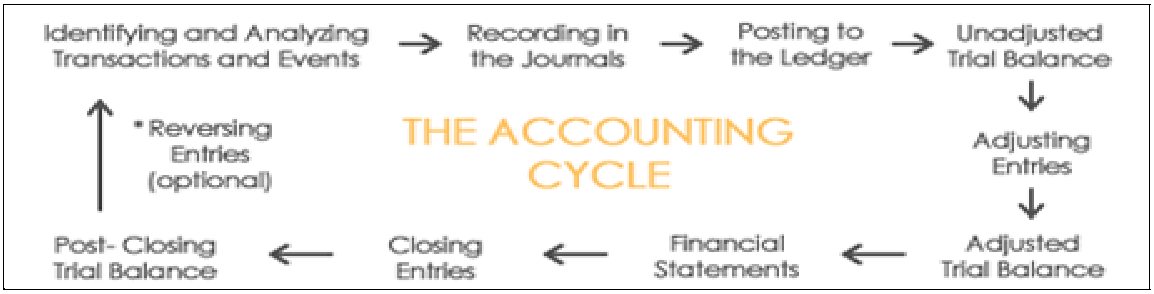
(d) Convention of Conservatism

As per this convention, the anticipated profits should be ignored but all anticipated losses should be provided for in the books of accounts of an entity. This means that all prospective losses are taken into consideration, however, no doubtful income is taken into consideration in recording of transactions by an entity. For example, while provision for doubtful debts and discount is made on debtors or Accounts Receivables, no provision is made for likely discount receivable from creditors or Accounts Payables. Similarly, provision is made for diminution in value of investments; however, no provision is made for any appreciation in value of investments.

The Accounting Cycle: 9-Step Accounting Process

The accounting cycle, also commonly referred to as accounting process, is a series of procedures in the collection, processing, and communication of financial information.

As defined earlier, accounting involves recording, classifying, summarizing, and interpreting financial information. Financial information is presented in reports called financial statements. But before they can be prepared, accountants need to gather information about business transactions, record and collate them to come up with the values to be presented in these reports. The cycle does not end with the presentation of financial statements. Several steps are needed to be done to prepare the accounting system for the next cycle.



Though a detailed study of each of these accounting steps is incorporated later in this material, yet a brief overview about each of them is as under:

Accounting cycle steps:

1. Identifying and Analyzing Business Transactions

The accounting process starts with identifying and analyzing business transactions and events. Not all transactions and events are entered into the accounting system. Only those that pertain to the business entity are included in the process. For example, a loan made by the owner in his name that does not have anything to do with the entity is not accounted for. The transactions identified are then analyzed to determine the accounts affected and the amounts to be recorded. The first step includes the preparation of business documents, or source documents. A business document serves as basis for recording a transaction.

2. Recording in the Journals

A journal is a book – paper or electronic – in which transactions are recorded. Business transactions are recorded using the double-entry bookkeeping system. They are recorded in journal entries containing at least two accounts (one debited and one credited). To simplify the recording process, special journals are often used for transactions that recur frequently such as sales, purchases, cash receipts, and cash disbursements. A general journal is used to record those that cannot be entered in the special books. Transactions are recorded in chronological order and as they occur. Hence, journals are also known as Books of Original Entry.

3. Posting to the Ledger

Also known as Books of Final Entry, a ledger is a collection of accounts that shows the changes made to each account as a result of past transactions, and their current balances. This is the core of the classifying phase. After the posting process, the balances of each account can now be determined. For example, all journal entries made to Cash would be transferred into the Cash account in the ledger. Increases and decreases in cash will be entered into one ledger account. Thus, the ending balance of Cash can be determined.

4. Unadjusted Trial Balance

A trial balance is prepared to test the equality of the debits and credits. All account balances are extracted from the ledger and arranged in one report. Afterwards, all debit balances are added. All credit balances are also added. Total debits should be equal to total credits. When errors are discovered, correcting entries are made to rectify them or reverse their effect. Take note however that the purpose of a trial balance is only test the equality of total debits and total credits and not to determine the correctness of accounting records. Some errors could exist even if debits are equal to credits, such as double posting or failure to record a transaction.

5. Adjusting Entries

Adjusting entries are prepared as an application of the accrual basis of accounting. At the end of the accounting period, some expenses may have been incurred but not yet recorded in the journals. Some income may have been earned but not entered in the books. Adjusting entries are prepared to have the accounts updated before they are summarized into the financial statements. Adjusting entries are made for accrual of income, accrual of expenses, deferrals (income method or liability method), prepayments (asset method or expense method), depreciation, and allowances.

6. Adjusted Trial Balance

An adjusted trial balance may be prepared after adjusting entries are made and before the financial statements are prepared. This is to test if the debits are equal to credits after adjusting entries are made.

7. Financial Statements

When the accounts are already up-to-date and equality between the debits and credits have been tested, the financial statements can now be prepared. The financial statements are the end-products of an accounting system. A complete set of financial statements is made up of:

(1) Statement of Comprehensive Income (Income Statement and Other Comprehensive Income),

(2) Statement of Changes in Equity,

(3) Statement of Financial Position or Balance Sheet,

(4) Statement of Cash Flows, and

(5) Notes to Financial Statements.

8. Closing Entries

Temporary or nominal accounts, i.e. income statement accounts, are closed to prepare the system for the next accounting period. Temporary accounts include income, expense, and withdrawal accounts. These items are measured periodically. The accounts are closed to a summary account (often, Income Summary) and then closed further to the appropriate capital account. Take note that closing entries are made only for temporary accounts. Real or permanent accounts, i.e. balance sheet accounts, are not closed.

9. Post-Closing Trial Balance

In the accounting cycle, the last step is to prepare a post-closing trial balance. It is prepared to test the equality of debits and credits after closing entries are made. Since temporary accounts are already closed at this point, the post-closing trial balance contains real accounts only.

*Reversing Entries: Optional step at the beginning of the new accounting period

Reversing entries are optional. They are prepared at the beginning of the new accounting period to facilitate a smoother and more consistent recording process.

In this step, the adjusting entries made for accrual of income, accrual of expenses, deferrals under the income method, and prepayments under the expense method are reversed.

Chapter 4
Basic Accounting Procedures – I
Double Entry System of Book Keeping

Recording of business transactions has been in vogue in all countries of the world. In India, maintenance of accounts was practised not in such a developed form as we have today. **Kautilya's** famous **Arthasastra** not only relates to Politics and Economics, but also explains the art of account keeping in a separate chapter. Written in 4th century BC, the book gives details about account keeping, methods of supervising and checking of accounts and also about the distinction between capital and revenue, income and expenses etc.

Double entry system was introduced to the business world by an Italian merchant named Lucas Pacioli in 1494 A.D. Though the system of recording business transactions in a systematic manner has **originated in Italy, it was perfected in England** and other European countries during the 18th century only i.e., after the Industrial Revolution. Many countries have adopted this system today.

Double Entry Accounting System

Double Entry Accounting System recognizes that every transaction has a dual effect. There are two sides of every transaction. If one account is debited, any other account must be credited. Every transaction affects at least two accounts in opposite directions. It may, however be noted, that the double entry does not mean that a transaction is recorded twice. But it means that at least two accounts are affected by a transaction one account receiving a benefit and other account yielding a benefit. It is because of dual aspect principle that the two sides of the Balance Sheet are always equal and the following accounting equation will always hold good at any point of time.

Assets = Liabilities + Capital (or Net Worth)

Or

Capital (or Net Worth) = Assets – Liabilities

Whenever a transaction is to be recorded, it has to be recorded in two or more accounts to balance the equation. If a transaction affects (increases or decreases) one side of equation, it will also affect (increase or decrease) the other side of equation or increase one account and decrease another account on the same side of equation. Equation remains balanced whenever a transaction takes place. E.g. Mr. A commences a business with ₹ 5 Lacs in cash and takes a loan of ₹ 1 Lacs from bank, and this ₹ 6 Lacs are used in buying some assets say plant & machinery,

The equation will be as follows:

Assets = Liabilities + Capital

₹ 6 Lakh = ₹ 1 Lakh + ₹ 5 Lakh

S. No.	Transaction	Accounts affected	
		Assets	Liabilities & Capital
1	Capital brought in	Cash increases	Capital increases
2	Purchase Goods for Cash	Cash decreases Stock increases	

3	Purchase Goods on Credit	Stock increases	Creditors increase
4	Purchase Furniture for Cash	Furniture increases Cash decreases	
5	Paid Rent	Cash decreases	Rent = Expenses Therefore Capital decreases
6	Received Interest	Cash Increases	Interest = Income Therefore Capital increases
7	Sold Goods on Credit for ₹ 40,000 costing ₹ 30,000	Debtors increase by ₹ 40,000 Stock decreases by ₹ 30,000	Capital increases by ₹ 40,000 – 30,000 = ₹ 10,000
8	Paid to Creditors	Cash decreases	Creditors decrease

Account

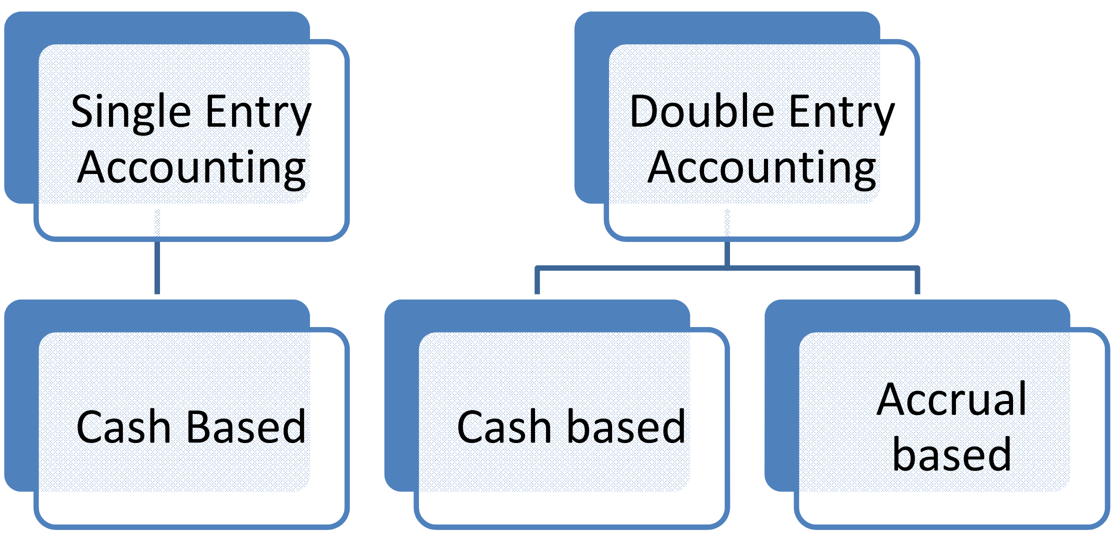
An account is a record of all business transactions relating to a particular person or item. In accounting, separate record of each individual, asset, liability, expenses or income is kept.

It is stated that 'an account is a summary of relevant transactions at one place relating to a particular head'.

All accounts are divided into two sides. The left side of an account is arbitrarily or traditionally called Debit side and the right side of an account is called the Credit side.

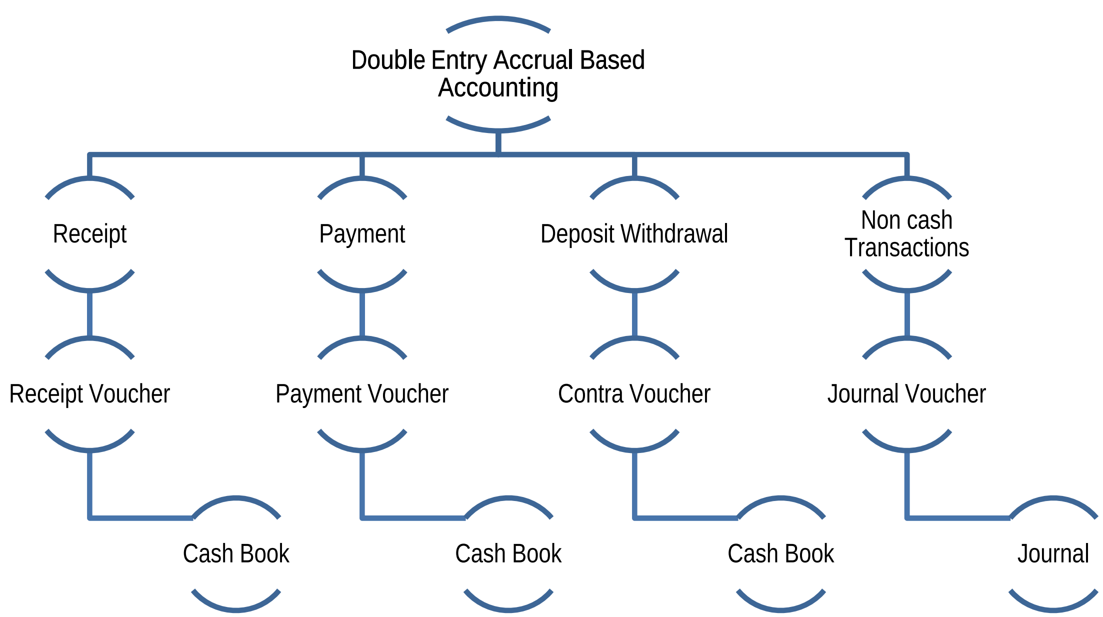
The terms originated from the Latin terms "debere" or "debitum" which means "what is due"; and "credere" or "creditum" which means "something entrusted or loaned". Every transaction has two aspects and each aspect has an account.

Different Accounting Systems and Basis of Accounting



Cash Based Double Entry Accounting System is rarely followed. Hence, we shall concentrate on understanding the basic difference between Cash Based Single Entry Accounting and Accrual Based Double Entry Accounting:

Basis of Distinction	Cash Based Single Entry Accounting	Accrual Based Double Entry Accounting
Nature of Transaction	All receipts and payments during the Accounting period are recorded whether or not the transactions actually belong to that accounting period.	All income and expenses relating to the Accounting period are recorded, whether or not received or paid actually.
Accounts	Only personal accounts and Cash Book are opened.	Personal, Real and Nominal accounts are opened.
Accuracy of results	Accuracy of transactions cannot be verified since all transactions are recorded on single entry basis and no trial balance is prepared.	All transactions are recorded based on double entry book keeping, a trial balance is prepared to check the arithmetical accuracy of the transactions.
Financial Performance	Only receipt and payment account is prepared, hence financial performance cannot be ascertained as Income and Expenditure Account is not prepared.	Financial performance of an entity can be ascertained by preparing the Income and Expenditure Statement.
Financial Position	Only a Statement of Affairs is prepared which does not give the true and fair statement of affairs.	A balance sheet is prepared on going concern basis which gives a true and fair state of affairs.
Authenticity	This system is not considered authentic by the Financial Institutions, lending agencies and other outside bodies.	This system of accounting is well accepted by Financial Institutions, lending agencies and all outside bodies.

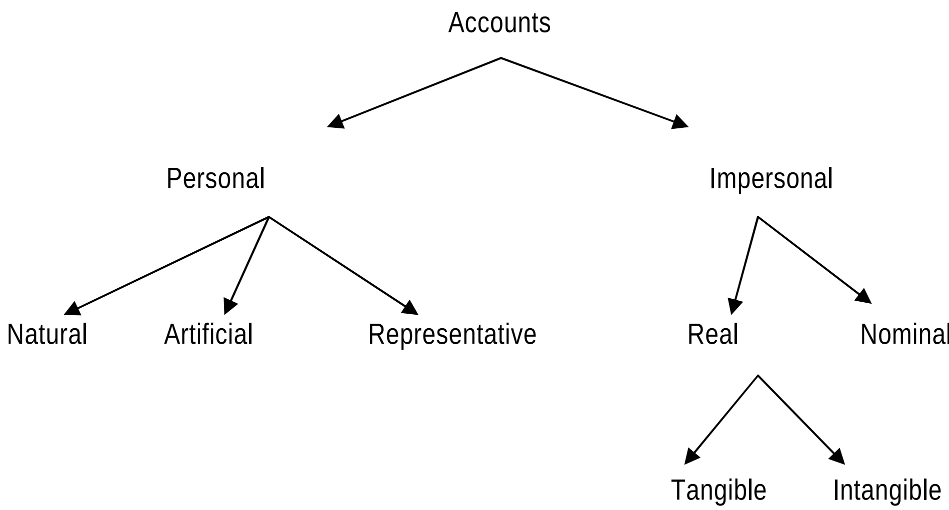


Classification of Accounts

Transactions can be divided into three categories.

- Transactions relating to individuals and firms
- Transactions relating to properties, goods or cash
- Transactions relating to expenses or losses and incomes or gains.

Therefore, accounts can also be classified into Personal, Real and Nominal. The classification may be illustrated as follows:



I. Personal Accounts: The accounts which relate to persons. Personal accounts include the following.

(i) Natural Persons: Accounts which relate to individuals. For example, Mohan's A/c, Shyam's A/c etc.

(ii) Artificial persons: Accounts which relate to a group of persons or firms or institutions. For example, HMT Ltd., Indian Overseas Bank, Life Insurance Corporation of India, Cosmopolitan club etc.

Representative Persons: Accounts which represent a particular person or group of persons. For example, outstanding salary account, prepaid insurance account, etc.

A business concern may keep business relations with all the above personal accounts, because of buying goods from them or selling goods to them or borrowing from them or lending to them. Thus they become either Debtors or Creditors.

The proprietor being an individual, his capital account and his drawings account are also personal accounts.

II. Impersonal Accounts: All those accounts which are not personal accounts. This is further divided into two types viz. Real and Nominal accounts.

(i) Real Accounts: Accounts relating to properties and assets which are owned by the business concern. Real accounts include tangible and intangible accounts. For example, Land, Building, Goodwill, Purchases, etc.

(ii) Nominal Accounts: These accounts do not have any existence, form or shape. They relate to incomes and expenses and gains and losses of a business concern. For example, Salary Account, Dividend Account, etc.

Illustration:

Classify the following items into Personal, Real and Nominal Accounts.

1.	Capital	2.	Sales
3.	Drawings	4.	Outstanding salary
5.	Cash	6.	Rent
7.	Interest paid	8.	Indian Bank
9.	Discount received	10.	Building
11.	Bank	12.	Chandrasekar
13.	Murugan Lending Library	14.	Advertisement
15.	Purchases		

Solution:

1.	Personal account	2.	Real account
3.	Personal account	4.	Personal (Representative) account
5.	Real account	6.	Nominal account
7.	Nominal account	8.	Personal (Legal Body) account
9.	Nominal account	10.	Real account
11.	Personal account	12.	Personal account
13.	Personal account	14.	Nominal account
15.	Real account		

Accounting Equation Based Classifications of Accounts

The source document is the origin of a transaction and it initiates the accounting process, whose starting point is the accounting equation.

Accounting equation is based on dual aspect concept (Debit and Credit). It emphasizes on the fact that every transaction has a two sided effect i.e., on the assets and claims on assets. Always the total claims (those of outsiders and of the proprietors) will be equal to the total assets of the business concern. The claims are also known as equities, and are of two types: i.) Owners equity (Capital); ii.) Outsiders' equity (Liabilities).

The classification of accounts, accounting to 'Accounting Equation' approach is given below:

Type of Account	Meaning	Example
Asset Account	These accounts relate to tangible and intangible real assets	Tangible: Land, Building, Machinery, etc. Intangible: Trademarks, Goodwill
Liability Account	These accounts relate to the financial obligations of an organization towards outsiders.	Salaries payable, creditors, outstanding expenses, bank overdrafts, short terms/ long term borrowings. etc.
Capital Fund	These accounts relate to owners of the organization	Educational Institutions funds

Assets = Equities

Assets = Capital + Liabilities (A = C+L)

Capital = Assets – Liabilities (C = A–L)

Liabilities = Assets – Capital (L = A–C)

Effect of Transactions on Accounting Equation:

Illustration

If the capital of a business is ₹ 3,00,000 and other liabilities are ₹ 2,00,000 calculate the total assets of the business.

Solution

Assets = Capital + Liabilities

Capital + Liabilities = Assets

₹ 3,00,000 + ₹ 2,00,000 = ₹ 5,00,000

Illustration

If the total assets of a business are ₹ 3,60,000 and capital is ₹ 2,00,000, calculate liabilities.

Solution

Assets = Capital + Liabilities

Liabilities = Assets – Capital

Assets – Capital = Liabilities

₹ 3,60,000 – ₹ 2,00,000 = ₹ 1,60,000

Illustration

Transaction 1: Murugan started business with ₹ 50,000 as capital.

The business unit has received assets totalling ₹ 50,000 in the form of cash and the claims against the firm are also ₹ 50,000 in the form of capital. The transaction can be expressed in the form of an accounting equation as follows:

Assets = Capital + Liabilities

Cash = Capital + Liabilities

₹ 50,000 = ₹ 50,000 + 0

Transaction 2: Murugan purchased furniture for cash ₹ 5,000.

The cash is reduced by ₹,5,000 but a new asset (furniture) of the same amount has been acquired. This transaction decreases one asset (cash) and at the same time increases the other asset (furniture) with the same amount, leaving the total of the assets of the business unchanged. The accounting equation now is as follows:

			Assets	=	Capital	+	Liabilities
	Cash	+	Furniture	=	Capital	+	Liabilities
Transaction 1	50,000	+	0	=	50,000	+	0
Transaction 2	(–) 5,000	+	5,000	=	0	+	0
	45000	+	5000	=	50000	+	0

Transaction 3*:* He purchased goods for cash ₹ 30,000.

As a result, cash balance is reduced by the goods purchased, leaving the total of the assets unchanged.

					Assets	=	Capital	+	Liabilities
	Cash	+	Furniture	+	Stock	=	Capital	+	Liabilities
Transaction 1&2	45000	+	5000	+	0	=	50000	+	0
Transaction 3	(–) 30,000	+	0	+	30,000	=	0	+	0
	15000	+	5000	+	30000	=	50000	+	0

Transaction 4: He purchased goods on credit for ₹ 20,000.

The above transaction will increase the value of stock on the assets side and will create a liability in the form of creditors.

					Assets	=	Capital	+	Liabilities
	Cash	+	Furniture	+	Stock	=	Capital	+	Creditors
Transaction 1-3	15000	+	5000	+	30000	=	50000	+	0
Transaction 4	0	+	0	+	20000	=	0	+	20000
	15000	+	5000	+	50000	=	50000	+	20000

Transaction 5: Goods costing ₹ 25,000 sold on credit for ₹ 35,000.

The above transaction will give rise to a new asset in the form of Debtors to the extent of ₹ 35,000. But the stock of goods will be reduced by ₹ 25,000 i.e., the cost of goods sold. The net increase of ₹ 10,000 is the amount of revenue which will be added to the capital.

							Assets	=	Capital	+	Liabilities
	Cash	+	Furniture	+	Stock	+	Debtor	=	Capital + Revenue	+	Creditors
Transaction 1-4	15000	+	5000	+	50000	+	0	=	50000	+	20000
Transaction 5		+		+	(-)25,000	+	35000	=	10000	+	0
	15000	+	5000	+	25000	+	35000	=	60000	+	20000

Transaction 6: Rent paid ₹ 3,000.

It reduces cash and the rent is an expense, it results in a loss which decreases the capital.

							Assets	=	Capital	+	Liabilities
	Cash	+	Furniture	+	Stock	+	Debtor	=	Capital	+	Creditors
Transaction 1-5	15000	+	5000	+	25000	+	35000	=	60000	+	20000
Transaction 6	– 3,000	+	0	+	0	+	0	=	– 3,000	+	0
	12000	+	5000	+	25000	+	35000	=	57000	+	20000

From the above transactions, it may be concluded that every transaction has a double effect and in each case – Assets = Capital + Liabilities, i.e., **'Accounting equation is true in all cases'.** The last equation appearing in the books of Mr. Murugan may also be presented in the form of a statement called Balance Sheet. It will appear as below:

Balance Sheet of Mr. Murugan as on . . . .

Liabilities	₹	Assets	₹
Capital	57,000	Cash	12,000
Creditors	20,000	Stock	25,000
		Debtors	35,000
		Furniture	5,000
	77,000		77,000

Practical Problem

Show the Accounting Equation on the basis of the following transactions and prepare a Balance Sheet on the basis of the last equation.

1.	Maharajan commenced business with cash	1,00,000
2.	Purchased goods for cash	70,000
3.	Purchased goods on credit	80,000
4.	Purchased furniture for cash	3,000
5.	d rent	2,000
6.	SolSold goods for cash costing ₹ 45,000	60,000
7.	Paid to creditors	20,000
8.	Withdrew cash for private use	10,000
9.	Paid salaries	5,000
10.	Sold goods on credit (cost price ₹ 60,000)	80,000

Chapter 5
Basic Accounting Procedures – II
Journal

Accounting process starts with identifying the transactions to be recorded in the books of accounts. Accounting identifies only those transactions and events which involve money. They should be of financial character. Business transaction should be supported by documentary evidence such as cash memos, invoices, bills, receipts and vouchers. These business documents are called Source Documents.

In the accounting process, the first step is the recording of transactions in the books of accounts. The origin of a transaction is derived from the source document.

Source Documents

Source documents are the evidences of business transactions which provide information about the nature of the transaction, the date, the amount and the parties involved in it. Transactions are recorded in the books of accounts when they actually take place and are duly supported by source documents. *According to the verifiable objective principle of Accounting,* each transaction recorded in the books of accounts should have adequate proof to support it. These supporting documents are the written and authentic proof of the correctness of the recorded transactions. These documents are required for audit and tax assessment. They also serve as the legal evidence in case of a dispute. Source documents are also prepared for recording internal events such as depreciation and valuation of stocks. The following are the most common source documents.

Cash Memo

When a trader sells goods for cash, he gives a cash memo and when he purchases goods for cash, he receives a cash memo. Details regarding the items, quantity, rate and the price are mentioned in the cash memo.

<table>
<tr><td colspan="4" align="center">Cash Memo</td></tr>
<tr><td colspan="4">Vinoth Watch Co.
135, South Usman Road, Thyagaraya Nagar, Chennai-17.
No: 52   Date : 18.8.2013
To ....</td></tr>
<tr><th>Qty.</th><th>Description</th><th>Rate
₹</th><th>Amount
₹</th></tr>
<tr><td>3</td><td>Titan Regulia</td><td>1,800</td><td>5,400</td></tr>
<tr><td>2</td><td>Titan Raga</td><td>1,200</td><td>2,400</td></tr>
<tr><td></td><td></td><td></td><td>7,800</td></tr>
<tr><td></td><td>Less: Discount 10%</td><td></td><td>780</td></tr>
<tr><td>5</td><td colspan="2" align="center">Total</td><td>7,020</td></tr>
<tr><td colspan="4">Goods once sold are not taken back.
Manager
for Vinoth Watch Co.</td></tr>
</table>

Invoice or Bill

When a trader sells goods on credit, he prepares a sale invoice. It contains full details relating to the amount, the terms of payment and the name and address of the seller and buyer. The original copy of the sale invoice is sent to the purchaser and its duplicate copy is kept for making records in the books of accounts.

Similarly, when a trader purchases goods on credit, he receives a credit bill from the supplier of goods.

