CLASS XI

Accounting for BUSINESS

(PART - 1)

CENTRAL BOARD OF SECONDARY EDUCATION

2, Community Centre, Preet Vihar, Delhi-110092

Accounting for BUSINESS

(PART - 1)

CLASS XI

CENTRAL BOARD OF SECONDARY EDUCATION
PREET VIHAR, DELHI-110092

Accounting for Business (Part-I) for Class XIth.

PRICE : Rs.

FIRST EDITION 2007 © CBSE, INDIA

COPIES : 2000

PUBLISHED BY : The Secretary, Central Board of Secondary Education, Shiksha Kendra, 2, Community Centre, Preet Vihar, Delhi - 110092.

DESIGN, LAYOUT & ILLUSTRATIONS BY : Multi Graphics, 5745/81, Reghar Pura, Karol Bagh, New Delhi - 110005 Phone : 25783846

PRINTED BY :

Preface

Accelerated pace of knowledge creation and radical transformation in work and employment have generated new educational needs all over the world. Schools and institutions of higher learning can not afford to restrict courses of study within a conventional framework. The forces of liberalization that characterize economics and commerce have to be acknowledged in education too. To respond appropriately and strategically to the emerging needs of students, schools and colleges should identify new areas of knowledge that have relevance to the field of work and employment and offer them as courses of study. Many foreign Boards and Universities are already providing a wide range of subjects for students to choose from as per their needs and interests. CBSE realizes that the heightened level of awareness and enthusiasm seen today among the youth of the country, brought about by globalization and increased integration of technology, has to be harnessed for reengineering the process of human resource development. One of the ways to do it would be by providing new and exciting subjects of study at the senior secondary level. Such subjects should also form a part of vocational courses so that they address the emerging needs of students and thus become more relevant and attractive for them.

Keeping this in view CBSE is introducing new vocational courses that will be occupation-oriented and competency-driven packages. The first of such courses to be implemented in class XI from the 2007-08 academic year is Financial Market Management (FMM). This course will consist of three vocational subjects and two academic sector one of which must be a language. The syllabus and course materials for all the three vocational subjects have been prepared by CBSE with the help of professionals and experts in the respective fields.

Accounting for Business I is one of the three vocational subjects in the FMM package. The syllabus and course materials for this subject provide the students in depth knowledge in accounting procedures, banking, book keeping and taxation. Since the practical component is of 40% weightage there is adequate scope for developing the skills needed in accounting for business.

CBSE thankfully acknowledges the commendable work of the following authors who have prepared this book in a short time:

1. Shri S.S. Sehrawat, Assistant Commissioner, Kendriya Vidyalaya Sangathan, Chandigarh Region, Chandigarh

2. Shri A. Palanivel, Heal Business and Commerce Division, PSS Central Institute of Vocational Education (NCERT) Bhopal

3. Dr. S.C. Gupta, Reader, Ramjas College, University of Delhi, Delhi

4. Shri B.R. Bagri, Chairman, BLB Group of Financial Market, New Delhi

5. Shri Bakhte Munaeem, Post Graduate Teacher (Commerce), Kendriya Vidyalaya No. 2, Delhi Cantt., New Delhi

Shri Shashi Bhushan, Head of Department (Edusat) and Shri C. Dharuman, Education Officer (Voc. & Edusat) also deserve appreciation for coordinating the preparation and publication of the textbook. Suggestions for improvement of the book are always welcome.

ASHOK GANGULY
CHAIRMAN

ACKNOWLEDGEMENTS

CBSE Advisors

Sh. Ashok Ganguly, Chairman, CBSE, DELHI

Sh. Shashi Bhushan, HOD (Edusat & Vocational Education) CBSE, DELHI.

Authors

1. Sh S.S. Sehrawat, Assistant Commissioner, Kendriya Vidyalaya Sangathan, Chandigarh Region, Chandigarh.
2. Sh. A Palanivel, Heal Business and Commerce Division, PSS Central Institute of Vocational Education (NCERT) Bhopal.
3. Dr. S. C. Gupta, Reader, Ramjas College, University of Delhi, Delhi.
4. Sh. B. R. Bagri, Chairman, BLB Group of Financial Markets, New Delhi.
5. Sh. Bakhte Munaeem, Post Graduate Teacher (Commerce), Kendriya Vidyalaya No. 2, Delhi Cantt, New Delhi.

Co-Ordinator

Sh. C. Dharuman, Education Officer, (VOC. & Edusat). CBSE, DELHI.