INVOICE

Ramesh Electronics
306, Anna Salai, Chennai – 600 002
No. 405

Date : 20.8.2013

Name & address of the Customer: Bhanu Enterprises
43, Eldams Road, Teynampet, Chennai – 18
Terms : 5% cash discount if payment is made within 30 days.

Qty.	Description	Rate ₹	Amount ₹
5	Refrigerators	9,000	45,000
10	Washing Machines	15,000	1,50,000
			1,95,000
	Sales Tax @ 10%		19,500
			2,14,500
	Handling & delivery charges		1,500
15	Total		2,16,000

(Rupees Two lakhs sixteen thousand only)
Partner
E&O.E   for Ramesh Electronics

Note: E.&O.E., means errors and omissions excepted. In other words, if there is any error in the invoice, the same has to be adjusted accordingly.

Receipt

When a trader receives cash from a customer, he issues a receipt containing the date, the amount and the name of the customer. The original copy is handed over to the customer and the duplicate copy is kept for record. In the same way, whenever we make payment, we obtain a receipt from the party to whom we make payment.

RECEIPT	
Saravana Book House	
43, 1st Main Road, Chennai – 35.	
Receipt No. 315	Date :16.9.2013
Received with thanks a sum of ₹ 15,000 (Rupees fifteen thousand only) from M/s. Sulthan & Sons being the supply of books as per the list enclosed.	
Cheque/DD/No. : 10345	
Date: 10.9.2003	
Canara Bank, Trichy	Signature
	Seal

Debit Note

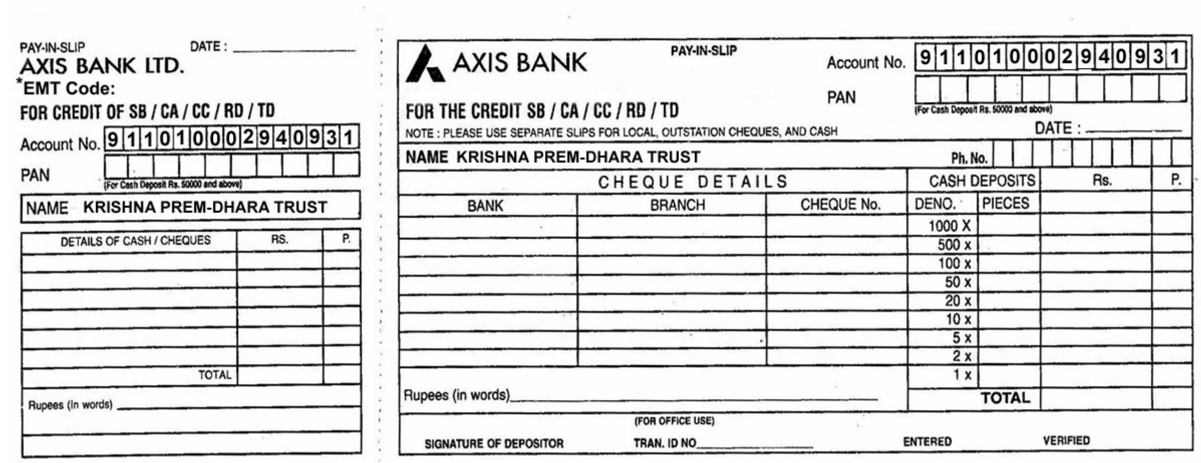
When we return goods to suppliers, we prepare a debit note and sent it to the supplier along with returned goods. It is a source document which contain date of transactions, name of account which is debited, the amount and the reason for debit. A duplicate copy of the debit note is retained by us.

Credit Note

When goods are received back from customers, credit note is send to him indicating that the customer account has been credited in our books. A duplicate copy of the credit note is retained for the record purpose.

Pay-in-slip

Pay-in-slip is a form available in banks and is used to deposit money into a bank account. Each pay-in-slip has a counterfoil which is returned to the depositor duly sealed and signed by the cashier of the bank. This source document relates to bank transactions. It gives details regarding date, account number, amount deposited (in cash or cheque) and name of the account holder.



PAY-IN-SLIP DATE :
AXIS BANK LTD.
*EMT Code:
FOR CREDIT OF SB / CA / CC / RD / TD
Account No. 9 1 1 0 1 0 0 0 2 9 4 0 9 3 1
PAN
(For Cash Deposit Rs. 50000 and above)
NAME KRISHNA PREM-DHARA TRUST

DETAILS OF CASH / CHEQUES	RS.	P.
TOTAL		

Rupees (In words)

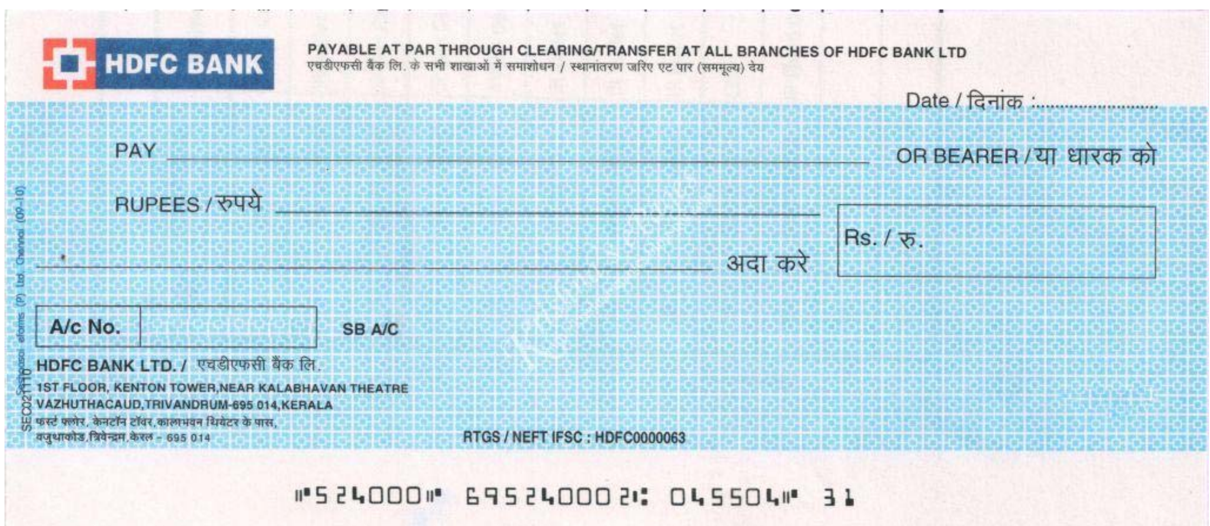
AXIS BANK PAY-IN-SLIP Account No. 9 1 1 0 1 0 0 0 2 9 4 0 9 3 1
PAN
(For Cash Deposit Rs. 50000 and above)
FOR THE CREDIT SB / CA / CC / RD / TD
NOTE : PLEASE USE SEPARATE SLIPS FOR LOCAL, OUTSTATION CHEQUES, AND CASH
DATE :
NAME KRISHNA PREM-DHARA TRUST Ph. No.

CHEQUE DETAILS			CASH DEPOSITS		Rs.	P.
BANK	BRANCH	CHEQUE No.	DENO.	PIECES		
			1000 X			
			500 x			
			100 x			
			50 x			
			20 x			
			10 x			
			5 x			
			2 x			
Rupees (in words)			1 x			
			TOTAL			

SIGNATURE OF DEPOSITOR (FOR OFFICE USE) TRAN. ID NO ENTERED VERIFIED

Cheque

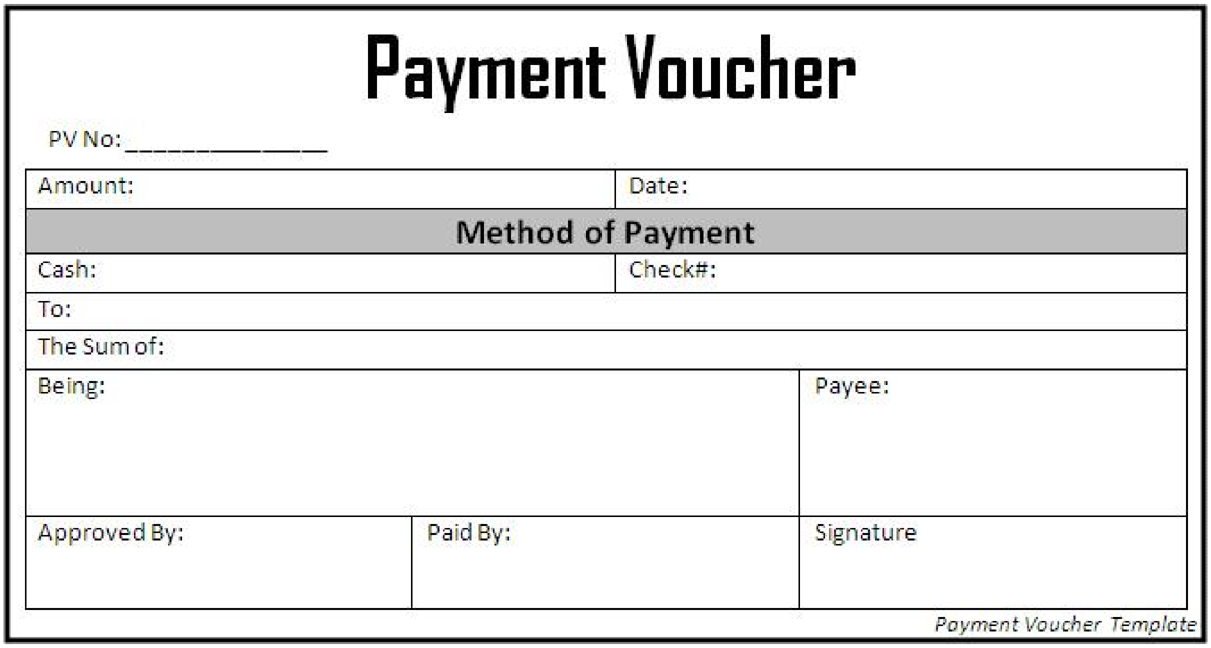
A **cheque** is a document in writing drawn upon a specified banker to pay a specified sum to the bearer or the person named in it and payable on demand. Each cheque book has a counterfoil in which the same details in the cheque are filled. The counterfoil remains with the account holder for his future reference. The counterfoil forms the source document for entries to be made in the books of accounts.



HDFC BANK
PAYABLE AT PAR THROUGH CLEARING/TRANSFER AT ALL BRANCHES OF HDFC BANK LTD
एचडीएफसी बैंक लि. के सभी शाखाओं में समाशोधन / स्थानांतरण जरिए एट पार (सममूल्य) देय
Date / दिनांक :
PAY OR BEARER / या धारक को
RUPEES / रुपये
अदा करे
Rs. / रु.
A/c No. SB A/C
HDFC BANK LTD. / एचडीएफसी बैंक लि.
1ST FLOOR, KENTON TOWER,NEAR KALABHAVAN THEATRE
VAZHUTHACAUD,TRIVANDRUM-695 014,KERALA
RTGS / NEFT IFSC : HDFC0000063
⑈524000⑈ 695240002⑆ 045504⑈ 31

Vouchers

A **voucher** is a written document in support of a business transaction. Vouchers are prepared by an accountant and each voucher is counter signed by an authorised person of the organisation.



Payment Voucher

PV No:______________

Amount:	Date:	
Method of Payment		
Cash:	Check#:	
To:		
The Sum of:		
Being:		Payee:
Approved By:	Paid By:	Signature

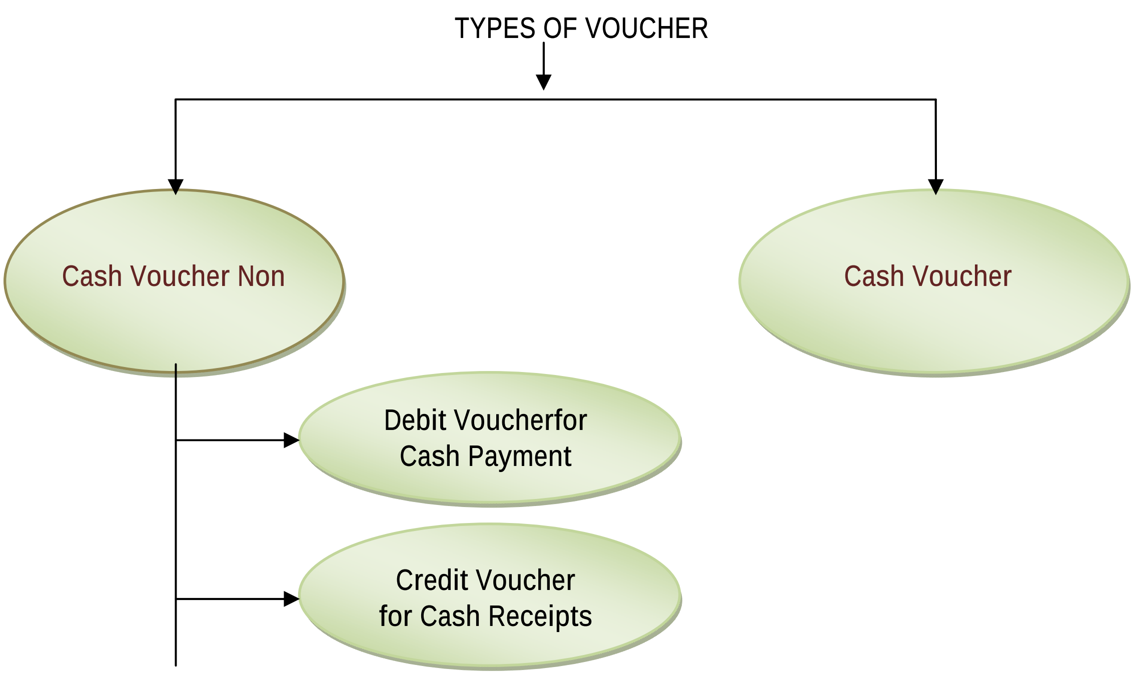
Payment Voucher Template

A serial number is put on each voucher and the relative source documents are attached with the voucher. The vouchers are properly filed according to their serial number so that auditors may easily vouch them and these also serve as a documentary evidence in future.

There are two types of vouchers :-

1. **Cash Vouchers** which record cash transactions such as cash sales, rent paid, etc. Cash Vouchers are again sub divided into two parts i.e. **Debit Voucher for Cash Payment** which include paid for expense, paid for purchase of goods, etc and **Credit voucher for Cash Receipts** which include receipt of cash from debtor, cash sales, etc.

2. **Non-Cash Voucher** which record non cash transactions such as credit sales, bad-debt, etc.



Distinction between Source Document and Voucher Document

S. No.	Source Document	Voucher Document
1.	It is a support to the voucher.	It is supported by the source document.
2.	It is not prepared to record transaction.	It is prepared to record transaction.
3.	It is an evidence of the transaction.	It is a document of correct recording of transactions.
4.	It contains full details of transactions.	It puts emphasis on which account is debited and which account is credited.

Rules for Debiting and Crediting

In actual practice, the individual transactions of similar nature are recorded, added and subtracted at one place. Such place is customarily the meaning of debit and credit, it is essential to understand the meaning and form of an account.

An account is a record of all business transactions relating to a particular person or asset or liability or expense or income. In accounting, we keep a separate record of each individual, asset, liability, expense or income. The place where such a record is maintained is termed as an 'Account'.

All accounts are divided into two sides. The left hand side of an account is called Debit side and the right hand side of an account is called Credit side. In the abbreviated form Debit is written as Dr. and Credit is written as Cr. For example, the transactions relating to cash are recorded in an account, entitled 'Cash Account' and its format will be as given below:

Debit (Dr.)	Cash Account	Credit (Cr.)

In order to decide when to write on the debit side of an account and when to write on the credit side of an account, there are two approaches. They are: 1) Accounting Equation Approach, 2) Traditional Approach.

Nature of Account

The accounting equation is a statement of equality between the debits and the credits. The rules of debit and credit depend on the nature of an account. For this purpose, all the accounts are classified into the following five categories in the accounting equation approach:-

1. Assets Accounts
2. Capital Account
3. Liabilities Accounts
4. Revenues or Incomes Accounts
5. Expenses or Losses Accounts

If there is an increase or decrease in one account, there will be equal decrease or increase in another account. Accordingly, the following rules of debit and credit in respect of the various categories of accounts can be obtained.

The rules may be summarised as below:-

1. Increases in assets are debits; decreases in assets are credits.
2. Increases in capital are credits; decreases in capital are debits.
3. Increases in liabilities are credits; decreases in liabilities are debits.
4. Increases in incomes and gains are credits; decreases in incomes and gains are debits.
5. Increases in expenses and losses are debits; decreases in expenses and losses are credits.

Another manner to understand the concept of Debit and Credit is – The "Normal Balance" manner:

Each account has a debit and a credit side. You could picture that as a big letter T, hence the term "T-account". Again, debit is on the left side and credit on the right. Normal balance is the side where the balance of the account is normally found.

Asset accounts normally have debit balances, while liabilities and capital normally have credit balances. Income has a normal credit balance since it increases capital . On the other hand, expenses and withdrawals decrease capital, hence they normally have debit balances.

Now what is the significance of the "normal balance"?

When you place an amount on the normal balance side, you are increasing that account. If you put an amount on the opposite side, you are decreasing the account. Therefore, to increase an asset, you debit it. To decrease an asset, you credit it. To increase liability and capital accounts, credit. To decrease them, debit.

Example

Let us take Cash. Cash is an asset account. Again, asset accounts normally have debit balances. Therefore, to increase Cash you debit it. To decrease Cash, you credit it.

For another example, let's take Accounts Payable. It is a liability account. Liability accounts normally have credit balances. Thus, if you want to increase Accounts Payable, you credit it. If you want to decrease Accounts Payable, you debit it.

And the same rule applies to all asset, liability, and capital accounts.

To Sum It Up

Here's a table summarizing the normal balances of the accounting elements, and the actions to increase or decrease them. Notice that the normal balance is the same as the action to increase the account.

Accounting element	Normal Balance	To increase	To decrease
Assets	Dr	Dr	Cr
Liabilities	Cr	Cr	Dr
Capital	Cr	Cr	Dr
Withdrawal	Dr	Dr	Cr
Income	Cr	Cr	Dr
Expense	Dr	Dr	Cr

In the traditional approach, all the accounts are classified into the following three types.

1. Personal Accounts
2. Real Accounts

3. Nominal Accounts

Golden Rules for Debit and Credit:

1.	Personal Accounts	–	(a) Debit the receiver	(b) Credit the giver
2.	Real Accounts	–	(a) Debit what comes in	(b) Credit what goes out
3.	Nominal Accounts	–	(a) Debit all expenses and losses	(b) Credit all incomes and gains

Books of Original Entry

The books in which a transaction is recorded for the first time from a source document are called Books of *Original Entry or Prime Entry.* Journal is one of the books of original entry in which transactions are originally recorded in a chronological (day-to-day) order according to the principles of Double Entry System.

Journal

Journal is a date-wise record of all the transactions with details of the accounts debited and credited and the amount of each transaction.

Format
Journal of ....

Date	Particulars	L.F.	Debit Amount ₹	Credit Amount ₹

Explanation:

1. **Date**: In the first column, the date of the transaction is entered. The year and the month is written only once, till they change. The sequence of the dates and months should be strictly maintained.
2. **Particulars:** Each transaction affects two accounts, out of which one account is debited and the other account is credited. The name of the account to be debited is written first, very near to the line of particulars column and the word Dr. is also written at the end of the particulars column. In the second line, the name of the account to be credited is written, starts with the word 'To', a few space away from the margin in the particulars column to the make it distinct from the debit account.
3. **Narration:** After each entry, a brief explanation of the transaction together with necessary details is given in the particulars column with in brackets called narration. The words 'For' or 'Being' are used before starting to write down narration. Now, it is not necessary to use the word 'For' or 'Being'. It helps to know in future the reason for the entry and as to why particular amount is debited or credited
4. **Ledger Folio (L.F):** All entries from the journal are later posted into the ledger accounts. The page number or folio number of the Ledger, where the posting has been made from the Journal is recorded in the L.F column of the Journal. Till such time, this column remains blank.
5. **Debit Amount**: In this column, the amount of the account being debited is written.
6. **Credit Amount**: In this column, the amount of the account being credited is written.

Steps in Journalising

The process of analysing the business transactions under the heads of debit and credit and recording them in the Journal is called **Journalising**. An entry made in the journal is called a '**Journal Entry**'.

Step 1 — Determine the two accounts which are involved in the transaction.

Step 2 — Classify the above two accounts under Personal, Real or Nominal.

Step 3 — Find out the rules of debit and credit for the above two accounts.

Step 4 — Identify which account is to be debited and which account is to be credited.

Step 5 — Record the date of transaction in the date column. The year and month is written once, till they change. The sequence of the dates and months should be strictly maintained.

Step 6 — Enter the name of the account to be debited in the particulars column very close to the left hand side of the particulars column followed by the abbreviation Dr. in the same line. Against this, the amount to be debited is written in the debit amount column in the same line.

Step 7 — Write the name of the account to be credited in the second line starting with the word 'To' a few space away from the margin in the particulars column. Against this, the amount to be credited is written in the credit amount column in the same line.

Step 8 — Write the narration within brackets in the next line in the particulars column.

Step 9 — Draw a line across the entire particulars column to separate one journal entry from the other.

Illustration

1. Exam fees received – ₹ 15 lakh

Cash at Bank	Dr	15,00,000	
To Exam Fees			15,00,000
(Being Exam fees received.)			

Rule

Debit what comes in

Credit all income

2. Salary paid – ₹ 2 lakh

Salary	Dr	2.00,000	
To Cash at bank			2,00,000
(Being Salary amount paid.)			

Rule

Debit all expenses

Credit what goes out

3. Furniture purchased for (cash purchase) ₹ 1 lakh

Furniture	Dr	1,00,000	
To Cash			1,00,000
(Being furniture purchase for cash)			

Rule

Debit what comes in

Credit what goes out

4. Computer purchased on credit ₹ 1.5 lakh

Computer	Dr	1,50,000	
To Creditor			1,50,000

(Being computer purchase on credit)

Rule

Debit what comes in

Credit the giver

5. In entry no. 1 out of ₹ 5 lakh, ₹ 1 lakh was on account of Hostel charges.

Exam Fees	Dr	1,00,000	
To Hostel Charges			1,00,000

(Being hostel charges received)

Rule

Debit decrease in income

Credit all income

6. Interest for ₹ 1 lakh has become due but has not been received

Interest Receivable/ Accrued Interest	Dr	1,00,000	
To Interest			1,00,000

(Being Interest amount accrued but not received)

Rule

Debit what comes in – right to get interest

Credit all income

7. Creditor for Computer paid ₹ 1 lakh

Creditor	Dr	1,00,000	
To Cash at Bank			1,00,000

(Being cash paid to creditor)

Rule

Debit the receiver

Credit what goes out

8. Money received from Alumini for construction of road – ₹ 100 lakh

Cash at Bank	Dr	10,00,000	
To Advance – Alumini			10,00,000

(Being advance amount received from Alumini for construction of road)

9. Work for CC pavement awarded to M/s X & Co.

No Entry

10. M/s X & Co. completes the work, work is certified and bill is passed for ₹ 3 lakh (Security Deposit ₹ 30,000, TDS ₹ 15,000, Work Tax ₹ 10,000)

CC Pavement	Dr	3,00,000	
To Security Deposit			30,000
To TDS – Contractor			15,000
To Work Tax			10,000
To M/s X & Co.			2,45,000

(Being amount to be paid to M\s X & Co. for CC Pavement)

11. Cash Withdrawn from bank ₹ 5 lakh

Cash in hand	Dr	5,00,000	
To Cash at Bank			5,00,000

(Being cash withdrawn from bank)

12. Permanent Imprest issued to Mr. A ₹ 50,000

Permanent Imprest-Mr. A	Dr	50,000	
To Cash at Bank			50,000

(Being paid to Mr. A for petty cash expenses)

13. Mr. A submit bills and permanent imprest recouped

Stationery	Dr	15,000	
Running & Maint. of Vehicles	Dr	30,000	
To Permanent Imprest-Mr. A			45,000

(Being Stationery items purchase and vehicles repaired)

Permanent Imprest-Mr. A	Dr	45,000	
To Cash at Bank			45,000

(Being Imprest amount recouped)

14. Salary bill for Mr. B passed for ₹ 25,000. Deduction on account of PPF & TDS to be made for ₹ 3,000 & ₹ 2,000 respectively, payment made.

Pay & Allowance	Dr	25,000	
To PPF			3,000
To TDS-Salary			2,000
To Salary Payable			20,000

(Being salary amount due after deducting PPF and TDS)

Salary Payable	Dr	20,000	
To Cash at Bank			20,000

(Being salary paid to employees)

Accounting Entry Related To MGNREGA scheme

(1) At the time of Government Grant Received:

Bank Account Debit

To Government Grant*

(Being Government Grant Received From DPRO Office Under ………… Scheme)

Note -* Separate Grant Account be opened for each type of grant.

(2) At the time of Cash Withdrawal from Bank:

Cash Account Debit

To Bank Account

(Being Cash withdrawn from bank for ………………. Purpose)

(3) For Cash Deposited in Bank:

Bank Account Debit

To Cash Account

(Being Cash deposited in Bank.)

(4) For Wages / Salary Paid:

Wages / Salary Account Debit

To Bank / Cash Account

(Being Wages / Salaries paid to labour / workers by MGNREGA LIST NO ……. Vide Cheque No…….)

(5) For Wages / Salaries Payable:

Wages / Salary Account Debit

To Wages / Salary Payable Account

(Being Wages / Salary to be paid for the period ……… / Muster Role No ……)

(6) For Expensed Paid in Cash:

Expenses Account (Name of Expense) Debit

To Cash Account

(Being Expenses Paid.)

(7) For Expenses paid by Cheque:

Expenses Account (Name of Expense) Debit

To Bank Account

(Being Expenses paid vide Cheque No ………)

(8) For Material Purchased (Cement, Brick, Nursery Plant etc.):

Material (By Name) Purchased Account Debit

To Bank / Cash Account

(Being Material Purchased vide bill / C.M. No ……. And paid by Cheque No…….)

(9) **For payment of Freight:**

Freight Account Debit

To Cash/Bank Account

(Being Freight paid for material purchased vide bill no………)

(10) **For Bank Charges:**

Bank Charges Account Debit

To Bank Account

(Being Bank charges paid/ deducted………….)

(11) **For Interest Income:**

Bank Account Debit

To Bank Interest

(Being Interest earned on Saving Bank A/c No.)

(12) **For Payment to Program Coordinator:**

Program Coordinator Account Debit

To Bank Account

(Being payment made to Program Coordinator vide Ch. No.)

(13) **For Machinery / other assets purchased**

Machinery / other assets Account Debit

To bank / Cash

(Being ………. Purchased vide bill / CM No……… from M/s………..)

(14) **For sale of Wastage / Salvage / Scrap / Old Machinery**

Bank / Cash Account Debit

To Wastage / Salvage / Scrap / Old Machinery

(Being sale of ………………..)

Practical Problems

1. Correct the following entries wherever you think:

(i) **Brought capital in to business:**

Capital A/c Dr.

To Cash A/c

(ii) **Cash Purchases:**

Cash A/c Dr.

To Sales A/c

(iii) Salaries paid to clerk Mr.Kanniyappan:

Salaries A/c Dr.

To Kanniyappan A/c

(iv) Paid carriage:

Carriage A/c Dr.

To Cash A/c

2. What do the following Journal Entries mean?

(i) Cash A/c Dr.

To Furniture A/c

(ii) Rent A/c Dr.

To Cash A/c

(iii) Bank A/c Dr.

To Cash A/c

(iv) Tamilselvi A/c Dr.

To Sales A/c

3. Journalise the following Opening Entry:

	₹
Cash in hand	2,000
Plant	50,000
Furniture	5,000
Creditors	13,000
Debtors	18,000

4. Journalise the following transactions in the books of Tmt. Amutha

		₹
2013, Jan.1	Tmt. Amutha commenced business with cash	50,000
2	Purchased goods for cash	10,000
5	Purchased goods from Mohan on credit	6,000
7	Paid into Bank	5,000
10	Purchased furniture	2,000
20	Sold goods to Suresh on credit	5,000
25	Cash sales	3,500
26	Paid to Mohan on account	3,000
31	Paid salaries	2,800

5. Journalise the following transactions of Mrs. Rama

		₹
2013, Jan1	Mrs. Rama commenced business with cash	30,000
2	Paid into bank	21,000
3	Purchased goods by cheque	15,000
7	Drew cash from bank for office use	3,000
15	Purchased goods from Siva	15,000
20	Cash sales	30,000
25	Paid to Siva	14,750
	Discount Received	250
31	Paid rent	500
	Paid Salaries	2,000

6. Journalise the following transactions of Mr.Moorthi

		₹
2013, June 3	Received cash from Ramkumar	60,000
4	Purchased goods for cash	15,000
11	Sold goods to Damodaran	22,000
13	Paid to Ramkumar	40,000
17	Received from Damodaran	20,000
20	Bought furniture from Jagadeesan	5,000
27	Paid rent	1,200
30	Paid salary	2,500

7. Journalise the following in the Journal of Thiru. Gowri Shankar

		₹
2013, Oct. 1	Received cash from Siva	75,000
7	Paid cash to Sayeed	45,000
10	Bought goods for cash	27,000
12	Bought goods on credit from David	48,000
15	Sold goods for cash	70,000

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

		₹
2013, Feb. 3	Bought goods for cash	84,500
7	Sold goods to Dhanalakshmi on credit	`55,000

9	Received commission	3,000
10	Cash Sales	1,09,000
12	Bought goods from Mahalakshmi	60,000
15	Received five chairs from Revathi & Co. at	400 each
20	Paid Revathi & Co., cash for five chairs	
28	Paid Salaries	10,000
	Paid Rent	5,000

9. Journalise the following transactions in the books of Thiru. Kalyanasundaram.

		₹
2013, March 1	Sold goods on credit to Mohanasundaram	75,000
12	Purchased goods on credit from Bashyam	70,000.
15	Sold goods for cash to David	50,000.
20	Received from Mohanasundaram	70,000.
25	Paid to Bashyam	50,000.

Chapter 6

Basic Accounting Procedures – III

Ledger

In the Journal, each transaction is dealt with separately. Therefore, it is not possible to know at a glance, the net result of many transactions. So, in order to ascertain the net effect, all the transactions relating to a particular account are collected at one place in the Ledger.

A Ledger is a book which contains all the accounts whether personal, real or nominal, which are first entered in journal or special purpose subsidiary books.

The ledger that is normally used in a majority of business concerns is a bound note book. This can be preserved for a long time. Its pages are consequently numbered. Each account in the ledger is opened preferably on a separate page. If one page is completed, the account will be continued in the next or some other page. But in bigger concerns, it is not practical to keep the ledger as a bound note book, Loose-leaf ledger now takes the place of a bound note book. In a loose-leaf ledger, appropriate ruled sheets of thick paper are introduced and fixed up with the help of a binder. Whenever necessary additional pages may be inserted, completed accounts can be removed and the accounts may be arranged and rearranged in the desired order. Therefore, this type of ledger is known as **Loose-leaf Ledger/ Loose-leaf Binder**.

According to L.C. Cropper, "The books which contain a classified and permanent record of all transactions of a business is called a Ledger."

Need and Importance of Ledger

1. How much amount is due from customer?
2. How much amount the firm has to pay to each supplier?
3. How much amount has been spent on expenditure?
4. How much amount has been earned on income?

Utility

Ledger is a principal or main book which contains all the accounts in which the transactions recorded in the books of original entry are transferred. Ledger is also called the **'Book of Final Entry'** or **'Book of Secondary Entry'**, because the transactions are finally incorporated in the Ledger. The following are the advantages of ledger:

(i) **Complete information at a glance:** All the transactions pertaining to an account are collected at one place in the ledger. By looking at the balance of that account, one can understand the collective effect of all such transactions at a glance.

(ii) **Arithmetical Accuracy:** With the help of ledger balances, Trial balance can be prepared to know the arithmetical accuracy of accounts.

(iii) **Result of Business Operations:** It facilitates the preparation of final accounts for ascertaining the operating result and the financial position of the business concern.

(iv) **Accounting information:** The data supplied by various ledger accounts are summarised, analysed and interpreted for obtaining various accounting information.

Format

Name of Account

Dr. Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
Year Month Date	To (Name of Credit Account in Journal)			Year Month Date	By (Name of Debit account in Journal)		

Posting

The process of transferring the entries recorded in the journal or subsidiary books to the respective accounts opened in the ledger is called Posting. In other words, posting means grouping of all the transactions relating to a particular account at one place. It is necessary to post all the journal entries into various accounts in the ledger because posting helps us to know the net effect of various transactions during a given period on a particular account.

Rules of posting

All transactions relating to an account should be entered at one place. In other words, two separate accounts should not be opened for posting transactions relating to the same account.

1. The word "To" is used before the account which appears on the debit side of an account. Similarly, the word "By" is used before the account which appears on the credit side of an account.
2. If an account has been debited in the Journal entry, the posting in the Ledger should also be made on the debit side of such account. In the Particular column, the name of the other account which has been credited in the Journal entry should be written for reference.
3. If an account has been credited in the Journal entry, the posting in the ledger should also be made on the credit side of such account. In the Particular column, the name of the other account which has been debited in the Journal entry should be written for reference.
4. Similar amount which has been posted on the debit side of an account should also be posted on the credit side of another account.

Illustration:

Mr. Ram started business with cash ₹ 5,00,000 on 1st June 2013.

The above transaction will appear in Journal and Ledger as under.

Solution:

In the Books of Ram

Journal

2013	Cash A/c.	Dr	5,00,000	
June 1	To Ram's Capital A/c			5,00,000

(Ram started business with ₹ 5,00,000)

Note: Here two accounts are involved, Cash Account and Ram's capital account, so we should allot in the ledger a page for each account.

Ledger

Dr. Cash Account Cr.

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F.	Amount ₹
2013 June 1	To Ram's Capital A/c		5,00,000 5,00,000				

Dr. Ram's Capital Account Cr.

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F.	Amount ₹
				2013 June 1	By Cash A/c		5,00,000

Illustration:

Journalise the following transactions in the books of Amar and post them in the Ledger:

2013		
March 1	Bought goods for cash	₹ 25,000
2	Sold goods for cash	₹ 50,000
3	Bought goods for credit from Gopi	₹ 19,000
5	Sold goods on credit to Robert	₹ 8,000
7	Received from Robert	₹ 6,000
9	Paid to Gopi	₹ 5,000
20	Bought furniture for cash	₹ 7,000

Journal of Amar

Date	Particulars		L.F	Debit ₹	P.	Credit ₹	P.
2013 Mar 1	Purchases A/c To Cash A/c (Cash purchases)	Dr.		25,000	–	25,000	–
2	Cash A/c To Sales A/c (Cash Sales)	Dr.		50,000	–	50,000	–
3	Purchases A/c To Gopi A/c (Credit purchases)	Dr.		19,000	–	19,000	–
5	Robert A/c To Sales A/c (Credit Sales)	Dr.		8,000	–	8,000	–

7	Cash A/c Dr. To Robert A/c (Cash received)		6,000	–	6,000	–
9	Gopi A/c Dr. To Cash A/c (Cash paid)		5,000	–	5,000	–
20	Furniture A/c. Dr. To Cash A/c (furniture purchased)		7,000	–	7,000	–

Explanation: There are six accounts involved: Cash, Purchases, Sales, Furniture, Gopi & Robert, so six accounts are to be opened in the ledger.

Ledger of Account

Dr. Cash Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 Mar 5 7	 To Sales A/c To Robert A/c		 50,000 6,000	2013 Mar 1 9 20	 By Purchases A/c By Gopi A/c By Furniture A/c		 25,000 5,000 7,000

Dr. Purchases Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 Mar 1 3	 To Cash A/c To Gopi A/c		 25,000 19,000				

Dr. Sales Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
				2013 Mar 2 5	 By Cash A/c By Robert A/c		 50,000 8,000

Dr. Furniture Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 Mar 20	 To Cash A/c		 7,000				

Dr. **Gopi Account** Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 Mar 9	To Cash A/c		5,000	2013 Mar 3	By Purchase A/c		19000

Dr. **Robert Account** Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 Mar 5	To Sales A/c		8,000	2013 Mar 7	By Cash A/c		6000

Posting of Compound Journal Entries

Compound or Combined Journal Entry is one where more than one transactions are recorded by passing only one journal entry instead of passing several journal entries. Since every debit must have the corresponding equal amount of credit, special care must be taken in posting the compound journal entry, where there may be only one debit aspect but many corresponding credit aspects of equal value or vise versa. The posting of such transactions is done in the same way as already explained.

Illustration: Jan. 12, 2013, Cash sales ₹ 10,000, Cash received from Kannan ₹ 5,000 and commission earned ₹ 2,500.

Date	Particulars	LF	Debit ₹	Credit ₹
2013	Cash A/c. Dr			
Jan 12	To Sales A/c.		17,500	
	To Kannan's A/c.			10,000
	To Commission A/c.			5,000
	(Received cash for sale, from			2,500
	Kannan and as commission)			

Solution :

Ledger

Cash Account

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F.	Amount ₹
2013 Jan 12	To Sales A/c		10,000				
	To Kannan's A/c		5,000				
	To Commission A/c		2,500				

Dr. Kannan's Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
				2013 Jan 12	By Cash A/c		5,000

Dr. Commission Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
				2013 Jan 12	By Cash A/c		2,500

Dr. Sales Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
				2003 Jan 12	By Cash A/c		10,000

Note: In the above transactions, there is only one debit aspect namely cash account and three credit aspects. Therefore, while posting in the cash account, the names of three credit aspects are entered in the cash account on the debit side, thus having a total of ₹ 17,500 which is equal to the amount in the debit column of the journal.

The cash account is written on the credit side of the three accounts, namely, Sales, Kannan and Commission received, as it acts as an opposite and corresponding accounts for Sales ₹ 10,000, Kannan ₹ 5,000 and Commission ₹ 2,500 respectively which are equal to the amount in the credit column of the journal.

Posting the Opening Entry

The opening entry is passed to open the books of accounts for the new financial year. The debit or credit balance of an account what we get at the end of the accounting period is known as closing balance of that account. This **closing balance becomes the opening balance in the next accounting year**.

The procedure of posting an opening entry is same as in the case of an ordinary journal entry. An account which has a **debit balance**, the words '**To balance b/d**' are recorded on the debit side in the particulars column. An account which has a **credit balance**, the words "**By balance b/d**" are recorded in the particulars column on the credit side. In fact opening entry is not actually posted but the accounts are merely incorporated in the ledger, if the ledger is a new one or old.

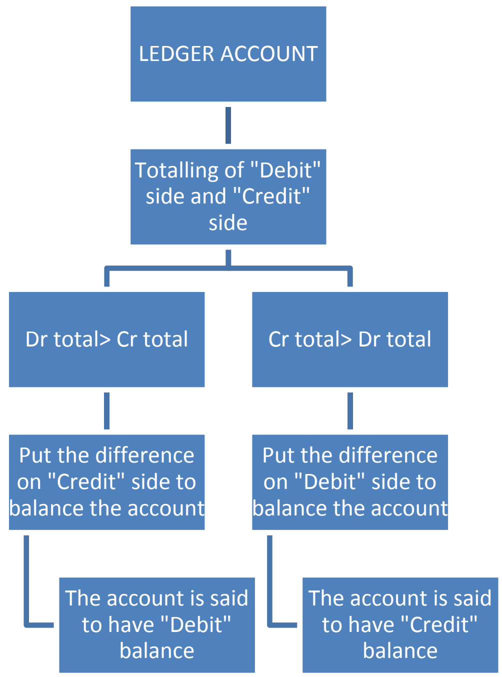
Balancing an Account

The first step in preparation of financial statements is "Balancing of Accounts". This step is carried after all the transactions are accounted. In order to balance an account, the two sides, namely Debit and Credit are totalled up separately and the difference is ascertained.

Balance is the difference between the total debits and the total credits of an account. When posting is done, many accounts may have entries on their debit side as well as credit side. The net result of such debits and credits in an account is the balance.

Balancing means the writing of the difference between the amount columns of the two sides in the lighter (smaller total) side, so that the grand totals of the two sides become equal.

If debit side of an account is heavier than the credit side, the account is said to have Debit balance and if credit side is heavier than the debit side, the account is said to have Credit balance. It could be understood as under-



Significance of balancing

There are three possibilities while balancing an account during a given period. It may be a debit balance or a credit balance or a nil balance depending upon the debit total and the credit total.

(i) **Debit Balance**: The excess of debit total over the credit total is called the debit balance. When there is only debit entry in an account, the amount itself is the balance of that account, i.e., the debit balance. It is first recorded on the credit side, above the total. Then it is entered on the debit side, below the total, as the first item for the next period.

Dr. Cash Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
2013				2013			
Mar 2				Mar 5			
12	To Sales A/c		15,000	28	By Purchase A/c		8,000
	To Kumar's A/c		4,000		By Salary A/c		2,500
					By Balance c/d		8,500
			19,000	31			19,000
Apr 1	To Balance b/d		8,500				

(ii) **Credit Balance:** The excess of credit total over the debit total is called the credit balance. When there is only credit entry in an account, the amount itself is the balance of that account i.e., the credit balance. It is first written in the debit side, as the last item, above the total. Then it is recorded on the credit side, below the total, as the first item for the next period.

Dr. Capital Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 Mar 31	To Balance c/d		50,000	2012 Apr 1	By Cash		50,000
			50,000				50,000
				2013 Apr 1	By Balance b/d		50,000

(iii) **Nil Balance:** When the total of debits and credits are equal, it is closed by merely writing the total on both the sides. It indicates the equality of benefits received and given by that account.

Dr. Shankar Account Cr.

Date	Particulars	J.F	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 Mar 20	To Sales A/c		6,000	2013 Mar 25	By Cash		6,000
			6,000				6,000

Balancing of different accounts

Balancing is done periodically, i.e., weekly, monthly, quarterly, half- yearly or yearly, depending on the requirements of the business.

(i) **Personal Accounts:** These accounts are generally balanced regularly to know the amounts due to the persons (**creditors**) or due from the persons (**debtors**).

(ii) **Real Accounts** : These accounts are generally balanced at the end of the financial year, when final accounts are being prepared. However, cash account is frequently balanced to know the **cash on hand**. A debit balance in an asset account indicated the **value of the asset** owned by the business. Assets accounts always show debit balances.

(iii) **Nominal Account**: These accounts are in fact, not to be balanced as they are to be closed by transfer to final accounts. A debit balance in a nominal account indicates that it is **an expense or loss**. A credit balance in a nominal account indicates that it is **an income or gain**.

All such balances in personal and real accounts are shown in the Balance Sheet and the balances in nominal accounts are taken to the Profit and Loss Account.

Distinction between Journal and Ledger

Books of original entry (Journal) and Ledger can be distinguished as follows:

Basis of Distinction	Journal	Ledger
1. Book	It is the book of prime entry.	It is the main book of account.
2. Stage	Recording of entries in these books is the first stage.	Recording of entries in the ledger is the second stage.
3. Process	The process of recording entries in these books is called “Journalising”.	The process of recording entries in the ledger is called “Posting”.
4. Transactions	Transactions relating to a person or property or expense are spread over.	Transactions relating to a particular account are found together on a particular page.
5. Net effect	The final position of a particular account cannot be found.	The final position of a particular account can be ascertained just at a glance.
6. Next Stage	Entries are transferred to the ledger.	From the Ledger, first the Trial Balance is drawn and then final accounts are prepared.
7. Tax authorities	Do not rely upon these books	Rely on the ledger for assessment purpose.
8. Accuracy	Accuracy of books cannot be tested.	Accuracy of books can be tested by preparing Trial Balance.

Chapter 7
Subsidiary Books-I
Special Purpose Books

For a business having a large number of transactions it is practically impossible to write all transactions in one journal, because of the following limitations.

(i) Periodical details of some important business transactions cannot be known, from the journal easily, e.g., monthly sales, monthly purchases.

(ii) Such a system does not facilitate the installation of an internal check system since the journal can be handled by only one person.

(iii) The journal becomes bulky and voluminous.

Need

Moreover, transactions can be classified and grouped conveniently according to their nature, as some transactions are usually of repetitive in nature. Generally, **transactions are of two types: Cash and Credit.** Cash transactions can be grouped in one category whereas credit transactions can be grouped in another category. Thus, in practice, the main journal is sub-divided in such a way that a separate book is used for each category or group of transactions which are repetitive and sufficiently large in number.

Each one of the subsidiary books is a special journal and a book of original or prime entry. Though the usual type of journal entries are not passed in these sub-divided journals, the double entry principles of accounting are strictly followed.

Kinds of Subsidiary Books

The number of subsidiary books may vary according to the requirements of each business. The following are the special purpose subsidiary books.

Transactions

Day Books
- Purchase Book
- Sales Book
- Purchase Return
- Sales Return

Bills Books
- Bill Receivable Book
- Bill Payable Book

Cash Book

Journal Proper

Purpose

1. **Purchases Book** records only credit purchases of goods by the trader.
2. **Sales Book** is meant for entering only credit sales of goods by the trader.
3. **Purchases Return Book** records the goods returned by the trader to suppliers.
4. **Sales Return Book** deals with goods returned (out of previous sales) by the customers.

5. **Bills Receivable Book** records the receipts of bills (Bills Receivable).
6. **Bills Payable Book** records the issue of bills (Bills Payable).
7. **Cash Book** is used for recording only cash transactions i.e. receipts and payments of cash.
8. **Journal Proper** is the journal which records the entries which cannot be entered in any of the above listed subsidiary books.

Advantages

The advantages of maintaining subsidiary books can be summarised as under:

1. **Division of Labour:** The division of journal, resulting in division of work, ensures more clerks working independently in recording original entries in the subsidiary books.
2. **Efficiency:** The division of labour also helps the reduction in work load, saving in time and stationery. It also gives advantages of specialisation leading to efficiency.
3. **Prevents Errors and Frauds:** The accounting work can be divided in such a manner that the work of one person is automatically checked by another person. With the use of internal check, the possibility of occurrence of errors and frauds may be avoided.
4. **Easy Reference:** It facilitates easy references to any particular item. For instance total credit sales for a month can be easily obtained from the Sales Book.
5. **Easy Postings:** Posting from the subsidiary books are made at convenient intervals depending upon the nature of the business.

Purchases Book

Purchases book also known as **Bought Day Book** is used to record all credit purchases of goods which are meant for resale in the business. **Cash purchases of goods, cash and credit purchases of assets are not entered in this book.**

Format

Purchases Book

Date	Particulars	Inward Invoice No.	L.F.	Amount		Remarks
				Details ₹	Total ₹	

1. **Date Column** – Represents the date on which the transaction took place.
2. **Particulars Column** – This column includes the name of the seller and the particulars of goods purchased.
3. **Inward Invoice No. Column** – Reveals the serial number of the inward invoice.
4. **LF. Column** – This column shows the page number of the suppliers account in the ledger accounts.
5. **Details Column** – Reveals the amount of goods purchased and the amount of trade discount.

6. **Total Column** – This column represents the net price of the goods, i.e. the amount which is payable to the creditors after adjusting discount and expenses if any.

7. **Remarks Column** – Contains any extra information.

At the end of each month, the purchase book is totalled. The total shows the total amount of goods or materials purchased on credit.

Difference between Purchase Book and Purchase Account

S.No.	Purchase Book	Purchase Account
1.	It is a part of Journal.	It is a part of Ledger.
2.	It is not divided into debit and Credit sides.	It is divided into debit and Credit sides.
3.	It record only credit purchase of goods.	It record both cash and credit purchase of goods.

Illustration: From the following transactions of Ram for July, 2013 prepare the Purchases Book and ledger accounts connected with this book.

2013

July	5	Purchased on credit from Kannan & Co.	
		50 Iron boxes	@ ₹ 500
		10 Grinders	@ ₹ 3,000
	6	Purchased for cash from Siva & Bros.	
		25 Fans	@ ₹ 1,250
	10	Purchased from Balan & Sons on credit	
		20 Grinders	@ ₹ 2,500
		10 Mixie	@ ₹ 3,000
	20	Purchased, on credit, one Computer from Kumar for ₹ 35,000.	

Solution:

In the books of Ram
Purchase Book

Date	Particulars	Inward Invoice No.	L.F.	Amount Details ₹	Amount Total ₹
2013					
July 5	Kannan & Co.				
	50 Iron boxes @ ₹ 500			25,000	
	10 Grinders @ ₹ 3,000			30,000	55,000
	Goods purchased vide their bill No....... Dated......				
	Balan & Co.				
10	20 Grinders @ ₹ 2,500			50,000	

	10 Mixie @ ₹ 3,000 Goods purchased vide their bill No....... Dated......			30,000	80,000
	Total				1,35,000

Ledger Accounts

Dr. Purchases Account Cr.

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 July 31	To Sundries as per Purchases Book		1,35,000				

Dr. Kannan & Co. Account Cr.

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F	Amount ₹
				2013 July 5	By Purchases A/c		55,000

Dr. Balan & Co. Account Cr.

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F	Amount ₹
				2013 July 10	By Purchases A/c		80,000

Note : July 6th transaction is a cash transaction and July 20th transaction is purchase of an asset, so both will not be recorded in the purchases book.

Sales Book

The sales book is used to record all credit sales of goods dealt with by the trader in his business. **Cash sales, cash and credit sales of assets are not entered in this book.** The entries in the sales book are on the basis of the invoices issued to the customers with the net amount of sale. The format of sales book is shown below:-

Format

Sales Book

Date	Particulars	Outward Invoice No.	L.F.	Amount		Remarks
				Details ₹	Total ₹	

1.	Date Column	–	Represents the date on which the transaction took place.
2.	Particulars Column	–	This column includes the name of purchasers and the particulars of goods sold.
3.	Outward Invoice No. Column	–	Reveals the serial number of the outward invoice.
4.	L.F. Column	–	The page number of the customers accounts in the Ledger is recorded.
5.	Details Column	–	Contains the amount of goods sold and the amount of trade discount if any.
6.	Total Column	–	This column shows the net amount which is receivable from the customers.
7.	Remarks Column	–	Any other extra information will be recorded.

Difference between Sales Book and Sales Account

S. No.	Sales Book	Sales Account
1.	It is a part of Journal.	It is a part of Ledger.
2.	It is not divided into debit and Credit sides.	It is divided into debit and Credit sides.
3.	It record only credit sales of goods.	It record both cash and credit sales of goods.

Illustration:

From the transactions given below prepare the Sales Book of Ram for July 2013.

2013

July 5	Sold on credit to S.S. Traders		
	10 Chairs	@ ₹ 250}	Less 10%
	10 Tables	@ ₹ 850}	Discount
8	Sold to Raja for cash		
	15 Chairs	@ ₹ 250	
20	Sold to Mohan & Co.		
	5 Almirah	@ ₹ 2,200	
	10 Tables	@ ₹ 850	
	23 Sold on credit to Narayanan old computer for ₹ 5,000		
	28 Sold to Kumaran for cash		
	15 Chairs	@ ₹ 250	

Solution :

In the books of Ram
Sales Book

Date	Particulars	Outward Invoice No.	L.F.	Amount Details ₹	Amount Total ₹	Remarks
2013	S.S. Traders & Co. 10 Chairs @ ₹ 250 10 Tables @ ₹ 850 Less : 10% Discount Sold to S.S. Traders, Invoice No....... dated			2,500 8,500 11000 1100	9900	
	Mohan & Co. 5 Almirah @ ₹ 2,200 10 Tables @ ₹ 850 Sales as per Invoice No...... dated			11,000 8,500	19,500	
	Total				29,400	

Ledger Accounts

Dr. Sales Account Cr.

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F	Amount ₹
				2013 July 31	By Sundries as per sales book		29,400

Dr. S.S. Trader's Account Cr.

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 July 5	To Sales A/c		9,900				

Dr. Mohan & Co.'s Account Cr.

Date	Particulars	J.F.	Amount ₹	Date	Particulars	J.F	Amount ₹
2013 July 20	To Sales A/c		19,500				

Returns Books

Returns Books are those books in which the goods returned to the suppliers and goods returned by the customers are recorded. The reasons for the return of goods are

1. not according to the order placed.
2. not upto the samples which were already shown.
3. due to damage condition.
4. due to difference in the prices charged.
5. undue delay in the delivery of the goods.

Kinds of Returns Books

The following are the kinds of Returns Books:

1. Purchases Return or Returns outward book
2. Sales Return or Returns inward book

When the business concern returns a part of the goods purchased on credit, the returns fall under the category Purchases Return or Returns Outward.

When the business concern receives a part of the goods sold on credit, the returns fall under the category of Sales Return or Returns Inward.

Purchases Return Book

This book is used to record all returns of goods by the business to the suppliers. The entries in the Purchases Returns Book are usually made on the basis of debit note issued to the suppliers or credit note received from the suppliers. We call it a debit note because the party's (supplier) account is debited with the amount written in this note. The same note is termed as credit note from the receiving party's point of view because he will credit the account of the party from whom he has received the note together with goods.

Format

Purchases Return Book

Date	Particulars	Debit Note No.	L.F.	Amount		Remarks
				Details ₹	Total ₹	

Note : The reason for goods returned is recorded in Remarks column.

Illustration

Enter the following transactions in the purchases return book of Hari and post them into the ledger.

2013

Jan 5 Returned goods to Anand 5 chairs @ ₹ 200 each, not in accordance with order.

14 Returned goods to Chandran 4 chairs @ ₹ 200 each and 10 tables @ ₹ 350 each, due to inferior quality.

Solution :

In the books of Hari
Purchases Return Book

Date	Particulars	Debit Note No.	L.F.	Amount Details ₹	Amount Total ₹	Remarks
Jan 5	Anand 5 Chairs @ ₹ 200				1,000	
14	Chandran 4 Chairs @ ₹ 200 10 Tables @ ₹ 350			800 3500	4,300	
	Total				5,300	

Sales Return Book

This book is used to record all returns of goods to the business by the customers. The entries in the sales return book are usually on the basis of credit notes issued to the customers or debit notes issued by the customers.