Editors

Sh. Bakhte Munaeem, Post Graduate Teacher (Commerce), Kendriya Vidyalaya No. 2, Delhi Cantt., New Delhi.

Ms. Neena Chandra, New Delhi.

भारत का संविधान

उद्देशिका

हम, भारत के लोग, भारत को एक [1][सम्पूर्ण प्रभुत्व-संपन्न समाजवादी पंथनिरपेक्ष लोकतंत्रात्मक गणराज्य] बनाने के लिए, तथा उसके समस्त नागरिकों को:

सामाजिक, आर्थिक और राजनैतिक न्याय,

विचार, अभिव्यक्ति, विश्वास, धर्म

और उपासना की स्वतंत्रता,

प्रतिष्ठा और अवसर की समता

प्राप्त कराने के लिए,

तथा उन सब में,

व्यक्ति की गरिमा और [2][राष्ट्र की एकता

और अखण्डता] सुनिश्चित करने वाली बंधुता

बढ़ाने के लिए

दृढ़संकल्प होकर अपनी इस संविधान सभा में आज तारीख 26 नवम्बर, 1949 ई० को एतद्द्वारा इस संविधान को अंगीकृत, अधिनियमित और आत्मार्पित करते हैं।

1. संविधान (बयालीसवां संशोधन) अधिनियम, 1976 की धारा 2 द्वारा (3.1.1977) से "प्रभुत्व-संपन्न लोकतंत्रात्मक गणराज्य" के स्थान पर प्रतिस्थापित।
2. संविधान (बयालीसवां संशोधन) अधिनियम, 1976 की धारा 2 द्वारा (3.1.1977 से), "राष्ट्र की एकता" के स्थान पर प्रतिस्थापित।

भाग 4 क

मूल कर्त्तव्य

51 क. मूल कर्त्तव्य – भारत के प्रत्येक नागरिक का यह कर्त्तव्य होगा कि वह –

(क) संविधान का पालन करे और उसके आदर्शों, संस्थाओं, राष्ट्रध्वज और राष्ट्रगान का आदर करे;

(ख) स्वतंत्रता के लिए हमारे राष्ट्रीय आंदोलन को प्रेरित करने वाले उच्च आदर्शों को हृदय में संजोए रखे और उनका पालन करे;

(ग) भारत की प्रभुता, एकता और अखंडता की रक्षा करे और उसे अक्षुण्ण रखे;

(घ) देश की रक्षा करे और आह्वान किए जाने पर राष्ट्र की सेवा करे;

(ङ) भारत के सभी लोगों में समरसता और समान भ्रातृत्व की भावना का निर्माण करे जो धर्म, भाषा और प्रदेश या वर्ग पर आधारित सभी भेदभाव से परे हों, ऐसी प्रथाओं का त्याग करे जो स्त्रियों के सम्मान के विरुद्ध हैं;

(च) हमारी सामासिक संस्कृति की गौरवशाली परंपरा का महत्त्व समझे और उसका परीक्षण करे;

(छ) प्राकृतिक पर्यावरण की जिसके अंतर्गत वन, झील, नदी, और वन्य जीव हैं, रक्षा करे और उसका संवर्धन करे तथा प्राणिमात्र के प्रति दयाभाव रखे;

(ज) वैज्ञानिक दृष्टिकोण, मानववाद और ज्ञानार्जन तथा सुधार की भावना का विकास करे;

(झ) सार्वजनिक संपत्ति को सुरक्षित रखे और हिंसा से दूर रहे;

(ञ) व्यक्तिगत और सामूहिक गतिविधियों के सभी क्षेत्रों में उत्कर्ष की ओर बढ़ने का सतत प्रयास करे जिससे राष्ट्र निरंतर बढ़ते हुए प्रयत्न और उपलब्धि की नई उंचाइयों को छू ले।

THE CONSTITUTION OF INDIA

PREAMBLE

WE, THE PEOPLE OF INDIA, having solemnly resolved to constitute India into a [1] **SOVEREIGN, SOCIALIST, SECULAR, DEMOCRATIC REPUBLIC** and to secure to all its citizens :

JUSTICE, social, economic and political;

LIBERTY of thought, expression, belief, faith and worship;

EQUALITY of status and of opportunity; and to promote among them all

FRATERNITY assuring the dignity of the individual and the [2] [unity and integrity of the Nation];

IN OUR CONSTITUENT ASSEMBLY this twenty-sixth day of November, 1949, do **HEREBY ADOPT, ENACT AND GIVE TO OURSELVES THIS CONSTITUTION.**