Format

Date	Particulars	Credit Note No.	L.F.	Amount Details ₹	Amount Total ₹	Remarks

Illustration

Enter the following transactions in Returns Inward Book:

2013

April 6 Returned by Shankar 30 shirts each costing ₹ 150, due to inferior quality.

8 Amar Tailors returned 10 Baba suits, each costing ₹ 100, on account of being not in accordance with their order.

21 T.N. Stores returned 12 Salwar sets each costing ₹ 200, being not in accordance with order.

Solution:

Sales Return Book

Date	Particulars	Credit Note No.	L.F.	Details ₹	Amount ₹	Remarks
2013 April 6	Shankar 30 shirts @ ₹ 150			4,500		Due to inferior quality
8	Amar Tailors 10 Baba suits					Not in accordance

21	@ ₹ 100 T.N Stores 12 Salwar sets @ ₹ 200			1,000 2,400	7,900	with the order Not in accordance with order.
	Total				7,900	

Journal Proper

Journal proper is used for making the original record of such transactions for which no special journal has been kept in the business. The usual entries that are put through this journal are explained below.

1. Opening Entries

Opening entries are used at the beginning of the financial year to open the books by recording the assets, liabilities and capital appearing in the balance sheet of the previous year.

Example:

Mr. Ramnath commenced business with the following items, make the opening entries in journal proper as on 1st January 2013.

Cash	₹	30,000
Stock	₹	15,000
Furniture	₹	3,000
Sundry creditors	₹	10,000

Date	Particulars		L.F.	Debit ₹	Credit ₹
2013 Jan. 1	Cash A/c	Dr.		30,000	
	Stock A/c	Dr.		15,000	
	Furniture A/c	Dr.		3,000	
	To Sundry Creditors A/c				10,000
	To Capital A/c				38,000
	(Commencement of business with assets & liabilities)				

2. Closing Entries

Closing entries are recorded at the end of the accounting year for closing accounts relating to expenses and revenues. These accounts are closed by transferring the balances to the Trading, Profit and Loss Account.

Example: Salaries paid ₹ 15,000. Give the closing entry as on Dec. 31, 2013.

Date	Particulars		L.F.	Debit ₹	Credit ₹
2013 Dec.31	Profit & Loss A/c	Dr.		15,000	
	To Salaries A/c				
	(Closing entry for salaries paid)				15,000

3. Adjusting Entries

To arrive at a correct figure of profits and loss, certain accounts require some adjustments. Entries for making such adjustments are called as adjusting entries. These are needed at the time of preparing the final accounts.

Example: Provide depreciation on furniture ₹ 1,00,000 @ 10% per annum. Give adjustment entry as on Dec. 31, 2013.

Date	Particulars	L.F.	Debit ₹	Credit ₹
2013 Dec.31	Depreciation A/c Dr. To Furniture A/c (Depreciation charged on Furniture)		10,000	10,000

4. Transfer Entries

Transfer entries are passed in the journal proper for transferring an item entered in one account to another account.

Example: When the proprietor takes goods ₹ 5,000 for personal use. Give transfer entry on Dec. 31, 2013.

Date	Particulars	L.F.	Debit ₹	Credit ₹
2013 Dec.31	Drawings A/c Dr. To Purchases A/c (Goods withdrawn for personal use)		5,000	5,000

5. Rectifying Entries

Rectifying entries are passed for rectifying errors which might have been committed in the book of accounts.

Example: Purchase of furniture for ₹ 10,000 was debited to Purchases Account. Pass rectifying entry on Dec. 31, 2013.

Date	Particulars	L.F.	Debit ₹	Credit ₹
2013 Dec.31	Furniture A/c Dr. To Purchases A/c (Wrong debit to purchases account rectified)		10,000	10,000

6. Miscellaneous Entries or Entries of Casual Nature

These are entries of casual nature which do not occur so frequently. Such transactions include the following:

1. Credit purchases and credit sale of assets which cannot be recorded through purchases or sales book
2. Endorsement, renewal and dishonour of bill of exchange which cannot be recorded through bills book.
3. Other adjustments like interest on capital and loan, bad debts, reserves etc.

Chapter 8
Subsidiary Books-II
Cash Book

In every business house there are cash transactions as well as credit transactions. All credit transactions will become cash transactions when payments are made to creditors or cash received from debtors. Since, cash transactions will be numerous, it is better to keep a separate book to record only the cash transactions.

Features

A cash book is a special journal which is used to record all cash receipts and cash payments. The cash book is a book of original entry or prime entry since transactions are recorded for the first time from the source documents. The cash book is a ledger in the sense that it is designed in the form of a cash account and records cash receipts on the debit side and cash payments on the credit side. **Thus, the cash book is both a journal and a ledger**. **Cash Book will always show debit balance**, as cash payments can never exceed cash available. In short, cash book is a special journal which is used for recording all cash receipts and cash payments.

Advantages

1. **Saves time and labour:** When cash transactions are recorded in the journal a lot of time and labour will be involved. To avoid this all cash transactions are straight away recorded in the cash book which is in the form of a ledger.

2. **To know cash and bank balance:** It helps the proprietor to know the cash and bank balance at any point of time.

3. **Mistakes and frauds can be prevented:** Regular balancing of cash book reveals the balance of cash in hand. In case the cash book is maintained by business concern, it can avoid frauds. Discrepancies if any, can be identified and rectified.

4. **Effective cash management:** Cash book provides all information regarding total receipts and payments of the business concern at a particular period. So that, effective policy of cash management can be formulated.

Kinds of Cash Book

The various kinds of cash book from the point of view of uses may be as follow:

Kinds of cash book

- I Single column cash book
- II Double column cash book
  - (a) With discount and Cash columns
  - (b) With cash and Bank columns
- III Triple column cash book with discount, cash and bank columns
- IV Petty cash book

Single Column Cash Book

Single column cash book (simple cash book) has one amount column in each side. All cash receipts are recorded on the debit side and all cash payments on the credit side. In fact, this book is nothing but a Cash Account. Hence, there is no need to open cash account in the ledger. The format of a single column cash book is given below.

Format

Single Column Cash Book of …………

Debit Side   Credit Side

Date	Particulars	R.N.	L .F.	Amount (₹)	Date	Particulars	R.N.	L .F.	Amount (₹)

Illustration

Enter the following transactions in a single column cash book of Mr.Kumaran.

2013 Jan				
1	Started business with cash	...	₹	1,000
3	Purchased goods for cash	...	₹	500
4	Sold goods	...	₹	1,700
5	Cash received from Siva	...	₹	200
12	Paid Balan	...	₹	150
14	Bought furniture	...	₹	200
15	Purchased goods from Kala on credit	...	₹	2,000
20	Paid electric charges	...	₹	225
24	Paid salaries	...	₹	250
28	Received commission	...	₹	75

Solution:

Cash Book
of Mr. Kumaran

Date	Particulars	R. N.	L .F.	Amount ₹	Date	Particulars	V. N.	L .F.	Amount ₹
2013					2013				
Jan 1	To Capital A/c			1,000	Jan 3	By PurchasesA/c			500
4	To Sales A/c				12	,, Balan A/c			150

5	To Siva A/c			1,700	14	,, Furniture A/c			200
28	To Commission A/c			200	20	,, Electric charges A/c			225
				75	24	,, Salaries A/c			250
					31	,, Balance c/d			1,650
				2,975					2,975
2013 Feb 1	To Balance b/d			1,650					

Double Column Cash Book

Cash Book with Cash and Bank Columns

When bank transactions are more in number, it is advisable to open a cash book by providing a separate column on either side of the cash book to record the bank transactions therein.

In such case, it is not necessary to open a separate Bank Account in the Ledger because the two columns in the cash book serve the purpose of Cash Account and Bank Account respectively. It is a combination of Cash Account and Bank Account. The format of this cash book is given below.

Double Column Cash Book

(Cash book with Cash and Bank Columns)

Debit Side Credit Side

Date	Particulars	R. N.	L. F.	Cash ₹	Bank ₹	Date	Particulars	V. N.	L. F.	Cash ₹	Bank ₹

There are two amount columns on debit side one for cash receipts and the other for bank deposits (i.e., payment made into Bank Account). Similarly there are two amount columns on the credit side, one for payments in cash and the other for payments by cheques respectively.

Contra Entry

When an entry affects both cash and bank accounts it is called a contra entry. Contra in Latin means *opposite*. In contra entries both the debit and credit aspects of a transaction are recorded in the cash book itself.

Example: Cash paid into bank

Bank A/c Dr. x x x

To Cash A/c x x x

(Cash paid into bank)

This is a contra entry. As the cash book with cash and bank columns is a combined cash and bank account, both the aspects of the transaction will be entered in the same book. In the debit side 'To Cash A/c' will be entered in the particulars column and the amount will be entered in the bank column. In the credit side 'By Bank A/c' will be entered in the particulars column and the amount will be entered in the cash column.

Such contra entries are denoted by writing the letter 'C' in the L.F. column, on both sides of the cash book. They indicate that no posting in respect thereof is necessary in the ledger.

Example: Cash withdrawn from bank for office use.

Cash A/c	Dr.	x x x	
To Bank A/c			x x x

(Cash withdrawn for office use)

This is also a contra entry. In the debit side 'To Bank A/c' will be entered in the particulars column and the amount will be entered in the cash column. In the credit side 'By Cash A/c' will be entered in the particulars column and the amount will be entered in the bank column.

Such contra entries are denoted by writing the letter 'C' in the L.F. column, on both sides of the cash book. They indicate that no posting in respect thereof is necessary in the ledger.

Illustration

Enter the following transactions in the double column cash book of Mr. Rajesh and balance it.

2013

Aug.	1	Opening Balance: Cash in Hand ₹ 4,250
		Cash at Bank ₹ 13,750
	2	Paid to petty cashier ₹ 2,500
	2	Cash sales ₹ 1,750
	3	Paid to Arun by cheque ₹ 3,750
	3	Received a cheque from Mr.Ram Babu ₹ 4,500 paid into bank.
	5	Received cheque from Mr.Jayaraman ₹ 6,000 paid into bank
	8	Cash purchases ₹ 2,500
	8	Paid rent by cheque ₹ 2,500
	9	Cash withdrawn from bank for office use ₹ 2,500
	10	Cash sales ₹ 3,750
	14	Stationery purchased ₹ 1,000
	20	Cash sales ₹ 6750
	21	Paid into bank ₹ 10,000
	23	Withdrew cash for personal use ₹ 1,000
	25	Salaries paid by cheque ₹ 9000.

Solution:

Double Column Cash Book of Mr. Rajesh

(Cash book with Cash and Bank Column)

Date	Particulars	RN	L.F.	Cash	Bank	Date	Particulars	RN	L.F.	Cash	Bank
2013						2013					
1-Aug	To Balance B/d			4,250	13,750	2-Aug	By Petty Cash A/c			2,500	
2	,, Sales A/c			1,750		3	,, Arun's A/c				3,750
3	,, Ram Babu's A/c				4500	8	,, Purchase A/c			2,500	
5	,, Jayaramans A/c				6,000	8	,, Rent A/c				2,500
9	,, Bank A/c		C	2,500		9	,, Cash A/c		C		2,500
10	,, Sales A/c			3,750		14	,, Stationery A/c			1,000	
20	,, Sales A/c			6,750		21	,, Bank A/c		C	10,000	
21	,, Cash A/c		C		10,000	23	,, Drawings A/c				1,000
						25	,, Salary A/c				9,000
						31	,, Balance c/d			3,000	15,500
				19,000	34,250					19,000	34,250
1-Sep	To Balance b/d			3,000	15,500						

Points to be remembered while preparing cash book:

S.No.	Transaction	Debit/credit Side of Cash Book	The column in which the amount to be entered
1.	Cash/ M.O./P.O. – received	Debit	Cash
2.	Cash paid	Credit	Cash
3.	Discount allowed	Debit	Discount allowed
4.	Discount received	Credit	Discount received
5.	Cash deposited in the bank	Debit (C) Credit (C)	Bank Cash
6.	Cash withdrawn for office use	Debit (C) Credit (C)	Cash Bank
7.	Cheque received	Debit	Cash
8.	Cheque deposited into bank	Debit (C) Credit (C)	Bank Cash
9.	Cheque received and deposited into bank for collection immediately	Debit	Bank
10.	Cheque issued	Credit	Bank
11.	Customer directly paid into bank	Debit	Bank
12.	Cheque deposited and dishonoured	Credit	Bank
13.	Cheque issued and dishonoured	Debit	Bank

Triple Column Cash Book

Large business concerns receive and make payments in cash and by cheques. Where cash discount is a regular feature, a Triple Column Cash Book is more advantageous. This cash book has three amount columns (cash, bank and discount) on each side. All cash receipts, deposits into bank and discount allowed are recorded on debit side and all cash payments, withdrawals from bank and discount received are recorded on credit side.

Illustration

Compile three column cash book of Mr. Sundar from the following transactions:

2013

Aug 1 Sundar started business with cash ₹ 2,00,000

2 Deposited into Bank ₹ 50,000.

4 Cash purchases ₹ 5,000.

5 Purchases by cheque ₹ 6,000.

6 Goods sold to Nathan on credit ₹ 5,000.

8 Received cheque from Mano ₹ 490, Discount allowed ₹ 10.

10 Paid carriage ₹ 1,000.

12 Withdrew from Bank for office use ₹ 10,000.

15 Paid to Sundari ₹ 4,960, Discount allowed by her ₹ 40.

20 Received a cheque for ₹ 4950 from Nathan in full settlement of his account, which is deposited into Bank.

Solution:

Triple Column Cash Book of Mr. Sundar

Date	Particulars	R.N.	L.F.	Dis. Allowed	Cash	Bank	Date	Particulars	R.N.	L.F.	Dis. Allowed	Cash	Bank
2013							2013						
1 Aug	To Capital A/c				2,00,000		2 Aug	By Bank A/c		C		50,000	
2 Aug	,, Cash A/c		C			50,000	4	,,Purchases A/c				5,000	
8	,, Mano's A/c			10	490		5	,,Purchases A/c					6,000
12	,, Bank A/c		C		10,000		10	,, Carriage A/c				1,000	
20	,, Nathan's A/c			50		4,900	12	,, Cash A/c		C			10,000
							15	,, Sundari's A/c			40	4,960	
							31	,, Balance c/d				1,49,530	38,900
				60	2,10,490	54,900					40	2,10,490	54,900
1 Sep	To Balance b/d				1,49,530	38,900							

Illustration

Enter the following transactions in three column cash book of Mrs. Anu Radha.

2013

Sep 1 Cash in hand ₹ 50,000

Bank balance ₹ 15,000

2 Sold goods to Udayakumar for ₹ 15,000, cash discount allowed 1% and received cash for the balance.

3 Tax paid ₹ 1,000.

7 Bought goods from Munuswamy for ₹ 2,400, cash discount received 2% paid cheque for the balance.

9 Received repayment of loan from Elangovan ₹ 10,000.

12 Paid into Bank ₹ 5,000.

14 Paid ₹ 1,400 to Aravind & Co., half by cash and half by cheque.

16 Dividend collected by the Bank as per pass book ₹ 2,000.

18 Sold goods for cash and deposited into the bank on the same day ₹ 5,000.

20 Sent to Bharathi by money order ₹ 460, the money order commission being ₹ 20.

Solution:

Date	Particulars	R.N.	L.F.	Dis. Allowed	Cash	Bank	Date	Particulars	R.N.	L.F.	Dis. Allowed	Cash	Bank
1-Sep	To Balance b/d				50,000	15,000	3-Sep	By Tax A/c				1,000	
2	,, Sales A/c			150	14,850		7	,, Purchases A/c			48		2,352
9	,, Elangovan's Loan				10,000		12	,, Bank A/c		C		5,000	
12	,, Cash A/c		C			5,000	14	,, Arawind & Co. A/c				700	700
16	,, Dividend A/c					2,000	20	,, Bharathi A/c				460	
18	,, Sales A/c					5,000	20	,, Money Order Commission A/c				20	
							30	,, Balance A/c				67,670	23,948
				150	74,850	27,000					48	74,850	27,000
1-Oct	To Balance b/d				67,670	23,948							

Chapter 9

Subsidiary Books-III
Petty Cash Book

In every business, of whatever size, there are many small cash payments such as conveyance, carriage, postage, telegram, etc. These expenses are generally repetitive in nature. If all these small payments are recorded in the cash book, it will be difficult for the cashier to maintain the records all by himself. In order to make the task of the cashier easy, these small and recurring expenses are recorded in a separate cash book called "**Petty Cash Book**" and the person who maintains the petty cash is called the "**Petty Cashier**".

Petty means 'small'. The petty cash book is a book where small recurring payments like carriage, cartage, postage and telegram, printing and stationery etc., are recorded by the petty cashier, a person other than the main cashier.

Imprest System

Imprest means 'money advanced on loan'. Under this system the amount required to meet out various petty expenses is estimated and given to the petty cashier at the beginning of the specified period, usually a month. All the payments are supported by vouchers. At the end of the given period or earlier, when the petty cashier has spent the petty cash amount, he closes the petty cash book for the period and balances it. Then he submits the accounts to the cashier. He verifies the petty cash book with the vouchers. After satisfying himself as to the correctness and genuiness of the payments an amount equal to the cash spent is given to the petty cashier. This amount together with the unspent amount will bring up the cash in hand to the amount with which he originally started i.e., **the imprest amount**. Thus the system of reimbursing the amount spent by the petty cashier at fixed period, is known as the **imprest system of petty cash**.

For example, On June 1, 2013, ₹ 1,000 was given to the petty cashier. He had spent ₹ 940 during the month. He will be paid ₹ 940 on 30th June by the cashier so that he may again have ₹ 1,000 for the next month i.e., July.

Analytical Petty Cash Book

As in the case of any other cash book, petty cash book also has the debit side and the credit side. The debit side is smaller and has very infrequent entries because cash receipt by the petty cashier is mainly from the cashier at the beginning or close of a specified period. The credit side is bigger and thus has many columns. For each important petty expenses there is a separate column, and therefore columnar cash book is another name for this petty cash book. These analytical columns helps to know the actual amount spent on each and every type of petty expenses for the specified period. Each petty payment is first entered in the total payments column, and then recorded in the respective analytical column, so that:

1. The total amount spent on each expense for a particular period can be easily ascertained by adding up the respective column.
2. Only the periodical total of each column is posted to the ledger.
3. The total petty payment for any period can be easily ascertained from the total payments column.

The analytical petty cash book may be designed according to the requirements of the business.

Format

The format is given in the next page.

Explanation of columns in the analytical petty cash book

1. *Receipts:* This is the first column of the petty cash book. Amount received by the petty cashier for meeting petty expenses and the opening balance of petty cash will be recorded in this column.

2. *C.B.F.N:* This refers to Cash Book Folio Number. In this column we write the page number of the cash book where cash paid by the cashier is recorded.

3. *Date:* In this column, the date of receipt / payment of cash is recorded.

4. *Particulars:* This column records the details of the receipts / payments. Cash received in the beginning is shown as 'To cash' and all the petty expenses are shown as 'By expenses' (name of the expense).

5. *V.N.:* The serial number of the voucher (cash payment) is written in this column.

6. *Total Payments:* This column records the amount of every expense. At the end of the week or month expenses are totalled and afterwards balanced. The total expenses of the week or the month is compared with the total of the receipts column and the balance is obtained.

7. *Postage and Telegrams:* This column records postal expenses like post card, envelope, inland letter, postage stamps, registered letter, parcel, telegrams and telephone charges.

8. *Printing & Stationery:* It includes expenses incurred for purchasing materials such as paper, ink, pencil, eraser, carbon paper and other items of stationery.

9. *Cartage / Freight / Carriage:* In this column carriage inward of goods is recorded. It includes cartage paid to coolie, tempo charges etc.

10. *Travelling Expenses / Conveyance:* In this column fare for hiring auto rickshaw, bus, train, taxi etc., are recorded.

11. *Office Expenses & Repairs:* Minor repairing charges and petty office expenses like cleaning are included in this column.

12. *Sundry Expenses / Sundries:* Generally columns of important petty expenses of the business according to the nature and type of business are prepared. In addition to these important expenses, there may be certain expenses, which may not have specific columns for them. Expenses like refreshment, charity, tips, amount paid to scavangers etc., are recorded in this column.

13. *L.F.:* This refers to the page number of the ledger where the respective account is recorded.

14. *Personal Accounts:* Small amount of money paid to individuals are entered in this column.

Analytical Petty Cash Bank……………..

Receipts		C.B.F.N	Date	Particulars	V.N.	Total Payments		Postage and Telegrams		Printing and Stationery		Carriage		Travelling Expenses		Sundries		LF	Personal Accounts	
₹	P		2014			₹	P	₹	P	₹	P	₹	P	₹	P	₹	P		₹	P

Balancing Petty Cash Book

At the end of the period i.e., week or month the total payments column and individual expenses columns are totalled. It should be ascertained that the total of petty expenses column must be equal to the total of payments column. The total payments column is compared with the total of receipts column and balance is obtained. The closing balance is shown as 'By Balance c/d'. The closing balance is carried forward to the beginning of the next week or month. It is shown as 'To Balance b/d'.

Posting of Entries in the Petty Cash Account

I. When petty cash is advanced at the beginning

A separate petty cash account is opened in the ledger. When advance is received by the petty cashier petty cash account will be debited and cash account will be credited.

II. When individual expenses column are periodically totalled

The total of various petty expenses are debited and the petty cash account is credited with the total of the payments made.

The petty cash account will show the balance of cash. This balance will be shown in the balance sheet as part of cash balance.

Illustration: Record the following transactions in the analytical petty cash book of Mr.Manoharan. Balance the book on 6th May, 2013. Give Journal entries and post the balances to concerned ledger accounts.

2013
May1. Received for petty cash payment ₹ 1,500
2. Paid taxi hire ₹ 250
3. Bought stamps ₹ 75
4. Paid for carriage ₹ 120
4. Paid for Telegrams ₹ 75
4. Paid for auto ₹ 125
5. Paid for carriage ₹ 300
6. Bought revenue stamps ₹ 50

Solution:

Analytical Petty Cash Bank of Mr. Manoharan

Receipts		C.B.F.N	Date	Particulars	V.N.	Total Payments		Postage and Telegrams		Printing and Stationery		Carriage		Travelling Expenses		Repair		Sundries		L.F	Personal Accounts	
₹	P.		2013 May			₹	P.	₹	P.	₹	P.	₹	P.	₹	P	₹	P.	₹	P.		₹	P.
1500	00		1	To Cash A/c																		
			2	By Taxi Hire	-	250	00	-	-	-	-	-	-	250	00	-	-	-	-	-	-	-
			3	By Stamps	-	75	00	75	00	-	-	-	-	-	-	-	-	-	-	-	-	-
			4	By Carriage	-	120	00	-	-	-	-	120	00	-	-	-	-	-	-	-	-	-
			4	By Telegrams	-	75	00	75	00	-	-	-	-	-	-	-	-	-	-	-	-	-
			4	By Auto fare	-	125	00	-	-	-	-	-	-	125	00	-	-	-	-	-	-	-
			5	By Carriage	-	300	00	-	-	-	-	300	00	-	-	-	-	-	-	-	-	-
			6	By Revenue Stamps	-	50	00	50	00	-	-	-	-	-	-	-	-	-	-	-	-	-
						995	00	200	00	-	-	420	00	375	00							
			6	By balance c/d		505	00															
1500	00					1500	00															
505	00		7	To Balance b/d																		
995	00		7	To Cash A/c																		

Chapter 10

Bank Reconciliation Statement

It is a statement prepared mainly to reconcile the difference between the Bank Balance shown by the Cash Book and the Pass book.

Cash Book

Cash book with cash and bank columns have been explained earlier. On the debit side of the cash book, the bank column represents:

1. Cheques deposited into bank for collection.
2. Cash paid into bank and
3. Some entries that are made only after receiving the information from the bank viz.
   (i) Amounts collected by the bank on our behalf as per the standing instructions, for example, Interest collected on investment.
   (ii) Interest given by the banker for the balance kept by us in our bank account.
   (iii) The amount paid by our customers directly into our bank account.

On the other hand, on the credit side of the cash book, represents:

1. Cheques issued for payment.
2. Cash withdrawn from bank for office use and personal use.
3. In addition, some entries are made after receiving information from the bank viz.
   (i) Amounts paid by the bank on our behalf as per the standing instructions, for example, payment of insurance premium.
   (ii) Interest charged by the bank for the amount drawn over and above the actual balance kept in the bank account.
   (iii) Bank charges payable for the agency and utility services rendered by the bank.

Bank Pass Book

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

Date	Particulars	Dr. Withdrawals ₹	Cr. Deposits ₹	Balance Dr / Cr ₹	Initials

In the date column, the dates of the transactions are recorded. In the particulars column withdrawals and deposits are recorded. The balance after each transaction is recorded in the next column and the bank official signs in the last column.

Following the principles of Double Entry, banker credits the account of the customer for all the amounts received from the customer and on his behalf. Similarly the banker debits the account of the customer for all withdrawals and amounts paid to others on behalf of the customers. The main point to be remembered is that entries are made only after cash is received or paid, except in the case of interest and bank charges. Interest and bank charges are mere book adjustments and in these, there is neither receipt of cash nor payment of cash.

Difference between Cash book and Pass Book:

S.No	Basis of Distinction	Cash Book (Bank Column)	Pass Book
1.	Maintained by	Cashier	Banker
2.	Deposits of Cash	Entered on the debit side of the cash book.	Entered on the credit column of the pass book.
3.	Withdrawals of Cash	Entered on the credit side of the cash book.	Entered on the debit column of the pass book.
4.	Cheques deposited for collection	Entered on the debit side of the cash book on the date of depositing the cheques into the bank.	Entered in the pass book only on the date of the realisation of the cheque.
5.	Cheques issued	Entered on the credit side of the cash book on the date of issuing the cheque to the creditors.	Entered on the debit column of the pass book only on the date on which they are presented and paid.
6.	Collections and payments as per customers standing instructions	Entered in the Cash book after seeing the pass book.	Entered in the Pass book first.
7.	Signature	It is not signed by the cashier	It is signed by the Bank official after each transaction.
8.	Balancing	It is balanced at the end of a specified period.	It is balanced after each transaction

Bank Reconciliation Statement

The balance of the bank column in the double or triple column cash book represents the customers cash balance at bank. It should be the same as shown by his bank pass book on any particular day. For every entry made in the cash book if there is a corresponding entry in the pass book (maintained by the banker) or vice versa, the bank balance will be the same in both the books.

However, it must be noted that the cash book and the pass book are maintained by two different parties and hence it is not certain that entry in one book will always have a corresponding entry in the other. Normally entries in the cash book should tally (agree) with those in the pass book and the balances shown by both the books should be the same. But in practice, the balances generally differ. In case of disagreement in the balance of the cash book and the pass book, the need for preparing Bank Reconciliation Statement arises.

Definition

Bank reconciliation statement is a list in which the various items that cause a difference between bank balance as per cash book and pass book on any given date are indicated'.

Need and Importance

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

(i) The errors that might have taken place in the cash book in connection with bank transactions can be easily found.

(ii) Regular preparation of bank reconciliation statement prevents frauds.

(iii) It indirectly imposes moral check on the accounting staff.

(iv) By the preparation of bank reconciliation statement, uncredited cheque can be detected and steps can be taken for their collection.

Causes of disagreement between the balance shown by the cash book and the balance shown by the pass book

1. Cheques paid into bank but not yet collected

The cheques paid into bank for collection but not credited into the account of the customer, because the cheque is

(i) Not collected and credited till that date.

(ii) Collected but the bank staff has forgotten to make entry.

(iii) Collected but credited to wrong account.

(iv) Dishonoured.

(v) Collected for No.I account but credited to No.II account of the same customer.

As soon as the cheques are sent to the bank, entries are made in the debit side of the cash book (bank column). But, usually bank credits the customers account only when they have received payment from the bank concerned, in other words, when the cheques have been collected. Hence, there will be a time gap between the depositing of the cheques and the collection by the bank.

For example, Bharat Company Limited deposited a cheque on March 28, 2013 for a sum of ₹ 3,000. The cheque was collected on April 4, 2013. In case the bank sends a statement of account upto March 31, 2013, there will be a difference of ₹ 3,000 between the balance shown by the cash book and the pass book.

2. Cheques issued but not yet presented for payment

The cheques issued but not debited customers account may be because the cheque is

(a) Not cashed till date.

(b) Not presented till date.

(c) Presented but dishonoured for some reasons or other.

(d) Lost by the party to whom the cheque was issued.

(e) Cashed out of No. I account but wrongly debited to No. II account of the same customer.

In all of the above cases, the entry in the cash book is made immediately on the issue of cheque but naturally the entry will be made by bank only when the cheque is presented for payment. Thus there will be a gap of some days between the entry for issue of cheque in the cash book and the entry for payment made in the pass book.

For example, Bharat Company Limited issued a cheque in favour of Mr. Krishna on March 28, 2013 for a sum of ₹ 5,000. The cheque is presented for payment at the bank on April 4, 2013. In case, bank sends a statement of account upto March 31, 2013, there will be a difference of ₹ 5,000 between the balance as shown by the cash book and the balance as shown by the pass book.

3. Amount credited by the banker in the pass book without the immediate knowledge of the customer

The following are some of the examples for the above statement:

(a) The bank might have collected rent, dividend, bills of exchange, interest etc., due for the customer as per standing instructions.

(b) Some debtors might have directly paid into bank.

(c) Bank credits interest on the credit balance of the customer's account.

(d) The banker has wrongly credited this account instead of some other account.

In all the above cases, the entry will be first entered in the pass book. The customer will know this only after he verifies the entries in the pass book. So there may be a time gap of some days before the customer includes entries made in the pass book.

For example, the bank has credited Bharat Company Limited's account for interest amounting to ₹ 500 on March 31, 2013. The bank prepares and sends a statement of account on March 31, 2013. If the customer receives the statement of account on April 4, 2013, there will be a difference of ₹ 500 between the balance shown by the cash book and the balance shown by the pass book.

4. Amounts debited by the banker in the pass book without the immediate knowledge of the customer

The following are some of the examples for this.

(i) The banker has recorded bank charges, interest on overdraft etc.

(ii) The banker has paid insurance premium, subscription for periodicals, etc. on behalf of the customer as per the standing instructions.

(iii) The banker has wrongly debited this account instead of some other account.

(iv) The banker has paid the bills payable of the customer as per standing instructions.

(v) Dishonour of a cheque deposited and discounted bills receivable.

In all the above cases, the entry will be first entered in the pass book of the customer. And the customer will know only after he verifies the entries in the pass book or statement of account. So there may be a time gap of some days before the customer includes the entries made in the pass book.

For example, the bank has debited Bharat Company Limited's account for its charges amounting to ₹ 250 on March 31, 2013. In case, the bank sends a statement of account upto March 31, 2013 there will be a difference of ₹ 250 between the balance as per the cash book and the balance as per the pass book.

For example, A cheque for ₹ 5,000 dishonoured on March 28, 2013. In case, the bank sends a statement of account upto March 31, 2013 there will be a difference of ₹ 5,000 between the balance as shown by the cash book and the balance as shown by the pass book.

After tracing the various items of differences, a Bank reconciliation statement is prepared by starting with the balance shown by any of the two books. But in actual practice, a Bank reconciliation statement is prepared by the customer starting with the balance as per cash book and will ensure that the balance as per pass book is arrived at.

Bank Overdraft

Bank overdraft is an amount drawn over and above the actual balance kept in the bank account. This facility is available only to the current account holders. Interest will be charged for the amount overdrawn i.e., overdraft. The Cash book will show a credit balance i.e., unfavourable balance. The pass book will show a debit balance.

A summary of the transactions and the reconciliation procedure is given in the table below.

Procedure for Preparing Bank Reconciliation Statement

S.No	Transactions	Entries by customer in the cash book (Bank column)	Entries by Bank in the pass book	Effect	Procedure to ascertain the balance as per pass book from cash book	
					Favourable balance	Unfavou -rable balance (over- -draft)
1.	When cash is deposited	Customer enters in the debit side	Bank enters in the credit column	Cash book = Pass book	–	–
2.	When cash is withdrawn	Customer enters in the credit side	Bank enters in debit column	Cash book = Pass book	–	–
3.	Issue of cheque	Customer enters in the credit side immediately	Bank enters in the debit column only on the date when presented for payment.	Cash book <Pass book	Add	Less
4.	Cheque received and entered in cash book and sent to bank for collection	Customer debits cash book	Only after collection, the amount will be entered in the credit column of the pass book because the process takes some time	Cash book >Pass book	Less	Add

5.	Bank charges for services rendered by bank	No entry can be found in cash book till the pass book is verified.	Entered in the debit column of the passbook immediately.	Cash book > Pass book	Less	Add
6.	Interest, dividend etc collected by bank on behalf of customer	No entry can be found in cash book till the pass book is verified.	These are entered in the credit column of the passbook immediately after receiving the amount	Cash book < Pass book	Add	Less
7.	Interest allowed by bank	No entry is made unless pass book is verified.	Entered in the credit column of the pass book first.	Cash book < Pass book	Add	Less
8.	Amount directly remitted into bank	No entry is found in cash book till the pass book is verified.	Entered in the credit column of the pass book on the same day of receipt.	Cash book < Pass book	Add	Less
9.	Subscription, premium etc paid by the banker as per the standing instructions of the customer	Entry is made only after the pass book is verified.	Entered in the debit column of the pass book on the same day of payment	Cash book > Pass book	Less	Add
10.	Dishonour of bills receivable or cheques paid into bank	No entry in the cash book till the customer is intimated by the banker	Entered in the debit column of the pass book immediately	Cash book > Pass book	Less	Add
11.	Dishonour of bills payable or cheques issued	No entry in the cash book till the customer is intimated by the banker	Entered in the credit column of the pass book immediately	Cash book < Pass book	Add	Less
12.	Wrong credit in the pass book	No entry is found in cash book unless it is verified with the pass book.	Entered (wrongly) in the credit column in the pass book	Cash book < Pass book	Add	Less
13.	Wrong debit in the pass book	No entry is found in cash book unless it is verified.	Entered (wrongly) in the debit column in the pass book	Cash book > Pass book	Less	Add

Format

The format of Bank Reconciliation Statement when bank balance as per cash book is taken as the starting point.

Bank Reconciliation Statement as on ………………….

	Particulars	Amount ₹	Amount ₹
A	Balance as per Cash Book		* *
B	Cheques issued but not presented for payment	* *	
	Interest credited by bank but not recorded in cash book	* *	
	Debtors directly paid into bank but not recorded in cash book	* *	
	Wrong credit by banker	* *	
	Collections by banker as per customer standing instructions	* *	
C	Total (B)		
D	(Total A + B)		
	Cheques deposited but not credited by the bank	* *	**
	Dishonoured cheques appeared in the pass book but not entered in the cash book	* *	* *
	Bank charges as per pass book	* *	
	Wrong debit by banker	* *	
E	Payments as per standing instructions	* *	
	Total (D)		* *
	Balance as per pass book (C- D)		* *

Points to be noted:

To work out the problems on Bank Reconciliation Statement, the following points are to be remembered.

(i) The heading is given as "Bank Reconciliation Statement as on ____________"

(ii) All items to be added are grouped together and shown in the inner column and the total is taken to the outer column for the purpose of addition (B).

(iii) All items to be deducted are grouped together in the inner column and the total can be shown in the outer column for deduction.(D).

(iv) Favourable balance means the cash book will have a debit balance and the passbook will have a credit balance.

(v) Bank overdraft or unfavourable balance means cash book will have a credit balance and passbook will have debit balance.

For easy reference the table given below will be useful.

Book	Favourable Balance	Unfavourable Balance (overdraft)
Cash	Debit	Credit
Pass	Credit	Debit

Illustration: When balance as per cash book is favourable.

From the following details, make out a bank reconciliation statement for M/s. Elavarasan & Company as on December 31, 2013 to find out the balance as per pass book.

		₹
1.	Cheques deposited but not yet collected by the bank	1,500
2.	Cheque issued to Mr.Raju has not yet been presented for payment	2,500
3.	Bank charges debited in the pass book	200
4.	Interest allowed by the bank	100
5.	Insurance premium directly paid by the bank as per standing instructions	500
6.	Balance as per cash book	200

	Particulars	Amount ₹	Amount ₹
A	Balance as per Cash Book		200
B	Cheques issued to Mr.Raju but not presented for payment	2,500	
	Interest allowed by bank but not recorded in cash book	100	2,600
			2,800
C	Less: Cheques deposited but not credited by the bank	1,500	
D	Bank has paid insurance premium as per standing instructions	500	
	Bank charges as per pass book	200	2,200
	Balance as per Pass Book		600

Illustration: When balance as per pass book (favourable) is given

Mr. Jame's pass book showed a balance of ₹ 25,000 on June 30, 2013. His cash book shows a different balance. On examination, it is found that:

1. No record has been made in the cash book for a dishonour of a cheque for ₹ 250
2. Cheques paid into bank amounting to ₹ 3,500 were paid into the bank on June 28, 2013and the same had not been entered in the pass book.
3. Bank charges of ₹ 300 have not been entered in the cash book.
4. Cheques amounting to ₹ 9,000 issued to Ms. Devi has not been presented for payment still.
5. Mr. Balu who owed ₹ 3,000 has directly paid the sum into the bank account.

You are required to prepare a Bank reconciliation statement and ascertain the balance as per cash book.

Solution

Bank Reconciliation Statement as on June 30, 2013

Particulars	Amount ₹	Amount ₹
Balance as per Pass book		25,000
Add: Dishonour of cheque not recorded in cash book	250	
Cheque deposited but not collected by the bank	3,500	
Bank charges not entered in Cash book	300	
		4,050
Less: Cheques issued but not presented for payment	9,000	29,050
Amount directly paid by Mr.Balu into the bank	3,000	
		12,000
		17,050
Balance as per cash book		

Illustration: When overdraft as per cash book is given

Prepare a Bank Reconciliation Statement as at June 30, 2013 for M/s.Jothi Sales Private Limited from the information given below

		₹
1.	Bank overdraft as per cash book	1,10,450
2.	Cheques issued on June 20, 2003 but not yet presented for payment	15,000
3.	Cheques deposited but not yet credited by bank	22,750
4.	Bills receivable directly collected by bank	47,200
5.	Interest on overdraft debited by bank	12,115
6.	Amount wrongly debited by bank	2,400

Solution

Bank Reconciliation Statement as on June 30, 2013

Particulars	Amount ₹	Amount ₹
Overdraft balance as per cash book		
Add: Cheques deposited but not yet credited		1,10,450
Interest on overdraft debited by bank	22,750	
Wrong debit by bank	12,115	
	2,400	
		37,265
		1,47,715
Less: Cheques issued but not presented		
for payment	15,000	
Bills receivable collected by bank	47,200	
Overdraft balance as per		62,200
bank pass book		85,515

Illustration: Given below are the entries in the bank column of the cash book and the pass book. Prepare a Bank Reconciliation Statement of Mr.Sekar as on August 31, 2013.

Dr. Cash Book (Bank Columns) Cr.

Date	Particulars	Amount	Date	Particulars	Amount
2013			2013		
Aug 1	To Balance b/d	20,525	Aug 8	By Kokila A/c	12,000
18	To Shanker A/c	6,943	26	By Geetha A/c	9,740
19	To Sales A/c (Rajan)	450	28	By Latha A/c	11,780
20	To Commission A/c (Babu)		30	By Salaries A/c (Amala)	720
20	To Nirmala A/c		31	By Balance c/d	1,688
	To Balance b/d	200			
		7,810			
		35,928			35,928
Sept 1		1,688			

Pass Book

Date	Particulars	Dr. Withdrawals ₹	Cr. Deposits ₹	Balance Dr./Cr. ₹	Initials
1.8.13	By balance b/d			20,525 Cr	
9.8.13	To Kokila			8,525 Cr	
19.8.13	By Shankar	12,000		15,468 Cr	
25.8.13	By Rajan		6,943	15,918 Cr	
26.8.13	To Geetha		450	6,178 Cr	

27.8.13	By Babu	9,740		6,378 Cr	
28.8.13	To Amala		200	5,658 Cr	
30.8.13	By B/R	720			
	By Interest		20,000		
	By Interest on Investment		25		
31.8.13	To B/P	4,000		27,503 Cr	
			1,820		
				23,503 Cr	

Solution:

In the above problem, an extract of the cash book (bank column) and the pass book of Mr.Sekar is given. The items given on the debit side of the cash book should match with the items given on the credit column of the pass book and vice versa. The items, which do not match, cause the difference between both the balances.

Bank Reconciliation Statement as on August 31, 2013

Particulars	Amount ₹	Amount ₹
Balance as per cash book		1,688
Bills receivable collected, not entered in cash book		
Interest collected, not entered in cash book	20,000	
	25	
Interest on investment collected, not entered in cash book	1,820	
Cheques issued but not collected – Latha	11,780	
Less: Cheques paid into bank, bu not collected – Nirmala		33,625
		35,313
Bills payable paid, not entered in cash book	7,810	
Balance as per pass book	4,000	
		11,810
		23,503

Chapter 11

Trial Balance and Rectification of Errors

In the previous chapters, you have learnt how to record and classify the transactions in the various accounts along with balancing thereof. The next step in the accounting process is to prepare a statement to check the arithmetical accuracy of the transactions recorded so for. This statement is called '**Trial Balance**'.

Trial balance is a statement which shows debit balances and credit balances of all accounts in the ledger. Since, every debit should have a corresponding credit as per the rules of double entry system, the total of the debit balances and credit balances should tally (agree). In case, there is a difference, one has to check the correctness of the balances brought forward from the respective accounts. Trial balance can be prepared in any date provided accounts are balanced.

Definition

"**Trial balance** is a statement, prepared with the debit and credit balances of ledger accounts to test the arithmetical accuracy of the books". Thus, Trial Balance may be defined as a statement which contains balances of all ledger accounts on a particular date.

Objectives

The objectives of preparing a trial balance are:

1. **To check the arithmetical accuracy:** Arithmetical accuracy in ledger posting means writing correct amount, in the correct account and on its correct side while posting transactions from various original books of accounts, such as Cash Book, Purchases Book, Sales Book, etc. It also means not only the correct balance of ledger account but also the totals of the special purpose Books.

2. **To locate the errors:** If total of two columns of the trial balance agrees it is a proof of arithmetical accuracy in the ledger posting. However, if the totals of the two columns do not tally it indicates that there is some mistake in the ledger accounts. This prompts the accountant to find out the errors.

3. **To facilitate the preparation of final accounts:** The ultimate objective of the accounting is to prepare financial statements i.e. Trading and Profit and Loss Account, and Balance sheet of a business enterprise at the end of an accounting year. These statements contain balances of various ledger accounts. As Trial Balance contains balances of all ledger accounts, in financial statements the balances of ledger accounts are carried from the Trial balance for proper analysis.

Advantages

The advantages of the trial balance are

1. It helps to ascertain the arithmetical accuracy of the book-keeping work done during the period.
2. It supplies in one place ready reference of all the balances of the ledger accounts.
3. If any error is found out by preparing a trial balance, the same can be rectified before preparing final accounts.
4. It is the basis on which final accounts are prepared.

Methods

A trial balance can be prepared in the following methods.

1. **The Total Method:** In this method the total of both sides of every account in the ledger is written against the name of the respective account without balancing them in the form of debit and credit balances respectively.

2. **The Balance Method:** In this Balance method, the balance of each account (which may be debit balance or credit balance) is extracted and written against each account; we write debit balance in the debit column and credit balance in the credit column.

The balance method is more widely used, as it supplies ready figures for preparing the final accounts.

Format

Trial Balance consists of a debit column with all debit balances of accounts and credit column with all credit balances of accounts. The totals of these columns if tally it is presumed that ledger has been maintained correctly. However, Trial Balance proves only the arithmetical accuracy of posting in the ledger.

Trial Balance of ABC Ltd. as on.................

Sl.No	Name of Account	L.F	Debit ₹	Credit ₹

Points to be noted:

(i) Date on which trial balance is prepared should be mentioned at the top.

(ii) Name of Account column contains the list of all ledger accounts.

(iii) Ledger folio of the respective account is entered in the next column.

(iv) In the debit column, debit balance of the respective account is entered.

(v) Credit balance of the respective account is written in the credit column.

(vi) The last two columns are totalled at the end.

Sundry Debtors and Sundry Creditors

In the ledger there are many personal accounts, some of them may show debit balances, some others may show credit balances. If all the names are to be written in the trial balance it will be unduly long. Therefore, a list of names with the debit balances is prepared. This list is known as '**Sundry Debtors**' (Sundry means 'many'). Similarly, a list of names with the credit balances is prepared. This list is known as '**Sundry Creditors**'.

Illustration

The following balances were extracted from the ledger of Rahul on 31st March, 2013. You are requested to prepare a trial balance as on that date in the proper form.

Plant & Machinery	34,300	Travelling Expenses	2,630
Commission Paid	1,880	Carriage Inward	240
Stock on 1.4.2012	11,100	Sundry Creditors	14,260
Repairs	1670	Capital, 1.4.2012	62,500

Sundry Expenses	460	Drawings	3,500
Returns Inward	1,000	Cash at Bank	1,090
Discount Allowed	1,150	Returns Outward	400
Rent and Rates	3,220	Investments	6,000
Sales	1,73,500	Sundry Debtors	1,430
Salary	36,320	Purchase	1,44,670

Solution:

Trial Balance of Rahul as on 31st March, 2013

S. No.	Name of the Account	L.F.	Dr. ₹	Cr. ₹	Nature of Balance (Why Dr. or Cr.)
1.	Salaries		36,320	–	Nominal A/c-expense
2.	Sales		–	1,73,500	Real A/c – goods
3.	Plant and Machinery		34,300	–	Real A/c – asset
4.	Commission Paid		1,880	–	Nominal A/c expense
5.	Stock on 1.4.2012		11,100	–	Real A/c – goods
6.	Repairs		1,670	–	Nominal A/c-expense
7.	Sundry Expenses		460	–	Nominal A/c-expense
8.	Returns Inward		1,000	–	Real A/c – goods
9.	Discount Allowed		1,150	–	Nominal A/c – loss
10.	Rent & Rates		3,220	–	Nominal A/c-expense
11.	Purchases		1,44,670	–	Real A/c – goods
12.	Sundry Debtors		1,430	–	Personal A/c – customers
13.	Travelling Expenses		2,630	–	Nominal A/c-expense
14.	Carriage Inward		240	–	Nominal A/c-expense
15.	Sundry Creditors		–	14,260	Personal A/c – suppliers
16.	Capital 1.4.2012		–	62,500	Personal A/c – owner
17.	Drawings		3,500	–	Personal A/c – owner
18.	Cash at Bank		1,090	–	Real A/c – asset
19.	Returns Outward		–	400	Real A/c – goods
20.	Investments		6,000	–	Real A/c. – asset
	TOTAL		2,50,660	2,50,660	

Note: The last column given in the solution does not appear in practice. It is included here to illustrate the following generalised rules, that

(i) a debit balance is either an asset or loss or expense; and

(ii) a credit balance is either a liability or income or gain.

Limitations

Though the trial balance helps to ensure the arithmetical accuracy of the books of accounts, it is possible only when the accountant has not committed any error. As all the errors made are not disclosed by the trial balance, it would not be regarded as a conclusive proof of correctness of the books of accounts maintained.

Errors in Accounting

The trial balance is prepared to check the arithmetical accuracy of accounts. If the trial balance does not tally, it implies that there are arithmetical errors in the accounts which require location, detection and rectification thereof. Even if the trial balance tallies, there may still exist some errors. There are two types of errors: (a) errors which are not revealed by the trial balance, and (b) errors which are revealed by the trial balance. Errors may happen at any of the following stages of the accounting cycle.

A. At Recording Stage

1. Errors of principle
2. Errors of omission
3. Errors of commission

B. At Posting Stage

1. Error of omission
   (i) Complete
   (ii) Partial
2. Error of commission
   (i) Posting to wrong account
   (ii) Posting on the wrong side

   Posting of wrong amount

C. Balancing Stage

1. Wrong totaling
2. Wrong balancing

D. Preparation of Trial Balance

1. Error of Omission
2. Error of Commission
   (i) Taking wrong amount
   (ii) Taking wrong account
   (iii) Taking to the wrong side

Errors can be classified into the following four categories on the basis of the nature of errors and explained here under:

(i) Errors of omission

(ii) Errors of commission

(iii) Compensating (offsetting) errors

(iv) Errors of principle.

(a) Errors of Omission

This error arises when a transaction is completely or partially omitted to be recorded in the books of accounts. Errors of omission may be classified as below:

(i) **Error of Complete Omission:** This error arises when a transaction is totally omitted to be recorded in the books of accounts. For example, Goods purchased from Ram completely omitted to be recorded. This error does not affect the trial balance.

(ii) **Error of Partial Omission:** This error arises when only one aspect of the transaction either debit or credit is recorded. For example, a credit sale of goods to Siva recorded in sales book but omitted to be posted in Siva's account. This error affects the trial balance.

(b) Errors of Commission

This error arises due to wrong recording, wrong posting, wrong casting, wrong balancing, wrong carrying forward etc. Errors of commission may be classified as follows:

(i) **Error of Recording:** This error arises when a transaction is wrongly recorded in the books of original entry. For example, Goods of ₹ 5,000, purchased on credit from Viji, is recorded in the book for ₹ 5,500. This error does not affect the trial balance.

(ii) **Error of Posting**: This error arises when information recorded in the books of original entry are wrongly entered in the ledger. Error of posting may be

(a) Right amount in the right side of wrong account

(b) Right amount in the wrong side of correct account

(c) Wrong amount in the right side of correct account

(d) Wrong amount in the wrong side of correct account

(e) Wrong amount in the wrong side of wrong account

(f) Wrong amount in the right side of wrong account, etc. This error may or may not affect the trial balance.

(iii) **Error of Casting (Totalling):** This error arises when a mistake is committed while totalling the subsidiary book. For example, instead of ₹ 12,000 it may be wrongly totalled as ₹ 13,000. This is called **overcasting**. If it is wrongly totalled as ₹ 11,000, it is called **undercasting**.

(iv) **Error of Carrying Forward**: This error arises when a mistake is committed in carrying forward a total of one page to the next page. For example, Total of purchase book in page 282 of the ledger ₹ 10,686, while carrying forward the balance to the next page it was recorded as ₹ 10,866.

(c) Compensating Errors

The errors arising from excess debits or under debits of accounts being neutralised by the excess credits or under credits to the same extent of some other account is compensating error. Since the errors in one direction are compensated by errors in another direction, arithmetical accuracy of the trial balance is not at all affected inspite of such errors. For example, If the purchases book and sales book are both overcast (excess totalling) by ₹ 10,000, the errors mutually compensate each other. This error will not affect the agreement of trial balance.

(d) 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 violations are known as errors of principle. As an illustration, Periodicity principle requires maintaining proper distinction between capital and revenue items. An error of principle may occur due to incorrect classification of expenditure or receipts 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. For example, amount spent on additions to the buildings should be treated as capital expenditure and must be debited to the asset account. Instead, if this amount is debited to maintenance and repairs account, it is treated as a revenue expense. This is an error of principle. Since instead of asset account, i.e. buildings, the maintenance and repairs account (expense) is debited, the trial balance will still tally but would not be correct as per generally accepted accounting principles.

Such errors are not disclosed by the trial balance. This will result in understating of income due to extra charge under maintenance and repairs account and understating the value of buildings in the balance sheet

Errors disclosed and not disclosed by trial balance

If the impact of the errors on trial balance is considered, errors may be classified into two categories – Errors disclosed by trial balance, and Errors not disclosed by trial balance.

Errors

Errors disclosed by Trial Balance	Errors not disclosed by Trial Balance
1. Errors of partial omission	1. Errors of complete omission
2. Errors of casting	2. Errors of recording
3. Errors of carrying forward	3. Errors of principle
4. Errors of posting in the wrong side of the correct account	4. Errors of posting to wrong account in the right side with the correct amount
5. Errors of posting to correct	5. Compensating Errors account with wrong amount
6. Double posting in the same account	

Illustration

State the type of error involved in the following transactions and say whether it will affect the agreement of the trial balance or not.

1. The sales book is undercast by ₹ 2,000.
2. The purchases book is overcast by ₹ 1,500.
3. The purchases return book is overcast by ₹ 5,000.
4. The sales return book is overcast by ₹ 1,000.
5. Goods returned by Vani worth ₹ 1,500 were not entered.
6. Goods returned by Venu & Co. ₹ 4,000 were not posted.
7. Goods sold to Robin for ₹ 2,600 has been debited to Robert's A/c.
8. A credit sale to Basha for ₹ 3,500 was entered as ₹ 5300.
9. A purchase of Machinery for ₹ 50,000 has been entered in the purchases book.
10. A credit purchase from Senthil for ₹ 6,250 was debited to Santhosh's A/c. from purchases book.

11. Cash received for commission ₹ 2,735 was posted to the commission account as ₹ 2,375.
12. The monthly total of discount column on the debit side of the cash book ₹ 1,350 was credited to discount allowed account.
13. Cash paid for insurance ₹ 6,310 was posted to the insurance A/c. as ₹ 6,130.
14. The monthly total of discount column on the credit side of the cash book ₹ 22,500 was debited to discount received account.
15. A sale to Kaveri ₹ 6,900 has been entered in the purchases book.

Solution:

1. This is an error of casting and it affect sales account only. The trial balance will not tally.
2. This is an error of casting and it affect purchases account only. The trial balance will not agree.
3. This is an error of casting and it affect purchases return account only. The trial balance will not agree.
4. This is an error of casting and it affect sales return account only. The trial balance will not agree.
5. This is an error of complete omission. Since both the aspects have been omitted, this error will not affect the agreement of the trial balance.
6. This is an error of partial omission. Since the principles of double entry are not completed, this error will affect the agreement of the trial balance.
7. This is an error of posting i.e., right amount in the right side of the wrong account. This error will not affect the agreement of the trial balance.
8. This is an error of recording i.e., wrong entry in the subsidiary book. Since the mistake is found in both debit and credit aspects to the same extent. The agreement of the trial balance will not be affected.
9. This is an error of principle. This error will not affect the agreement of the trial balance.
10. This is an error of recording i.e., wrong entry in the subsidiary book. Since, the mistake is found in both debit and credit aspects to the same extent. The agreement of the trial balance will not affected.
11. This is an error of posting involving posting of wrong amount. Since the commission account has an excess credit of ₹ 360, the trial balance will be affected.
12. This is an error of posting involving posting on the wrong side of an account. The amount must have been debited to discount allowed account. The trial balance will not agree to the extent of ₹ 2,700 i.e., twice the amount of the transaction.
13. This is an error of posting involving posting of wrong amount. Since the insurance account has a short debit of ₹ 180, the trial balance will be affected.
14. This is an error of posting involving posting on the wrong side of an account. The amount must have been credited to discount received account. The trial balance will not agree to the extent of ₹ 45,000, ie., twice the amount of the transaction.
15. This is an error of recording. In this transaction, error is made in the book of original entry; the trial balance will not be affected. An entry has been made wrongly in the purchases book instead of the sales book. To rectify this, Kaveri A/c is to be debited with ₹ 13,800 and Purchases A/c. and Sales A/c. are to be credited with ₹ 6,900 each.

Suspense Account

When it is difficult to locate the mistakes before preparing the final accounts, the difference in the trial balance is transferred to newly opened imaginary and temporary account called 'Suspense Account'. Suspense account is prepared to avoid the delay in the preparation of final accounts. If the total debit balances of the trial balance exceeds the total credit balances, the difference is transferred to the credit side of the suspense account. On the other hand, if the total credit balances of the trial balance exceeds the total debit balances the difference is transferred to the debit side of the suspense account. For example, total of the debit column exceeds the total of the credit column by ₹ 500. This amount of ₹ 500 will be written on the credit column against Suspense Account to make the Trial Balance tally

The suspense A/c is however a temporary arrangement to make the Trial Balance agree. When the errors affecting the suspense account are located, they are rectified with suspense account. Suspense account is continued in the books until the errors are located and rectified. Such balance will be shown in the balance sheet. Debit balance will be shown on the asset side and the credit balance will be shown on the liability side. When all the errors affecting the trial balance are located and rectified, the suspense account automatically gets closed.

Illustration

The following balances were extracted from the ledger of Mr. Ramakrishna as on 31st March 2013. You are required to prepare a trial balance as on that date.

	₹		₹
Drawings	60,000	Salaries	95,000
Capital	2,40,000	Sales return	10,000
Sundry creditors	4,30,000	Purchases return	11,000
Bills payable	40,000	Commission paid	1,000
Sundry debtors	5,00,000	Trading expenses	25,000
Bills receivable	52,000	Discount earned	5,000
Plant & Machinery	45,000	Rent	20,000
Opening stock	3,70,000	Bank overdraft	60,000
Cash in hand	9,000	Purchases	7,08,000
Cash at bank	25,000	Sales	11,80,000

Solution:

In the books of Mr. Ramakrishna Trial Balance as on 31st March 2013

S. No.	Name of the account	L.F.	Dr. ₹	Cr. ₹
1.	Capital		–	2,40,000
2.	Drawings		60,000	–
3.	Sundry creditors		–	4,30,000
4.	Bills payable		–	40,000
5.	Sundry debtors		5,00,000	–
6.	Bills receivable		52,000	–
7.	Plant & machinery		45,000	–
8.	Opening stock		3,70,000	–

9.	Cash in hand		9,000	–
10.	Cash at Bank		25,000	–
11.	Sales		–	11,80,000
12.	Salaries		95,000	–
13.	Sales return		10,000	–
14.	Purchases return		–	11,000
15.	Commission paid		1,000	–
16.	Trading expenses		25,000	–
17.	Discount earned		–	5,000
18.	Rent		20,000	–
19.	Purchases		7,08,000	–
20.	Bank overdraft			60,000
21.	Suspense A/c.		46,000	–
	TOTAL		19,66,000	19,66,000

Note : The difference in the Trial Balance is transferred to suspense account to avoid delay in the preparation of final accounts.

Rectification of Errors

Correction of errors in the books of accounts is not done by erasing, rewriting or striking the figures which are incorrect. Correcting the errors that has occured is called Rectification. Appropriate entry is passed or suitable explanatory note is written in the respective account or accounts to neutralise the effect of errors. From the point of rectification, errors may be classified as follows:

i. **Single sided errors** are errors which affect one side of an account.

ii. **Double sided errors** are errors which affect both the accounts in a transaction.

Basic Principles for Rectification of Errors

All errors, whatever may be their kind or nature, result in one of the following four positions in one or more accounts.

i. **Excess debit in one or more accounts:** This must be rectified by '**crediting**' the excess amount to the respective account or accounts.

ii. **Short debit in one or more accounts:** This must be rectified by a '**further debit**' to the respective account or accounts involved.

iii. **Excess credit in one or more accounts***:* This can be rectified by '**debiting**' the respective account with the excess amount involved.

iv. **Short credit in one or more accounts:** This can be rectified by a '**further credit**' to the respective account or accounts involved.

The following three steps may be adopted while attempting to rectify an error:

(i) Ascertain what has actually been done, i.e. **what is the error?.**

(ii) Make sure what ought to have been done, i.e., **the correct record.**

(iii) Decide what is to be done in view of what has been done and what ought to have been done. i.e., **rectification.**

Stages of Rectification

The stage in which rectification is done depends on identification or locating the error. Rectification of errors may be explained in two stages.

i. **Rectification before the preparation of trial balance:** In this stage errors are located before transferring the difference in the trial balance to Suspense Account.

ii. **Rectification after the preparation of trial balance:** In this stage the difference in the trial balance would have been transferred to Suspense Account. So wherever applicable suspense account is used while passing rectification entries.

Stage at which the errors are rectified	Manner in which the errors are rectified
When the errors are rectified before transferring the difference in the trial balance to the suspense account.	By debiting or crediting the respective account with the required amount by giving an explanatory note in the particulars column.
When the errors are rectified after transferring the difference in the trial balance to the suspense account.	By writing a journal entry with the respective account or accounts affected by the errors and suspense account.

Illustration

Rectify the following errors:

(i. Purchases book is carried forward ₹ 850 less.

(ii) Sales book total is carried forward ₹ 2,500 more.

(iii) A total of ₹ 7,580 in the purchases book has been carried forward as ₹ 8,570.

(iv) The total of the sales book ₹ 7,550 on page 20 was carried forward to page 21 as ₹ 5,570.

(v) Purchases return book was carried forward as ₹ 1,520 instead of ₹ 5,120.

Solution:

S.No.	Nature of mistake	Effect of mistake	Rectification
1.	Carrying forward lower amount in purchases book	Short debit in Purchases A/c	Give further debit on Purchases A/c
2.	Carrying forward higher amount in sales book	Excess credit in Sales A/c.	Debit sales A/c
3.	Carrying forward higher amount in purchases book	Excess debit in Purchases A/c	Credit purchases A/c
4.	Carrying forward lower amount in sales book	Short credit in Sales A/c.	Give further credit to Sales A/c
5.	Carrying forward lower amount in purchases return book	Short credit in Purchases return A/c	Credit Purchases return A/c

Rectification:

(i) Debit – Purchases A/c with ₹ 850.

(ii) Debit – Sales A/c with ₹ 2,500.

(iii) Credit – Purchases A/c with ₹ 990.

(iv) Credit – Sales A/c with ₹ 1,980.

(v) Credit – Purchases return A/c with ₹ 3,600.

Illustration:

Rectify the following errors:

(i) Purchases from Bagavathi for ₹ 4,500 has been posted to the debit side of her account.

(ii) Sales to Vijay for ₹ 1,520 has been posted to his credit as ₹ 1,250.

(iii) Purchases from Shakila for ₹ 750 has been omitted to be posted to the personal A/c.

(iv) Sales to Khader for ₹ 780 has been posted to his account as ₹ 870.

Solution:

(i) Purchases from Bagavathi should have been posted to the credit of Bagavathi's A/c., but it has been debited. Hence, Credit Bagavathi's A/c with double the amount i.e, ₹ 9,000.

(ii) Sales to Vijay has to be debited in Vijay's account but his account is credited with ₹ 1,250. Hence, Debit Vijay's A/c with ₹ 1,250 + ₹ 1,520 i.e, ₹ 2,770.

(iii) This is an error of omission. Posting must be to the credit of Shakila's A/c. Hence, post ₹ 750 to the credit of Shakila's A/c.

(iv) Here Khader's A/c has been debited with a wrong amount i.e., with excess amount. To rectify this error, the excess amount must be credited to his account. Hence, credit Khader's A/c with ₹ 90.

Illustration

The following errors were found in the books of Prabhu. Give the necessary entries to correct them:

(i) Salary of ₹ 10,000 paid to Murali has been debited to his personal account.

(ii) ₹ 3,500 paid for a typewriter was charged to office expenses account.

(iii) ₹ 8,000 paid for furniture purchased has been charged to purchases account.

(iv) Repairs made were debited to building account for ₹ 500.

(v) An amount of ₹ 5,000 withdrawn by the proprietor for his personal use has been debited to trade expenses account.

(vi) ₹ 2,000 received from Shanthi & Co. has been wrongly entered as from Shakila & Co.

Errors	Particulars	L.F	Debit ₹	Credit ₹
i.	Salaries A/c Dr.		10,000	
	To Murali A/c.			10,000
	[Correction of wrong debit to Murali's personal A/c for salaries paid]			
ii.	Typewriter A/c Dr.		3,500	
	To Office expenses A/c			3,500

	[Correction of wrong debit to office expenses A/c for purchase of typewriter]			
iii.	Furniture A/c Dr. To Purchases A/c [Correction of wrong debit to purchases account for furniture purchased]		8,000	8,000
iv.	Repairs A/c Dr. To Building A/c [Correction of wrong debit to building Account for repairs made]		500	500
v.	Drawings A/c Dr. To Trade expenses A/c [Correction of wrong debit to Trade Expenses A/c. for cash withdrawn by the proprietor for his personal use]		5,000	5,000
vi.	Shakila & Co. A/c. Dr. To Shanthy & Co. A/c [Correction of wrong credit to Shakila & Co. instead of Shanthi & Co.]		2,000	2,000

Illustration

An accountant could not tally the Trial balance. The difference of ₹ 5,180 was temporarily placed to the credit of suspense account for preparing the final accounts. The following errors were later located.

(i) Commission of ₹ 500 paid, was posted twice, once to discount allowed account and once to commission account.

(ii) The sales book was undercast by ₹ 1,000.

(iii) A credit sale of ₹ 2,780 to Roja though correctly entered in sales book, was posted wrongly to her account as ₹ 3,860.

(iv) A credit purchase from Nataraj of ₹ 1,500, though correctly entered in purchases book, was wrongly debited to his personal account.

(v) Discount column of the payments side of the cash book was wrongly added as ₹ 2,800 instead of ₹ 2,400.

You are required to:

(i) Pass the necessary rectifying entries. ii. Prepare Suspense Account

Solution:

Errors	Particulars	L.F	Debit ₹	Credit ₹
i.	Suspense A/c Dr. To Discount allowed A/c [Amount wrongly debited to discount account, now rectified]		500	500

ii.	Suspense A/c Dr. To Sales A/c [Sales book undercast by ₹ 100, now rectified]		1,000	1,000
iii.	Suspense A/c Dr. To Roja A/c [Wrong posting of sale of ₹ 2,780 to Roja as ₹ 3,860, now rectified]		1,080	1,080
iv.	Suspense A/c Dr. To Nataraj A/c [Credit purchase of ₹ 1,500 from Nataraj wrongly debited to his personal account now rectified]		3,000	3,000
v.	Discount received A/c Dr. To Suspense A/c [Excess credit in discount account, now rectified]		400	400

Dr. **Suspense Account** Cr.

Date	Particulars	L.F	₹	Date	Particulurs	L.F	₹
	To Discount allowed A/c		500		By Balance b/d		5,180
	To Sales A/c		1,000		By Discount received A/c		
	To Roja A/c		1,080				400
	To Nataraj A/c		3,000				
			5,580				5,580

Chapter 12

Capital and Revenue Transactions

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

Capital Transactions

The business transactions, which provide benefits or supply services to the business concern for more than one year or one operating cycle of the business, are known as capital transactions. The transactions which relate to capital are again sub-divided into capital expenditure and capital receipt.

Capital Expenditure

Capital expenditure consist of those expenditures, the benefit of which is carried over to several accounting periods. In other words the benefit of which is not consumed within one accounting period. It is non-recurring in nature.

Characteristics

In other words, it refers to the expenditure, which may be

(i) Purchase of a fixed asset.

(ii) Not acquired for sale.

(iii) It is non-recurring in nature.

(iv) Incurred to increase the operational efficiency of the business concern.

Examples

(i) Expenses incurred in the acquisition of Land, Building, Machinery, Furniture, Car, Goodwill, Copyright, Trade Mark, Patent Right, etc.

(ii) Expenses incurred for increasing the seating accommodation in a cinema hall.

(iii) Expenses incurred for installation of fixed assets like wages paid for installing a plant.

(iv) Expenses incurred for remodelling and reconditioning an existing asset like remodelling a building.

Capital Receipt

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

Characteristics

(i) Amount is not received in the normal course of business.

(ii) It is non-recurring in nature.

Examples

(i) Capital introduced by the owner

(ii) Borrowed loans

(iii) Sale of fixed asset

Revenue Transactions

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

Revenue Expenditure

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

Characteristics

(i) It helps in maintaining the earning capacity of the business concern.

(ii) It is recurring in nature.

Examples

(i) Cost of goods purchased for resale.

(ii) Office and administrative expenses.

(iii) Selling and distribution expenses.

(iv) Depreciation of fixed assets, interest on borrowings etc.

(v) Repairs, renewals, etc.

Revenue Receipt

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

Characteristics

(i) It is received in the normal course of business.

(ii) It is recurring in nature.

Examples

(i) Sale of goods or services.

(ii) Commission and Discount received.

(iii) Dividend and interest received on investments etc.

Revenue expenditure, Capital Expenditure and Deferred revenue expenditure – Distinction

S.No.	Basis of Distinction	Capital Expenditure	Revenue Expenditure
1.	Period of benefit	Benefit is enjoyed beyond the accounting year, lasts for a long time.	Benefit is consumed during the current year only.
2.	Purpose	Relates to the acquisition of fixed assets.	Incurred for the purpose of generating revenue.
3.	Nature of occurrence	Non-recurring in nature.	Recurring in Nature
4.	Aim	Helps to increase the earning capacity of the business.	Helps to earn the existing revenue
5.	Convertibility	Converted into cash.	Cannot be convert into cash.

Capital profit and Revenue profit

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

Capital profits

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

Revenue profits

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

Capital loss and Revenue loss

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

Capital Losses

Capital losses are the losses which arise not from the normal course of business. Loss on sale of fixed asset is an example for capital loss.

Revenue Losses

Revenue losses are the losses that arise from the normal course of the business. In other words, 'net loss' – i.e., excess of revenue expenditures over revenue receipts.

Illustration:

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

(i) Purchase of furniture ₹ 1,000.

(ii) Purchase of second hand machinery ₹ 4,000.

(iii) ₹ 50 paid for carriage on goods purchased.

(iv) ₹ 175 paid for repairs on second hand machinery as soon as it was purchased.

(v) ₹ 600 wages paid for installation of plant.

Solution

(i) Capital expenditure – as it results in the acquisition of fixed asset.

(ii) Capital expenditure – as it results in the acquisition of fixed asset.

(iii) Revenue expenditure – expenses incurred on purchases of goods for sale.

(iv) Capital expenditure – as it is spent for bringing the asset into working condition.

(v) Capital expenditure – as it is spent for bringing the asset into working condition.

Illustration:

Prasad Pictures Ltd. constructed a cinema house and incurred the following expenditures during the year ended 31.12.2013.

(i) Second hand furniture purchased worth ₹ 3,00,000.

(ii) Expenses in connection with obtaining a license were ₹ 30,000.

(iii) Fire insurance, ₹ 2500 was paid on 1st January 2013 for one year.

(iv) The manager's salary for the year was ₹ 60,000.

Classify the above transactions into capital, revenue and deferred revenue expenditures.

Solution

(i) Capital expenditure – as the amount spent results in acquisition of fixed assets.

(ii) Capital expenditure – as the amount was spent on acquiring a right to carry on business.

(iii) Revenue expenditure – amount spent relates to only one year.

(iv) Revenue expenditure–incurred for the functioning of business.

Illustration

Hari & Co. incurred the following expenses during the year 2013 Classify the expenses as capital and revenue.

(i) ₹ 750 spent towards replacement of a worn out part in a machinery.

(ii. ₹ 1,500 spent for legal expenses in relation to raising of a loan for the business.

(iii) ₹ 300 spent for ordinary repairs of plant.

(iv) ₹ 6,000 spent on replacing a petrol driven engine by a diesel driven engine.

(v) Electricity charges ₹ 1,200 per month.

Solution

(i) Capital expenditure – as it helps to increase the working condition of the machinery.

(ii) Capital expenditure – as it is spent as it helps to get a capital receipt.

(iii) Revenue expenditure – as it is spent for the maintenance of the asset.

(iv) Capital expenditure – as it helps to reduce cost of production.

(v) Revenue expenditure – expenditure incurred in the normal course of the business.

Illustration

Fashion Textiles gives the following transactions of their firm during the year 2013, you are required to classify the transactions into capital or revenue.

(i) ₹ 2,500 spent on purchasing a tyre for their lorry.

(ii) They had old machinery of value ₹ 10,000 was sold for ₹ 9,500.

(iii) They received ₹ 5000 towards dividend form their investments in shares.

(iv) They were able to sell cotton 'T' shirts (cost ₹ 1,200) for ₹ 1,500.

(v) ₹ 600 was spent on alteration of Machinery in order to reduce power consumption.

Solution

(i) Revenue expenditure – as it spent to replace a part of the lorry.

(ii) Capital loss ₹ 500 – as they have incurred a loss on sale of fixed asset and ₹ 9,500 will be a capital receipt as it is a sale of fixed asset.

(iii) Revenue receipt – earned in the ordinary course of business.

(iv) Revenue receipt – ₹ 300 is received in the ordinary course of business.

(v) Capital expenditure – as it reduces cost of production.

Chapter 13
Final Accounts

Trial balance proves the arithmetical accuracy of the business transactions, but it is not the end. The businessman is interested in knowing whether the business has resulted in profit or loss and what the financial position of the business is at a given period. In short, he wants to know the profitability and the financial soundness of the business. The trader can ascertain these by preparing the final accounts. The final accounts are prepared at the end of the year from the trial balance. Hence the trial balance is said to be the connecting link between the ledger accounts and the final accounts.

Final Accounts

Trading and
Profit and Loss Account

Balance Sheet

Parts of Final Accounts

The final accounts of business concern generally includes two parts. The first part is Trading and Profit and Loss Account. This is prepared to find out the net result of the business. The second part is Balance Sheet which is prepared to know the financial position of the business. However manufacturing concerns, will prepare a Manufacturing Account prior to the preparation of trading account, to find out cost of production.

Trading Account

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

Need

At the end of each year, it is necessary to ascertain the net profit or net loss. For this purpose, it is first necessary to know the gross profit or gross loss of the business. The trading account is prepared to ascertain this. The difference between the selling price and the cost price of the goods is the gross earning of the business concern. Such gross earning is called as gross profit. However, when the selling price is less than the cost of goods purchased, the result is gross loss.

Format

Dr. Trading Account for the year ending 31st March 2013 Cr.

Particulars	₹	₹	Particulars	₹	₹
To Opening Stock		xxx	By Sales	xxx	
To Purchases	xxx		Less : Returns		
Less: Returns			Inward		

outward			By Closing stock	xxx	xxx
To Wages	xxx		By Gross Loss c/d		xxx
To Freight		xxx	(transferred to		xxx
To Carriage		xxx	P&L A/c)		
Inwards		xxx			
To Clearing charges					
To Packing charges		xxx			
To Dock dues					
To Power (factory)		xxx			
To Octroi Duty					
To Gross Profit c/d		xxx			
(transferred to					
P&L A/c)		xxx			
		xxx			
		xxx			
		xxx			
		xxx			xxx

Items appearing in the debit side

1. **Opening stock:** Stock on hand at the beginning of the year is termed as opening stock. The closing stock of the previous accounting year is brought forward as opening stock of the current accounting year. In the case of new business, there will not be any opening stock.
2. **Purchases:** Purchases made during the year, includes both cash and credit purchases of goods. Purchase returns must be deducted from the total purchases to get net purchases.
3. **Direct Expenses:** Expenses which are incurred from the stage of purchase to the stage of making the goods in saleable condition are termed as direct expenses. Some of the direct expenses are:
   - (i) **Wages:** It means remuneration paid to workers.
   - (ii) **Carriage or carriage inwards:** It means the transportation charges paid to bring the goods from the place of purchase to the place of business.
   - (iii) **Octroi Duty:** Amount paid to bring the goods within the municipal limits.
   - (iv) **Customs duty, dock dues, clearing charges, import duty etc.:** These expenses are paid to the Government on the goods imported.
   - (v) **Other expenses:** Fuel, power, lighting charges, oil, grease, waste related to production and packing expenses.

Items appearing in the credit side

(i) **Sales:** This includes both cash and credit sale made during the year. Net sales is derived by deducting sales return from the total sales.

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

Illustration

Prepare a Trading Account from the following information of a trader.

Opening Stock ₹ 15000 Sales ₹ 30600

Purchase ₹ 16500 Closing Stock ₹ 13500

Solution:

Dr. Trading Account for the year ending 31st March 2013 Cr.

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

Illustration

Prepare Trading Account for the year ending 31st March 2013 from the following information.

Opening stock	₹ 1,70,000	Purchases return	₹ 10,000
Sales	₹ 2,50,000	Wages	₹ 50,000
Sales return	₹ 20,000	Purchases	₹ 1,00,000
Carriage inward	₹ 20,000	Closing stock	₹ 1,60,000

Solution:

Trading Account for the year ending 31st March 2013

Particulars	₹	₹	Particulars	₹	₹
To Opening Stock		1,70,000	By Sales	2,50,000	
To Purchases			Less Sales Return	20,000	
Less Purchases Return	1,00,000				2,30,000
	10,000	90,000			
To Wages		50,000	By Closing Stock		1,60,000
To Carriage Inwards		20,000			
To Gross Profit c/d		60,000			
(transferred to P&L A/c)		3,90,000			3,90,000

Balancing

The difference between the two sides of the Trading Account, indicates either Gross Profit or Gross Loss. If the credit side total is more, the difference represents Gross Profit. On the other hand, if the total of the debit side is more, the difference represents Gross Loss. The Gross Profit or Gross Loss is transferred to Profit & Loss Account.

Closing Entries

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

i. **If gross profit**

Trading A/c	... Dr	x x x	
To profit and loss account			x x x
(Gross Profit transferred to Profit and loss A/c)			

ii. **If gross loss.**

Profit and loss A/c	.. Dr	x x x	
To Trading A/c			x x x
(Gross Loss transferred to Profit and loss A/c)			

Profit and Loss Account

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

Need:

The aim of profit and loss account are as follows :-

- To ascertain the Net Profit or Net Loss of the business,
- Helpful in preparation of Balance Sheet,
- Helpful in comparison of current year profit with previous year profit,

Format

Dr. **Profit and Loss Account for the year ended......................** Cr.

Particulars	₹	Particulars	₹
To Trading A/c	x x x	By Trading A/c	x x x
(Gross Loss transferred from trading A/c)		(Gross profit transferred from trading A/c)	x x x
To Salaries	x x x	By Commission earned	x x x
To Rent & rates	x x x	By Rent received	x x x
To Stationeries	x x x	By Interest received	x x x
To Postage expenses	x x x	By Discount received	
To Insurance	x x x	By Net Loss	
To Repairs	x x x	(Transferred to	
To Trading expenses	x x x	Capital A/c)	x x x
To Office expenses	x x x		

To Interest paid	x x x		
To Bank charges	x x x		
To Sundry expenses	x x x		
To Commission paid	x x x		
To Discount allowed	x x x		
To Advertisement	x x x		
To Carriage outwards	x x x		
To Travelling expenses	x x x		
To Distribution expenses	x x x		
	x x x		
To Repacking charges	x x x		
To Bad debts	x x x		
To Depreciation			
To Net Profit (Transferred to Capital A/c)	x x x		
	x x x		x x x

Items appearing in the debit side

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

(i) **Office and Administrative Expenses:** Expenses incurred for the functioning of an office are office and administrative expenses – office salaries, office rent, office lighting, printing and stationery, postages, telephone charges etc.

(ii) **Repairs and Maintenance Expenses:** These expenses relates to the maintenance of assets – repairs and renewals, depreciation etc.

(iii) **Financial Expenses:** Expenses incurred on borrowings – Interest paid on loan.

(iv) **Selling and Distribution Expenses :** All expenses relating to sales and distribution of goods – advertising, travelling expenses, salesmen salary, commission paid to salesmen, discount allowed, repacking charges etc.

Items appearing in the credit side

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

(i) Interest received on investment

(ii) Interest received on fixed deposits.

(iii) Discount earned.

(iv) Commission earned.

(v) Rent Received

Note:

(i) If trial balance shows both trading expenses as well as office expenses, the trading expenses should be shown in the trading account and office expenses should be shown in profit & loss account. On the other hand, if the trial balance shows only trading expenses, it should be shown in the profit & loss account.

(ii) If in the trial balance, wages are clubbed with salaries and shown as '**wages and salaries**'. This item is shown in trading account. On the other hand, if it appears as '**salaries and wages**', this item is recorded in the profit & loss account. Income tax paid by a proprietor is considered as personal expenses. So it should be deducted from the capital.

Illustration

Prepare Profit and Loss Account, from the following balances of Mr.Kandan for the year ending 31.12.2013.

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

Solution:

Dr. **Profit and Loss Account of Mr. Kandan for the year ending 31st Dec 2013** Cr.

Particulars	₹	Particulars	₹
To Salaries	80,000	By Gross profit (transferred from the Trading A/c)	2,50,000
To Office Rent	30,000	By Discount received	4,000
To Stationeries	3,000		
To Printing Expenses	2,000		
To Tax, Insurance	4,000		
To Discount allowed	6,000		
To Travelling expenses	26,000		
To Advertisement	36,000		
To Net profit (transferred to capital A/c)	67,000		
	2,54,000		2,54,000

Balancing

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

Closing Entries

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

(i) If net profit

Profit and Loss A/c.............Dr	x x x	
To Capital A/c		x x x
(Net profit transferred to capital A/c)		

(ii) If net loss

Capital A/c....................Dr.	x x x	
To Profit and loss A/c		x x x
(Net loss transferred to capital A/c)		

Balance Sheet

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

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

A balance sheet gives a 'snapshot' of the business at a particular date- the end of the financial year. A typical business balance sheet will show:

(i) Assets- What the business owns:

1. Fixed assets, eg. Premises, vehicles, computers etc.
2. Current assets, eg Stock in trade, debtors, cash and bank balances

(ii) Liabilities- What the business owes:

1. Current liabilities eg. Creditors, overdrafts, VAT due
2. Long term liabilities eg. Long term bank loans

(iii) Net Assets- The total of fixed assets and current assets less current and long term liabilities. The net assets are financed by the owners of the business, in the form of capital. Net assets therefore, equals the total of the 'financed by' section- the balance sheet 'balances'.

(iv) Capital- Where the money to finance the business has come from, eg. The owner's investments, business profits etc.

Need

The need for preparing a Balance sheet is as follows:

(i) To know the nature and value of assets of the business

(ii) To ascertain the total liabilities of the business.

(iii) To know the position of owner's equity.

Format

The Balance sheet of a business concern can be presented in the following two forms

(i) Horizontal form or the Account form

(ii) Vertical form or Report form

(i) Horizontal form of Balance Sheet:

The right hand side of the balance sheet is asset side and the left hand side is liabilities side. All accounts having debit balance will appear in the asset side and all those having credit balance will appear in the liability side.

Balance Sheet of .... as on..................

Liabilities	₹	₹	Assets	₹	₹
Current Liabilities :			**Current Assets :**		
Sundry creditors		xxx	Cash in hand		xxx
Bills payable		xxx	Cash at bank		xxx
Bank overdraft		xxx	Bills receivable		xxx
Outstanding expenses		xxx	Sundry debtors		xxx
Long-term Liabilities :			Investments		xxx
Mortgage loans		xxx	Closing stock		xxx
Reserve fund		xxx	Prepaid expenses		xxx
Capital :			**Fixed Assets :**		
Opening Capital	xxx		Furniture & fittings		xxx
Add: Net profit (or)	xxx		Plant & machinery		xxx
Less: Net loss	xxx		Land & buildings		xxx
Less: Drawings	xxx		Business premises		xxx
Less: Income tax	xxx		Patents & trade marks		xxx
	xxx		Good will		xxx
		xxx			
		xxx			xxx

(ii) Vertical form of Balance Sheet

In this, Balance Sheet is presented in a statement form.

Balance Sheet as on........................

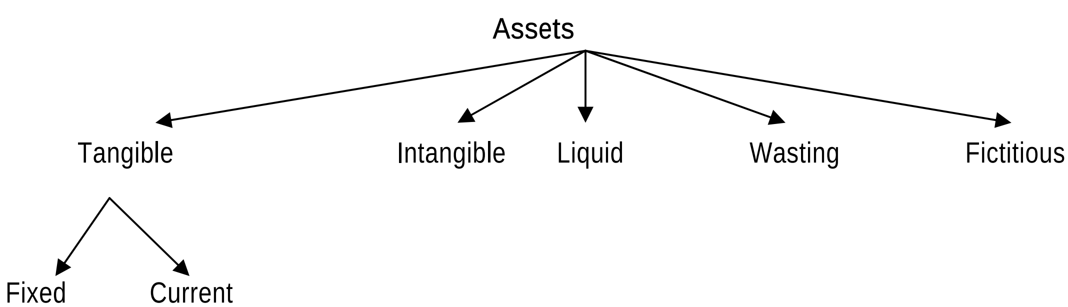
Particulars	₹	₹
Current Assets:		
Stock-in-Trade	x x x	
Sundry Debtors	x x x	
Prepaid Expenses	x x x	
Accrued Income	x x x	
Bills Receivable	x x x	
Cash at Bank	x x x	
Cash in Hand	x x x	
Total Current Assets		x x x
Less: Current Liabilities:		
Sundry Creditors	x x x	
Bills Payable	x x x	
Bank Overdraft	x x x	
Outstanding Expenses	x x x	
Total Current Liabilities		x x x
Net Working Capital		x x x
Add: Fixed Assets		
Goodwill	x x x	

Land and Building	x x x	
Plant and Machinery	x x x	
Furniture	x x x	
Investment	x x x	
Total Fixed Assets		x x x
		x x x
Capital Employed		
(Both owner's and outsiders)		
Less: Long Term Liabilities		
Debentures	x x x	
Loans	x x x	x x x
Total Long Term Liabilities		
Net Assets		
Represented by:		
Owner's Capital	x x x	
Reserves and surplus	x x x	x x x
Shareholders' Funds		x x x

Classification of Assets and Liabilities

Assets

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



(a) Tangible Assets:

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

i. Fixed assets:

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

ii. Current assets:

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

(b) Intangible Assets

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

(c) Liquid Assets

Assets which are either in cash form or can quickly converted into cash, such as Cash, Bill Receivable, Debtors etc.

Liquid Assets = Current Assets – Prepaid Expense – Closing stock

(d) Wasting Assets

These are the assets which are consumed over a period of time such as mines and oil-wells.

(e) Fictitious Assets

These are the assets which cannot be realised in cash or no further benefits can be derived from this assets. These are not really assets but are shown in Balance Sheet Assets side for the purpose of transferring them to Profit And Loss A\c gradually over a period of time. For example, Preliminary expense, Share issue expense, etc.

Liabilities

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

(a) Long Term Liabilities

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

(b) Current Liabilities

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

(c) Contingent liabilities

It is an anticipated liability which may or may not arise in future. For example, liability arising for bills discounted. Contigent liabilities does not appear in the balance sheet, but is shown as a foot note just below the balance sheet.

Marshalling of Assets and Liabilities

The term ‘Marshalling’ 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.

(a) In order of liquidity

Liquidity means convertability into cash. Assets will be said to be liquid if it can be converted into cash easily, they are placed at the top of the balance sheet. Liabilities are arranged in the order of their urgency of payment. The most urgent payment to be made is listed at the top of the balance sheet.

(b) In order of permanence

This order is exactly the reverse of the above. Assets and liabilities are recorded in the order of their life in the business concern.

Generally Sole Proprietors and Partnership Firms prepare their Balance Sheet in the order of Liquidity.

Balance Sheet Equation

An important thing to note about the Balance Sheet is that, the total value of the assets is always equal to the total value of the liabilities. This is because the liability to the owner – capital, is always made up of the difference between assets and liabilities. Thus,

Assets = Liabilities + Capital or

Capital = Assets – Liabilities

While preparing the trial balance in case it does not tally the difference is transferred to an imaginary account called as suspense account. In case the suspense account is not closed before the preparation of the final accounts then it has to be placed in the balance sheet, so that it can be rectified later. If suspense account has a debit balance it will appear as the last item in the asset side. In case it shows a credit balance it will appear as the last item in the liability side.

Difference between Trial Balance and Balance Sheet

S. No.	Basis Distinction	Trial balance	Balance sheet
1.	Objective	To know the arithmetical accuracy of the accounting work.	To know the true and fair financial position of a business.
2.	Format	The columns are debit balances and credit balances.	The two sides are assets and liabilities.
3.	Content	It is a summary of all the ledger balances – personal, real and nominal accounts.	It is a statement showing closing balances of personal & real accounts.
4.	Stage	It is the middle stage in the preparation of accounts.	It is the last stage in the preparation of accounts.
5.	Period	It can be prepared periodically, say at the end of the month, quarterly or half yearly, etc.	It is generally prepared at the end of the accounting period.
6.	Preparation	I t i s prepared before the preparation of trading, profit and loss account.	It is prepared after the preparation of trading, profit and loss account.
7.	Stock	It shows opening stock only.	It shows closing stock only.
8.	Order	Balances shown in the trial balance are not in order.	Balances shown in the balance sheet must be in order.
9.	Evidence	It cannot be produced as a documentary evidence in the court.	It can be produced as adocumentary evidence.
10.	Compulsion	Preparation of trial balance is not compulsory.	Preparation of the balance sheet is a must.

Illustration

From the following Trial Balance of M/s. Ram & Sons, prepare trading and profit and loss account for the year ending on 31st March 2013 and the balance sheet as on the date:

Trial Balance as on 31st March 2013

Particulars	Debit ₹	Credit ₹
Opening Stock (1.4.2012)	5,000	
Purchases	16,750	
Discount allowed	1,300	
Wages	6,500	
Sales		30,000
Salaries		
Travelling expenses	2,000	
Commission	400	
Carriage inward	425	
Administration expenses	275	
Trade expenses	105	
Interest	600	
Building	250	
Furniture	5,000	
Debtors	200	2,100
Creditors	4,250	13,000
Capital		
	45,100	45,100

Stock on 31st March 2013 was ₹ 6,000.

Solution :

M/s. Ram & Sons
Trading and Profit and Loss Account for the year ending 31st March 2013

Particulars	₹	Particulars	₹
To Opening stock	5,000	By Sales	30,000
To Purchases	16,750	By Closing stock	6,000
To Wages	6,500		
To Carriage inward	275		
To Gross profit c/d	7,475		
(transferred to P&L A/c)	36,000		36,000
To Discount	1,300	By Gross profit	7,475
To Salaries	2,000	(transferred from	
To Travelling expenses	400	P&L A/c)	
To Commission	425		
To Administration expenses	105		

To Trade expenses	600		
To Interest	250		
To Net profit (transferred to capital A/c)	2,395		
	7,475		7,475

Balance Sheet as on 31st March 2013

Liabilities	₹	₹	Assets	₹	₹
Creditors		2,100	Cash (Balancing figure)		2,045
Capital	13,000		Debtors		4,250
Add Net profit	2,395		Stock		6,000
			Furniture		200
		15,395	Building		5,000
		17,495			17,495

Chapter 14

Not For Profit Organisation

There are certain organisations which are formed not to earn profit but to render services to its members and to the public. Such organisations include clubs, hospitals schools, charitable institutions, etc. Though the main sources of Income of such organisations is membership subscription, donations and grants, etc. As the main aim is not to earn profit, so they do not prepare Trading and Profit and Loss A\c. But still they have to maintain proper accounts.

The Accounts which NPOs maintain are as follows :-

- **Receipt & Payment Account** which is similar to a Cash Book.
- **Income & Expenditure Account** which is a similar to Trading and Profit and Loss Account.
- **Balance Sheet** on the last date of accounting year

Distinction between Not-for-Profit Organisation and Profit Earning Organisation

S. No.	Basis of Distinction	Not-for-Profit Organisation	Profit Earning Organisation
1.	Primary Motive	Primary motive is to provide services.	Primary motive is to earn profit.
2.	Capital vs. Capital Fund	They maintain Capital Fund A\c comprising life membership fees, surplus, etc.	They maintain Capital A\c comprising profit\loss, drawing, etc.
3.	Financial Statement	Financial Statements include : • Receipt & Payment A\c • Income & Expenditure A\c • Balance Sheet	Financial Statements include : • Trading A\c • Profit and Loss A\c • Balance Sheet
4.	Surplus vs. Profit	The net result shown by Income & Expenditure A\c is surplus or deficit.	The net result shown by Profit & Loss A\c is net profit or net loss.
5.	Distribution of Profit	Surplus or Deficit is not distributed among its members.	Net Profit or Net Loss is distributed among the owners of the business.

Chapter 15

Preparation of Receipt & Payment Account and Income and Expenditure Account

Meaning

Like any other organisations Not-for-Profit Organizations (NPOs) also maintain cash book to record cash transactions on day to day basis. But at the end of the year they prepare a summary of cash transactions based on the cash-book. This summary is prepared in the form of an account. It is called Receipts and Payments account. As it is an account so it has the debit side and the credit side. All receipts are recorded on its debit side while all payments are shown on the credit side. This account begins with opening cash or/and bank balance. Closing balance of this account is cash in hand and or cash at bank/overdraft. Items in this account are recorded under suitable heads.

Following are the main features of Receipts and Payments Account:

1. It is prepared at the end of the year taking items from the cash book.
2. It is the summary of all cash transactions of a year put under various heads.
3. It records all cash transactions which occurred during the year concerned irrespective of the period they relate to i.e. previous/current/next year.
4. It records cash transactions both of revenue nature and capital nature.
5. Like any other account it begins with opening balance and ends with closing balance.

Need

As most of the transactions of Not-for-Profit Organisations are for cash, the Receipts and Payments Account shows most of the items at one place. As it is in a summary form, it gives an idea of large number of transactions at a glance. It contains accounting information under various heads. So it gives information item wise for the accounting year. It shows the closing cash or/and bank balance, this cash/Bank balance is taken to the Balance Sheet. The Receipts and Payments Account serves the purpose of trial balance and becomes the basis of preparing financial statements i.e. Income and Expenditure Account and Balance sheet for the organisation. Very small Not-for-Profit Organisations (NPOs) prepare only Receipts and Payments Account.

As the name itself suggests, Receipts and Payments Account is an account which has two sides, the debit side and the credit side. All receipts are written on the debit side and payments on the credit side. It has a definite format which is given below:

Format

Receipts and Payments Account

For the year ended on................

Receipts	Amount	Payments	Amount
Balance b/d :		Purchase of Assets	
Cash		Printing and stationery	
Bank		Repairs and Renewal	
Donations		Newspapers/Magazines	
Legacies		Rent and taxes	
Membership fees		Postage	
Entrance fees		Investments	
Subscriptions		Conveyance	
Donations		Honorarium	
Lockers Rent		Charity	
Sale of fixed assets		Insurance Premium	
Interest on investments		Upkeep of Ground	
Miscellaneous Receipts		Telephone Charges	
Sale of old periodicals		Balance c/d : Cash	
		Bank	

Preparation of Receipts and Payments Account

Following are the steps followed to prepare Receipts and Payments A/c:

1. At first the cash and bank balance carried forward from the last year is written on its debit side. In case there is bank overdraft at the beginning of the year, enter the same on the credit side of this account.

2. The amounts comprise of only cash and all cash received or paid during the period for which Receipts and Payments Account is prepared. No distinction is made between the items of revenue nature or capital nature and whether these belong to current year, previous year or the coming year.

Finally, this account is balanced by deducting the total of the credit side i.e. the total payments from the total of the debit side i.e. total receipts and is put on the credit side as 'balance c/d'.

It shows the closing cash and Bank balance which is written on the asset side of the Balance sheet of the concerned organisation.

Practical Problem

A student has prepared the following Receipts and Payments A/c. Some of the items have been entered on wrong side. Correct the statement.

Receipts and Payments A/c

For the year ended 31st December, 2013

Particulars	Amount	Particulars	Amount
Opening	1800	Entrance fees	400

Wages	800	Sale of Newspapers	200
Subscription	3600	Purchase of Books	2400
		Cash in hand	2300
		Telephone charges	600
		Interest on Fixed deposit	300
	6200		6200

Difference between Receipts and Payments Account and Cash Book

Receipts and Payment Account	Cash Book
1. It is prepared at the end the accounting year.	It is prepared on day to day basis.
2. Every item appears only once.	Items appear number of times on different dates depending upon their occurrence.
3. It serves the purpose of Trial Balance to prepare the financial statements.	It is a means of maintaining record of cash transactions.
4. It reflects the activities of the organisation.	It is only a systematic record of day to day cash transactions.
5. It is prepared only by Not-for-Profit Organisations (NPOs).	It is also prepared by business organisations meant to earn profit.

Illustration

From the information given below prepare Receipts and Payments Account for the year ending 31st December, 2013.

Cash in hand	1650	Purchase of Books	10000
Cash at Bank	18250	Purchase of Sports Material	20000
Subscription	15000	Purchase of Bicycle	2000
Entrance Fees	1200	Sale of Investment	25000
Donation	18000	Life Membership Fees	4000
Salaries	16000	Rent paid	12000
Stationery	500	Purchase of Development Bonds	10000
Insurance Premium	800	Closing Balance:	
Sale of old Furniture	1540	Cash in hand	1510
Interest on Securities	3670	Cash at Bank	20000
Lockers Rent received	4500		

Solution:

Receipts & Payments A/c
For the year ending 31st Dec. 2013

Receipts	Amount	Payments	Amount
Balance b/d:			
Cash in hand	1650	Salaries	16000
Cash at Bank	18250	Stationery	500
Entrance Fees	1200	Insurance Premium	800
Donation	18000	Purchase of Books	10000
Sale of old furniture	1540	Purchase of Sports Material	20000
Interest on securities	3670	Purchase of Bicycle	2000
Lockers Rent	4500	Rent paid	12000
Sale of Investment	25000	Purchase of development bonds	10000
Subscription	15000	Balance c/d:	
Life Membership fees	4000	Cash in hand	1510
		Cash at bank	20000
	92810		92810

Illustration:

From the information given below prepare Receipts and Payments Account of Rising Sun Club for the year ended on March 31, 2013.

Details		Amounts (₹)
Cash in hand as on 1.04.2012		9800
Cash at bank as on 1.04.2012		17600
Subscription :		
2011-12	7500	
2012-13	28600	
2013-14	6400	
Entrance Fees		42500
Life membership Fees		4000
Donations		8000
Sale of old Bats and Balls		35000
Printing and stationery		2200
Electricity Charges		2500
Telephone Charges		3600
Wages and Salaries		4200
Interest on Investments		14000
Lockers Rent received		2000
Purchase of Sports Material		2800
Purchase of Government Securities		20000
Cash in hand as on 31.0.3.2013		40000
Cash at bank as on 31.03.2006		7200
		32400

Solution:

Receipts and Payments A/c

For the year ended 31st March 2013

Particulars	Amount	Particulars	Amount
Balance b/d-		Printing & Stationery	2500
Cash in hand	9800	Electricity Charges	3600
Cash at bank	17600	Telephone Charges	4200
Subscription		Wages and Salaries	14000
2011-12 7500		Purchases of Sports Material	20000
2012-13 28600		Purchase of Government	40000
2013-14 6400	42500	Securities	
Entrance Fees	4000	Balance c/d-	
Life membership Fees	8000	Cash in hand	7200
Interest on Investments	2000	Cash at bank	32400
Locker Rent	2800		
Donations	35000		
Sales of old Bats and Balls	2200		
	123900		123900

Income and Expenditure Account

Meaning

It is the summary of incomes and expenditures of the organisation of a particular year and is prepared at the end of the year. This account is similar to the Profit and Loss Account of the Business Organisations. In this account revenue expenditure and revenue income of the year for which Income and Expenditure A/c is prepared are taken. That means any amount of these items pertaining to either previous year or next year are not considered. The balance amount of this account is either surplus or deficit. If the income side of this account exceeds the expenditure side, the difference is ‘surplus’. In case the expenditure side exceeds the income side, the difference is ‘deficit’.

Need of preparing Income and Expenditure Account

Even the Not for Profit Organisations would like to know the net result of their activities of a particular period which generally is one year. Though such organisations do not engage in trading activities and their objective is not earning profits, yet they would like to know whether income exceeds expenditure or vice a versa. The amount of the such difference is not termed as Net Profit or Net Loss as it is so termed in case of business organisations. In case of Not for Profit organisations the net result is termed as ‘surplus’ or ‘deficit’ as the case may be. Moreover of a preparation of Income and Expenditure Account is a legal requirement. It helps the organisations to control their expenditure.

Income and Expenditure A/c of ....

for the year ended 31st March ....

Particulars	Amount	Particulars	Amount
Rent **Less-** paid for last years outstanding **Less-** paid for next year **Add-** current year outstanding		Subscriptions received during the year **Less-** received on account of last year **Less-** received on account of next year	
Add- received last year On account of current year Salaries Newspaper expenses Loss on sale of furniture Depreciation Any other item of revenue expenses Expenses on consumable material say stationery Surplus-excess of income or expenditure		**Add-** subscription outstanding for current year **Add-** subscription received last year on account of current year Donations Grant in aid Sale of Grass Interest on Investment Miscellaneous Receipts Sale of old newspapers Revenue incomes Deficit : excess of expenditure over income	

Preparation of Income and Expenditure Account from Receipts and Payments Account

This account is prepared from Receipts and Payments account and additional information if any. While preparing an Income and Expenditure account, the following important points have to be kept in mind:

A. Steps for Expenditure side

The payment column of Receipts and Payments Account contains both revenue items as well as capital items. Revenue items such as rent paid salary, telephone charges etc. will be entered on the expenditure side of Income and Expenditure Account.

If necessary, adjustments will be made in these items for expenses that are outstanding at the end of the current year and/or were outstanding at the end of the previous year. Adjustment will also be made for prepaid expenses at the end of previous year as well as those at the end of current year.

B. Steps for Income side

The receipt column contains items of revenue receipts as well as capital receipts. Revenue receipts are entered in the income column of the Income and Expenditure Account. Example of such items are subscription, interest on investment, entrance fees etc.

These items need to be adjusted for the amount received for the previous year or for the next year. Similarly, adjustment should be made for outstanding income both at the current year and at the end of the previous year.

There may be other adjustments such as bad debts, depreciation, etc. which will also be entered in the expenditure column.

C. Surplus or Deficit

Finally, this account is balanced i.e. difference of the totals of two amount columns is worked out. If credit side is more than the debit side the difference amount is written on its debit side as surplus and if debit side exceeds the credit side, the difference is deficit is written on the credit side of the account.

Distinction between Income and Expenditure Account and Profit and Loss Account

S.No.	Basis of Distinction	Income and Expenditure Account	Profit and Loss Account
1.	Objective	The main objective is to ascertain excess of income over expenditure or excess of expenditure over income.	The main objective is to ascertain the net profit or net loss.
2.	Prepared by	It is prepared by Not-for-profit Organisation.	It is prepared by Profit seeking or Trading Organisation.
3.	Basis of Preparation	It is prepared on the basis of Receipts & Payment A/c and other information.	It is prepared on the basis of Trial Balance and other information.
4.	Balance	The balance of this account represents Surplus or Deficit.	The balance of this account represents net profit or net loss.

Illustration

Prepare Income and Expenditure A/c of the following information of Promising Sportsmen's club, Delhi for the year ending 31st December, 2013

	₹
Cash balance as on 1.1.2013	7000
Subscriptions	30000
Interest received	2500
Sports material	24000
Match fund	15000
Donations	2000
Sale of grass	300
Newspaper expenses	600
Investments purchased	10000
Salaries paid	16000
Rent paid	5400
Miscellaneous receipts	600
Telephone charges	1200
Cash balance as on 31.12.2013	200

Solution:

Books of Promising Sportsmen club
Income & Expenditure A/c
for the year ending 31st Dec., 2013

Expenditure	Amount	Income	Amount
Salaries	16000	Subscriptions	30000
Rent	5400	Interest Received	2500
Newspaper Expense	600	Sale of grass	300
Telephone charges	1200	Miscellaneous receipts	600
Surplus excess of income expenditure	12200	Donation	2000
	35400		35400

Illustration

Prepare Income and Expenditure Account from the Receipts and Payments

Account of Youngsters Health club, Jhansi for the year ending 31st December, 2013.

Receipt & Payment A/c

Receipts	Amount	Payment	Amount
Opening balance	2400	Rent	3600
Subscriptions	16000	Stationery	450
Entrance fees	200	Salary	4800
Sale of Investments	8000	Purchase of Equipments	5500
Sale of old Almirah	800	Expenses on competitions	2800
(Book value ₹ 1800)		Miscellaneous Expenses	650
Donation	2500	Furniture Purchased	4000
		Closing balance	8100
	29900		29900

Solution:

Books of Youngsters Health Clubs
Income & Expenditure A/c
for the year ending 31st Dec., 2013

Expenditure	Amount	Income	Amount
Rent	3600	Subscription	16000
Stationery	450	Entrance fees	200
Salary	4800	Donations	2500
Expenses on competitions	2800		
Miscellaneous Expenditure	650		
Loss on sale of almirah	1000		
Surplus (excess of Income over expenditure)	5400		
	18700		18700

Adjustment of Items in Income and Expenditure Account

Rent Paid

Rent paid is an item of expenditure. The adjustments required to made to the amount of rent paid during the year may be as follows:

(i) Rent outstanding for the current year

(ii) Rent paid in the current year as advance for the next year

(iii) Rent paid in the current year on account of the outstanding amount in the previous Year.

(iv) Rent paid in the previous year on account of current year. Journal entries in the books will be made as follows:

(i) Rent A/c Dr.

To Rent outstanding A/c

(Rent due but not paid)

(ii) Rent paid in advance A/c Dr.

To Bank A/c

(Rent paid in advance for the year)

(iii) Rent outstanding A/c Dr.

To Bank A/c

(Amount paid for outstanding rent of the previous year)

(iv) Rent A/c Dr.

To Rent paid in Advance

(Rent paid in advance last year being transferred to Rent A/c)

Calculation of Rent Amount to be shown for current year in the Income and Expenditure Account:

	Rent paid in the current year	-
Add:	Rent paid in advance in the previous year for current year	-
Add:	Rent due in current year but not paid	-
Less:	Outstanding Rent paid for previous year in current year	-
Less:	Advance rent paid for next year in current year	-
	Amount of rent to be debited to Income and Expenditure A/c	

Illustration

A club has paid rent of ₹ 20,000 in the year 2013. Rent still to be paid amounts to ₹ 2,000. Amount of ₹ 1,500 was paid in 2012 on account of the year 2013. Calculate the amount to be taken to Income & expenditure A/c of 2013.

Solution :

	₹
Rent paid in 2013	20,000
Add Rent outstanding for 2013	2,000
Add Rent paid in advance in 2012 for the year 2013	1,500
Rent for 2013 to be charged to Income and Expenditure A/c	23,500

Depreciation on Assets

Depreciation is a non cash item. It is to be charged on every fixed asset such as Land & Building, Furniture, Books etc. every year as per predetermined method. The amount of depreciation is shown on the expenditure side of the Income & Expenditure Account and is deducted from the respective value of the asset while showing it on asset side of the Balance Sheet.

Journal Entry for the same will be

1. Depreciation A/c

   To Asset A/c

2. Income and Expenditure A/c

   To Depreciation A/c

Illustration

The following is the Receipts and Payments Account of Help AID Society of India for the year ended 31st December, 2013.

Receipts and Payments A/c

Receipts	Amount	Payments	Amount
Balance b/d	8400	Salaries	12000
Subscriptions	7800	Rent	6000
Entrance fees	600	Purchase of Vans	28000
Government Grant	30000	Expenses of Motor Vans	6400
Donation for Building Fund	25000	Laundry charges	5200
Interest Received	2400	Drugs and incidental charges	9600
		Publicity expenses	4000
		Balance c/d	3000
	74200		74200

Additional Information

1. Subscription outstanding amounted to ₹ 1500
2. Interest accrued but not received ₹ 600
3. Salary outstanding is ₹ 1200
4. Provide depreciation on Motor Van @ 20%

Prepare Income & Expenditure A/c.

Solution:

Books of Help AID Society of India
Income & Expenditure A/c
for the year ending December 31, 2013

Expenditure		Amount	Income		Amount
Salaries	12000		Subscription	7800	
Add outstanding	1200	13,200	Add outstanding	1500	9300
Rent		6000	Entrance fees		600
Expenses of Motor Van		6400	Government Grant		30000
Laundry charges		5200	Interest	2400	
Drugs and incidental charges		9600	Add Interest Accrued	600	3000
Publicity Expenses		4000	Deficit i.e. excess of expenditure		
Depreciation on Motor Van		5600	over income		7100
		50000			50000

Difference between Receipts and Payments A/c and Income and Expenditure A/c

Basis of Difference	Receipts and payments A/c	Income and expenditure A/c
1. Nature	It is a summary of the Cash Book.	It is the summary of Revenue Income and Revenue Expenditure.
2. Side	Debit side of this account shows receipts and credit side shows payments.	Debit side of this account shows expenses and losses and credit side shows incomes and gains.
3. Opening Balance	It starts with the opening balance of Cash in hand or cash at bank.	There is no balance in the beginning.
4. Closing Balance	Closing balance of this account shows Cash in hand or cash at Bank.	Closing balance of this account shows Surplus or deficit.
5. Capital and Revenue Items	In Receipts and payments A/c, both capital and revenue items are recorded.	In Income and expenditure A/c, only revenue nature items are recorded.
6. Adjustment	Adjustments are not considered while preparing it.	It is necessary to consider adjustments while preparing it.
7. Transfer of closing balance	Closing balance of this account is transferred to the Receipts and Payments A/c for the next period.	Closing balance of this account is transferred to the capital fund general fund in the Balance Sheet.

Part B

Formats of Mandatory Registers maintained under MGNREGA scheme with description

Note

Ministry of Rural Development has prescribed following registers which are mandatory to prepare under MGNREGA scheme at Gram Panchayat level/ Block level/ District level:

1. Muster Roll
2. Muster Roll Issue Register (To be Maintained by the Issuing Authority i.e. Programme office at the Block Level)
3. Muster Roll Issue Register (To be Maintained by Gram Panchayat and Block)
4. Muster Roll Issue Register (To be Maintained by each Implementing Agency other than Gram Panchayat)
5. Pay Slip
6. Tender/Contract Register (To be Maintained at GP/Block/District level/ other implementing agencies)
7. Material Procurement Register (To be Maintained at GP/Block/District level/ other implementing agencies)
8. Job Card Application Register
9. Employment Register
10. Work Register
11. Assets Register
12. Complaint Register To Be Maintained At Block And District Level

In this part of Training Material includes the Format/ Performa, with description thereof, of the mandatory register to be maintained under MGNREGA scheme. Personnel are required to refer these sets of format while maintaining the documentation. Whereas, the Part A of training material will help in maintaining financial documents at respective level under the scheme.

1. Muster Roll & Accounting through Muster Roll

Gram Panchayat and Implementing Agencies are required to maintain a Muster Roll Register. The Muster Roll Register contains the details of day wise work done by every worker/labourer and payment made to such workers/labourers. For work done by daily labour, the subordinate in charge of the work will prepare a muster roll which will show the work done by daily labour and the amount payable on this account. The Muster Roll Register is the basic document through which accounting entries are passed in relation to amount paid or payable to workers. Hence, entries must be properly recorded in muster roll. Each payment should be made or witnessed by the inspection authority, who should certify the payments individually or by groups by a distinctive mark, his initial or signature. On the basis of entries made in muster roll, the worker wise pay slips are prepared.

MUSTER ROLL FORMAT

Sl. No of Muster Roll — Description of Work — Sanction Date (dd/mm/yy)

Measurement Book (Page No.) — Sanction Order No.

Sl. No	Name of worker	Job Card Regn No.	Sex (Male/Female)	Saving A/c No. (Bank or Post office if any)	Day 1*	Day 2*	Day 3*	Day 4*	Day 5*	Day 6*	Day 7*	Amt paid or credited to Bank or PO A/C	Sign/LTI of Payee
1	2	3	4	5	6	7	8	9	10	11	12	13	14
					Total Amount paid in Rs								
	Mode of payment	Number		Total of the day									
	Post office A/C			Signature of person recording attendance									
	Bank A/C												
	Business Correspondent			Signature of Inspecting Authority									
	Cash												
	Total												

*To mark attendance Workers may put their signature or LTI below the day's column. (Cont)

No. of differently abled person

Prepared by	Verified by
Name	Name
Designation	Designation

Signature and Seal of Sarpanch

Date

Note

Date Signature	Date Signature	1. Programme Office shall issue the Muster Roll 2. Numbered Muster Rolls will be maintained on the work site

Items appearing in Muster Roll Format

1) **SI. No-** Serial Number
2) **Name of worker-** Person's name who is appointed for the MGNREGA work.
3) **Job Card Regn No.** - Serial number/Registration number on the job card issued to the worker.
4) **Sex-** Male/Female
5) **Saving A/c No. (Bank or Post office if any)-** Bank account or post office account number of the concerned worker.

6-12) **Day 1* to 7*-** Attendance

13) **Amt paid or credited to Bank or PO A/C-** Whether amount is paid/credited to respective bank/post office account? (Yes/No)
14) **Sign/ LTI of Payee –** Signature and Left thumb impression of the worker.

2. Muster Roll Issue Register

Every issuing authority i.e. the programme office at the Block Level or Gram Panchayat or any other implementing agency where Gram Panchayat is not the implementing agency is required to maintain a “Muster Roll Issue Register”. The purpose of this register is to track and keep the record of all muster roll registers issued to the implementing agencies. In this register, all records regarding muster roll such as date of issue, serial number, the work for which it is issued, name of agency to whom the register is issued, etc are maintained. Further, the financial sanction number, amount sanctioned for such work and date of sanction is also required to be reported in this register. The total amount sanctioned mentioned in this register can be cross tallied with total amount paid against such work as shown in muster roll. The prescribed format of muster roll issue register is as follows:

MUSTER ROLL ISSUE REGISTER

(To be Maintained by the Issuing Authority i.e. Programme office at the Block Level)

SI. No	Date of Issue of Muster Roll	Muster Roll No.	Name of work for which issued	Financial Sanction Number and Date of Work			Name of Agency to whom Muster Roll Issued	Name, Designation and Signature of the official receiving Muster Roll
				Sanction No.	Amount	Date		
1	2	3	4	5	6	7	8	9

Items appearing in Muster roll issue register (maintained by Issuing Authority i.e. Programme office at the Block Level)

1) **Sl. No-** Serial number
2) **Date of Issue of Muster Roll-** Date on which muster roll is issued.
3) **Muster Roll No. -** Serial number of muster roll.
4) **Name of work for which issued-** Name/Description of work for which muster roll is issued.

Financial Sanction Number and Date of Work

5) **Sanction No. –** Serial number of sanction order to authorize the work.
6) **Amount-** Amount of such sanction order
7) **Date-** Date of such order.
8) Name of Agency to whom Muster Roll Issued
9) Name, Designation and Signature of the official receiving Muster Roll

MUSTER ROLL ISSUE REGISTER

(To be Maintained by Gram Panchayat and Block)

Sl. No	Muster Roll No.	Name of Work for which issued	Financial Sanction No. and Date of Work			For Muster Rolls of Works for which Gram Panchayat is the Implementing Agency		For Muster Rolls of Works for which Implementing Agencies are other than the Gram Panchayat	
			Sanction No.	Amount (In Rs.)	Date	Date of issue of muster roll by PO	Name Designation & Signature of the official	Date on which copy of the paid Muster Roll given to the GP	Date and signature of the receiving GP Official
1	2	3	4	5	6	7	8	9	10

Items appearing in Muster roll issue register (maintained by Gram Panchayat and Block)

1-6 same as Muster roll issue register (maintained by Issuing Authority i.e. Programme office at the Block Level)

For Muster Rolls of Works for which Gram Panchayat is the Implementing Agency

7) Date of issue of muster roll by PO.

8) Name Designation & Signature of the official issuing muster roll.

For Muster Rolls of Works for which Implementing Agencies are other than the Gram Panchayat

9) Date on which copy of the paid Muster Roll given to the GP.

10) Date and signature of the receiving GP Official.

MUSTER ROLL ISSUE REGISTER
(To be Maintained by each Implementing Agency other than Gram Panchayat)

Sl. No	Date of Issue/ Receipt of Muster Roll	Muster Roll No.	Name of work for which Issued	Financial Sanction No. and Date of Work			Name Designation & Signature of the official receiving Muster Roll	Date on which copy of the paid Muster Roll given to the GP for record	Date and Signature of the receiving GP official
				Sanction No.	Amount (In Rs.)	Date			
1	2	3	4	5	6	7	8	9	10

Items appearing in Muster roll issue register (maintained by each Implementing Agency other than Gram Panchayat)

1-7 same as Muster roll issue register (maintained by Issuing Authority i.e. Programme office at the Block Level)

8) Name Designation & Signature of the official receiving Muster Roll.

9) Date on which copy of the paid Muster Roll given to the GP for record.

10) Date and Signature of the receiving GP official.

3. Pay Slip

Pay slip is the basic document through which worker gets salary/wages for the work done by him. Further, this document also provides the details of work done by such worker such as work description, project description, wages amount, etc. Pay slips are prepared with the help of muster roll. The amount mentioned in the pay slip must be cross tallied with the amount mentioned in muster roll for such worker. The prescribed format of Pay Slip is as under:

PAY SLIP FORMAT

1. Name of Worker. (Name of the worker to whom pay slip is issued)
2. Address. (Permanent/Communication Address of the worker)*
3. Job Card No. (Serial number of Job Card issued to worker)*
4. Description of the Project where the worker has performed the work. (Project name and type of work where worker performed his work)*
5. Muster Roll I.D. (Serial number of Muster roll)
6. Credited amount Rs………………………………………………………………………………………………………

   (in words…….

   ……….)
7. Work done by you during period from…………….(Date) to ……………..(Date) (Period for which work is done by the worker)*
8. Pay Order No……………………Dated……………………(Number and date of cheque issued)

You are requested please collect the amount personally or through an authorized representative from…………………………………….. (Name of the Bank Branch) on

……………………. (Date) on production of this wage slip.

Thanking you

Yours faithfully,

(Name & Designation of authorized person with contact details)

*As per employment register.

4. Tender & Contract Register

A tender/contract register is to be maintained at every Gram Panchayat/Block/District Level/ other implementing agencies for recording details of tender advertised, its date, agency to whom tender is awarded and the amount for which tender is awarded. The entries in register must be properly recorded so as to ensure the proper accounting thereof. The amount entered in Column No. (5) of the tender register should be matched with the total contract cost accounted for in the books of account. The prescribed format of tender/contract register are as under:

TENDER & CONTRACT REGISTER

(To be Maintained at GP/Block/District level/ other implementing agencies)

SI. No	Description for which tender was advertised	Date of the advertisement of tender	No. of agencies/ vendor applied	Name of agency/ vendor to whom tender was awarded	Amount for which tender was awarded

Items appearing in TENDER/CONTRACT REGISTER -

1. **SI. No-** Serial Number
2. **Description for which tender was advertised-** Brief Description of work for which tender was advertised.
3. **Date of the advertisement of tender-** Date on which tender was advertised in newspaper, public portal, etc.
4. **No. of agencies/vendor applied-** Total number of applicant.
5. **Name of agency/vendor to whom tender was awarded.**
6. **Amount for which tender was awarded-** Amount of tender finalized (in Rupees).

5. Material Procurement Register

Material procurement register is the basic document in which all details regarding procurement of material such as description, date, quantity and name of vendor from whom material is purchased are kept at every Gram Panchayat, Block, District Level and other implementing agencies. However, in this register purchase value of material is not mentioned as it is not for financial users.

MATERIAL PROCUREMENT REGISTER

(To be Maintained at GP/Block/District level/ other implementing agencies)

SI. No	Description of procured material	Date of procurement	Quantity	Name of vendor

Items appearing in Material Procurement Register -

1. **SI. No-** Serial number
2. **Description of procured material-** Material/Item procured (Cement/Filling Sand/Hume pipe/Metal/Moorum/Sand for Mortar/Sign Board)
3. **Date of procurement-** Date of material/item received.
4. **Quantity-** Quantity of material received (Kgs/Numbers/Ton etc.)
5. **Name of vendor-** Name of the supplier/vendor from whom material is procured.

6. Job Card Application Register

Every worker/labourer must be registered before working under MGNREGA scheme. For registration, agency has to issue a Job Card with a serial number and date of issuance thereof to every worker/labourer. Every Gram Panchayat/Block/Implementing Agency has to maintain a register for recording the data regarding applicant name, date of receipt of application and number and date of Job Card issued to workers/labourers. The name and corresponding job card number must be tallied with entries made in muster roll. The prescribed Proforma for Job Card Application Register is as under:

PROFORMA FOR JOB CARD APPLICATION REGISTER

SI. No	Name of Applicant	Date of Receipt of Application of Job Card	No. and Date of Job Card Issued	Reasons, if Job Card not issued and any other reasons

Items appearing in Job Card Application Register-

1. **SI. No-** Serial Number
2. **Name of Applicant-** Name of the person from whom application is received.
3. **Date of Receipt of Application of Job Card-** Date on which application for Job Card is received.
4. **No. and Date of Job Card Issued-** Serial number and date on which Job card is issued to the applicant.
5. **Reasons, if Job Card not issued and any other reasons-** In case Job card is not issued to the applicant, reason thereof.

7. Employment Register

An employment register is required to be maintained by every Gram Panchayat or implementing agency for keeping records of details of every person who has worked for MGNREGA. In this register, the comprehensive details in respect of each worker is maintained such as application date, name, address, job card number, work allotted, work joining date, work done, amount paid, muster roll number, etc. The authority maintaining this register should keep following in mind:

1. The details regarding worker such as application date, name address, job card number, etc must be tallied with Job Card Application Register.
2. The details regarding work allotted, work joining date, work done, amount paid, etc must be tallied with muster roll.

EMPLOYMENT REGISTER

Sl. No	Date of Application for work	Name of Applicant with Father's or Husband's name	Address	Job Card No.	Date of Issue of Dated Acknowledgement receipt	Date of work allotment	Date of Joining work	Description of work	Total No. of days' worked	Total amount paid as wages (in Rs.)	Muster Rolls unique ID Nos.	Total Amount paid as unemployment allowance if any
1	2	3	4	5	6	7	8	9	10	11	12	13
Sub-Total for the page to be carried forward to the next page												

Items appearing in Employment Format-

1. **SI. No-** Serial Number
2. **Date of Application for work-** The date on which application is made for the work.
3. **Name of Applicant with Father's or Husband's name**
4. **Address-** Permanent/Communication Address (As per ID/Address proof)
5. **Job Card No. -** Serial number of job card issued to the worker.
6. **Date of Issue of Dated Acknowledgement receipt-**
7. **Date of work allotment-** Date on which work is allotted to worker.
8. **Date of joining work-** Date on which worker joined to work.
9. **Description of work-** Brief description of work which is allotted to worker.
10. **Total No. of days' worked-** Total number of days a worker worked on allotted work.
11. **Total amount paid as wages (in Rs.)-** Wage paid to worker in rupees.
12. **Muster Rolls unique ID Nos. –** Serial/unique number of worker's muster roll.
13. **Total Amount paid as unemployment allowance if any**

8. Work Register

Work Register contains all information about a work completed. It is a comprehensive register in which all details such as work, place, location, sanction date and number, date of start and completion, name of implementing agency, muster roll id, breakup of expenditure, date of audit, date of completion certificate, etc are kept. The total expenditure on wages must be tallied with muster roll register.

Format of Work Register

Work ID	Name of work	Village	Gram Panchayat	Location of Work (Khasra No./plot No.)	Priority in approved shelf of works	Implementing Agency	Sanction Order No. and Date		Date of Start	Date of Completion	Ids of muster roll used	Expenditure			Date of completion of social Audit	Date of issuance of completion certificate
							AS & FS	TS				Expenditure on wage	Expenditure on material	Total		
1	2	3	4	5		6	7		8	9	10	11	12	13	14	15

Items appearing in Work Register

1. **Work ID-** Serial number of work.
2. **Name of work-** Name/Description of work ID.
3. **Village-** Name of the respective village where work is sanctioned.
4. **Gram Panchayat-** Name of the respective gram panchayat where work is sanctioned.
5. **Location of Work (Khasra No. / Plot No.)**

Priority in approved shelf of works

6. **Implementing Agency-** Agency by whom work is implemented(Gram panchayat/other)
7. **Sanction Order No. and Date-** Serial number and Date of order sanctioning the work.

AS & FS

TS

8. **Date of Start-** Start date of work.
9. **Date of Completion-** Completion date of work.
10. **Ids of muster roll used**- Serial/ID number of muster roll used to carry out work.
11. **Expenditure on wage-** Total expenditure related to wages on respective work.
12. **Expenditure on material-** Total expenditure related to material on respective work.
13. **Total-** of 11& 12
14. **Date of completion of social Audit.**
15. **Date of issuance of completion certificate.**

9. Asset Register

Asset Register is an extension of work register. Asset Register is being maintained to track the post completion status, benefits, condition, etc of the asset. In this register, in addition to the details mentioned in work register some other details such as condition of the work, benefits derived from work and current status, etc are also maintained. The prescribed format of asset register is as under:

FORMAT FOR ASSETS REGISTER																		
Work ID	Name of work	Village	Gram Panchayat	Location of Work (Khasra No./plot No.)	Implementing Agency	Sanction Order No. and Date		Date of Start	Date of Completion	Ids of muster roll used	Expenditure			Date of completion of social Audit	Date of issuance of completion certificate	Condition of the work (Post-project)	Benefits derivable in terms of description of	Current status (useful/ partly derelict/ derelict)
						AS & FS	TS				Expenditure on wage	Expenditure on material	Total					
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19

Items appearing in Asset Register-

1-16 Same as of works register.

17. **Condition of the work (Post-project) -** Condition of site before starting work

18. **Benefits derivable in terms of description of capacity in area (Square meters), volume (cubic meter), length (meters), number etc.-** Increase in capacity, area, etc. of asset or site.

19. **Current status (useful/ partly derelict/ derelict) -** After completion of work whether the asset is ready to use/partly useful/non-useful)

10. Complaint Register

A complaint register shall be maintained at Block and District Level for registering complaints receiving from labourers/workers/contractors/officials etc. This register contains the details of complaint made such as name of complainant, type of complaint, action taken, disposal thereof, etc.

MAHATMA GANDHI NATIONAL RURAL EMPLOYMENT GURANTTE ACT
COMPLAINT REGISTER TO BE MAINTAINED AT BLOCK AND DISTRICT LEVEL

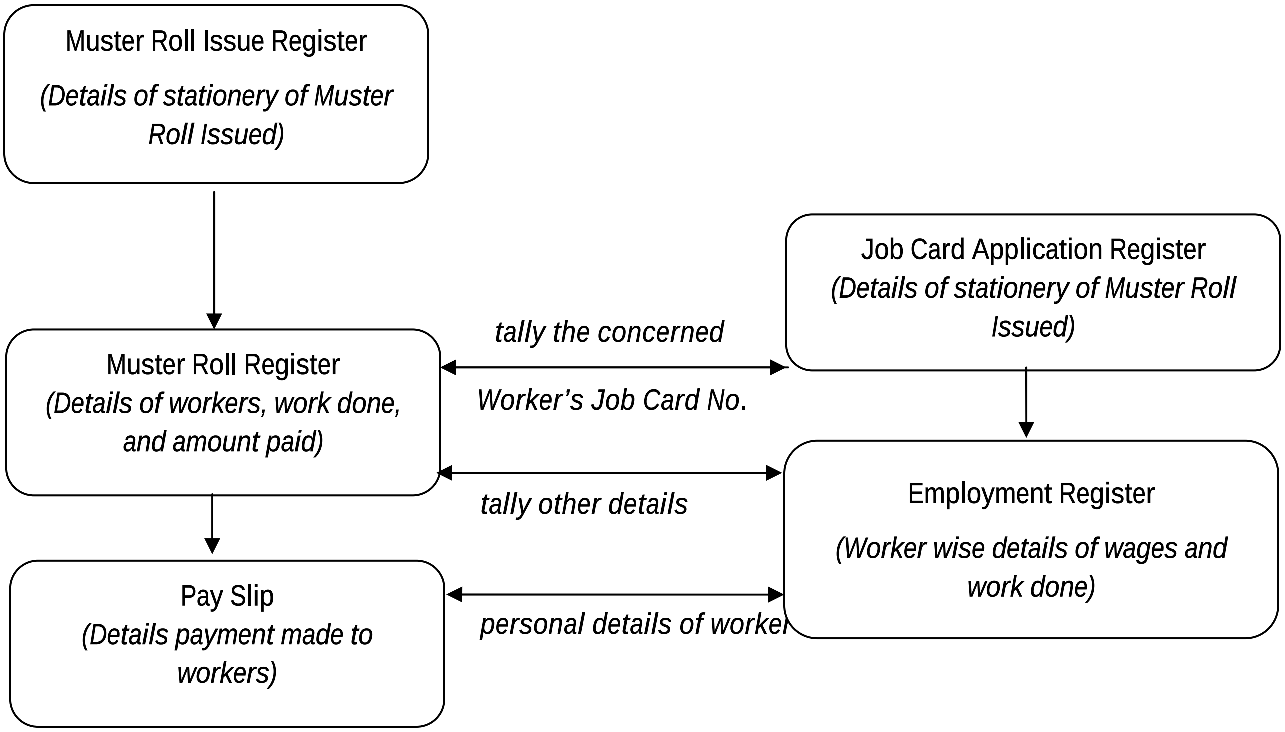
Sl. No	Date	Name and Address of Complainant	Name of Gram Panchayat and Block	Type of complaint	Complaint against whom	Action Taken	Date of Final Disposal
1	2	3	4	5	6	7	8

Items appearing in Complaint Register-

1. **Sl. No-** Serial number
2. **Date -** Date on which complaint is written.
3. **Name and Address of Complainant-** As per ID proof.
4. **Name of Gram Panchayat and Block**
5. **Type of Complaint**
6. **Complaint against whom-** Name and designation of official against whom complaint is received.
7. **Action Taken-** Action taken against the complaint.
8. **Date of Final Disposal-** Date on which complaint is resolved.

The flow of some of these registers can be understood through flow chart given below:

MGNREGA SPECIFIED REGISTERS



Accounting Aspects of Registers

Having studied and analyzed the basic source documents and their contents; let us now focus on the accounting aspect of each such register in a wholesome manner. In other words, let us now try and understand the impact of each entry made in such registers and its corresponding effect on the trial balance of the Scheme.

1. Muster Roll

The accounting entries through muster roll may be passed in the following manner:

1. Where payment to workers are made in CASH :

   Labour/Wages (Description of Work) A/c Dr.

   To Cash A/c Cr.

   (Being cash payment made to workers as per Muster Roll No. ______)

2. Where payment to workers are made through cheque / bank/ e-banking :

   Labour/Wages A/c (Description of Work) Dr.

   To ___Bank A/c Cr.

   (Being payment made to workers through cheque as per Muster Roll No. ______)

At this stage, all expenditure incurred towards labour and wages are accounted for under Labour/Wages A/c of such work and after completion of work, all expenditure incurred towards such work are capitalized for recognizing an asset.

2. Muster Roll Issue Register (To be Maintained by the Issuing Authority i.e. Programme office at the Block Level)

This register is not used for accounting purpose and used only for tracking of issued muster roll registers.

3. Muster Roll Issue Register (To be Maintained by Gram Panchayat and Block)

This register is not used for accounting purpose and used only for tracking of issued muster roll.

4. Muster Roll Issue Register (To be Maintained by each Implementing Agency other than Gram Panchayat)

This register is not used for accounting purpose and used only for tracking of issued muster roll.

5. Pay Slip

As it is a part of financials, it should be prepared with proper due diligence. The amount mentioned in each pay slip must be proper and verifiable from muster roll.

6. Tender/Contract Register

This register is not directly used for accounting purpose but the same may help in accounting such as amount paid to vendors can be cross verified with tender allotted. The amount/quantity/quality should be same as of mentioned in the tender/contract.

7. Material Procurement Register

At the time of procurement of material, the total quantity and its amount must be entered in books in the following manner:

a) **When material is purchased/received at site :**

Expenditure on Material (Work Description) A/c Dr.

To Vendor (Name) A/c Cr.

(Being _____ (Quantity) of material (description) is procured @_____ from ________ (vendor name) as per tender number ___)

b) **When payment is made to vendor through Bank/CASH :**

Vendor (Name) A/c Dr.

To Bank/CASH A/c Cr.

(Being payment made to vendor against material purchased through bill number _____)

The total quantity entered in the books of account must be same mentioned in the material procurement register. Further, the amount paid to vendor against material should not be more than amount of tender mentioned in the tender/contract register.

8. Job Card Application Register

This register is not used for accounting purpose.

9. Employment Register

Through this register, worker/labourer wise wages details can be identified. The total amount of employment register must be tallied with total amount of muster roll which contains the work wise details of wages.

10. Work Register

The accounting entries from work register may be entered in the following manner:

1. **For Expenditure incurred on wages**

Work-in-Progress (Description of Work) A/c Dr.

To Wages & Labour Account Cr.

[Being expenditure incurred on wages are transferred to ____(particular) Work-in-Progress account]

2. **For Expenditure incurred on material**

Work-in-Progress (Description of Work) A/c Dr.

To Expenditure on Material Account Cr.

[Being expenditure incurred on material are transferred to _______ (particular) Work-in-Progress A/c]

Through this register, a work can be recognized as an asset as it contains all information about a completed project. The total amount of a work should be capitalized in following manner in the books of account:

Asset (Description of Project) A/c Dr.

To Work-in-Progress (Description of Work) A/c Cr.

[Being WIP (description of work) is being capitalized as an asset]

11. Assets Register

Each total of asset register must be same as of mentioned in work register. As and when a work is recognized as an asset, it is entered in this register. The total amount of asset as mentioned in this register must also be tallied with the amount of asset recognized in the books of account.

12. Complaint Register To Be Maintained At Block And District Level

This register is not used for accounting purpose.

Accounting of other transactions and Trial Balance Preparation

1. Entries relating to Grant Received

Where any Gram Panchayat, Block or any other implementing agency receives grant from Government of India or Government of State, the accounting entries shall be passed in the following manner:

(Name of Bank) Bank A/c Dr.

To Grant Received from GOI Cr.

To Grant Received from GOS Cr.

(Being grant received from GOI/GOS vide____dated_____ for revenue/capital expenditure purposes)

Grant received may also be accounted for its nature wise such as capital or revenue. Where entries are required to be passed nature wise, the following entries may be passed:

(Name of Bank) Bank A/c Dr.

To Revenue Grants Cr.

To Capital Grants Cr.

(Being grant received from GOI/GOS vide____dated_____ for revenue/capital expenditure purposes)

2. Entries relating to other transactions

Where other transactions are carried out such as purchase of fixed assets/capital assets, payments to consultants, architects, suppliers, material rejection, interest, bank deposits, salary, fees, etc, they shall be accounted for in the books of Gram Panchayat or any other implementing agency in the manner prescribed in PART – A of this material.

3. Preparation of Trial Balance

After accounting of all transactions, a summary of transactions may be prepared in the form of "Trial Balance" in the manner prescribed in PART – A of this material. A summary trial balance may be prepared in the following manner:

Trial Balance of Gram Panchayat ______ as on _______

S. No.	Name of the Account	L.F.	Dr. Rs.	Cr. Rs.
1.	Grant Received – GOI			XXX
2.	Grant Received – GOS			XXX
3.	Bank A/c		XXX	
4.	Cash A/c		XXX	
5.	Wages & Labour A/c		XXX	
6.	Material A/c		XXX	
7.	Assets A/c		XXX	
8.	Vendor/Supplier A/c			XXX
9.	Sundry Expenses		XXX	
10.	Sundry Receipts/Incomes			XXX
11.	Other Assets		XXX	
12.	Other Liabilities			XXX
	TOTAL		XXX	XXX