1. Subs, by the Constitution (Forty-Second Amendment) Act. 1976, sec. 2, for "Sovereign Democratic Republic (w.e.f. 3.1.1977)
2. Subs, by the Constitution (Forty-Second Amendment) Act. 1976, sec. 2, for "unity of the Nation (w.e.f. 3.1.1977)

THE CONSTITUTION OF INDIA

Chapter IV A

Fundamental Duties

ARTICLES 51A

Fundamental Duties - It shall be the duty of every citizen of India-

(a) to abide by the Constitution and respect its ideals and institutions, the National Flag and the National Anthem;

(b) to cherish and follow the noble ideals which inspired our national struggle for freedom;

(c) to uphold and protect the sovereignty, unity and integrity of India;

(d) to defend the country and render national service when called upon to do so;

(e) to promote harmony and the spirit of common brotherhood amongst all the people of India transcending religious, linguistic and regional or sectional diversities; to renounce practices derogatory to the dignity of women;

(f) to value and preserve the rich heritage of our composite culture;

(g) to protect and improve the natural environment including forests, lakes, rivers, wild life and to have compassion for living creatures;

(h) to develop the scientific temper, humanism and the spirit of inquiry and reform;

(i) to safeguard public property and to abjure violence;

(j) to strive towards excellence in all spheres of individual and collective activity so that the nation constantly rises to higher levels of endeavour and achievement.

CONTENTS

CHAPTER 1

Introduction to Accounting
Meaning, Importance and Terminology

Learning Objectives

After studying this chapter you will be able to

- state the meaning and need for accounting
- understand the various types of accounting
- understand the basic terms used while doing accounting
- identify the various users of accounting information
- comprehend the meaning of Generally Accepted Accounting Principles (GAAP)
- explain the various concepts and conventions
- understand the different types of accounts, and
- comprehend the rules of Debit and Credit.

Evolution of accounting is spread over several centuries. It is as old as money itself. The modern system of accounting based on the principles of Double Entry System owes its origin to Luco Pacioli, who first published the principles of Double Entry System in 1494 at Venice in Italy. Over centuries, accounting has remained confined to the financial record keeping functions of the accountant. But in today's fast changing business environment, the role of an accountant has changed from that of a mere recorder of the financial transactions to that of the member providing information to the decision-making team. Accountants are now working in newer and newer areas such as financial planning, forensic accounting, e-commerce, environmental accounting etc. This has happened because of the fact that present day accounting is capable of providing information that managers and other interested persons need in order to make decisions concerning a business enterprise. Accounting now is regarded as an information system and has become an integral part of the Management Information System. As an information system, accounting collects data and communicates economic information about a business enterprise or about any other entity to a wide variety of persons whose decisions and actions are related to the performance of the business enterprise or any other entity. This introductory chapter deals with the meaning, nature, types and limitations of accounting.

1.1 Meaning of Accounting

The main purpose of accounting is to ascertain the profit or loss incurred during a specified period, generally one year, to show the financial condition of the business on a particular date and to have control over the property of the enterprise. Accounting records are required to be maintained to measure the income of the business and communicate the information so that the same may be used by the managers, owners and other parties. Accounting as a discipline records, classifies, summarizes and interprets financial information about the activities of an enterprise so that intelligent decisions can be made about the enterprise. The American Institute of Certified Public Accountants has defined financial accounting as " the art of recording, classifying and summarizing, in a significant manner and in terms of money, transactions and events which are in part, at least, of a financial character, and interpreting the results thereof ". American Accounting Association has defined accounting as " the process of identifying, measuring and communicating economic information to permit informed judgments and decisions by users of the information".

Accounting can, therefore, be defined as the process of identifying, measuring, recording and communicating the required information relating to the economic events of an organisation to the interested users of the information. From the above, the following attributes of accounting emerge

(i) It is the art of recording and classifying business transactions and events

(ii) The transactions or events of a business must be recorded in monetary terms

(iii) It is the art of making summaries, analysis and interpretation of the business financial transactions.

(iv) The result of such analysis must be communicated to the persons who are to make decisions or form judgments.

1.2 Types of Accounting

There are three important types or branches of accounting

(i) **Financial Accounting :** The most important branch of accounting it is concerned with the recording, classifying, summarizing and analysing of business transactions. It is directed towards the preparation of profit and loss account, and balance sheet. With the help of these financial statements business results are communicated to the interested parties or users for decision-making.

(ii) **Cost Accounting :** Cost accounting is the process of accounting for costs. It is a systematic procedure for determining the unit cost of output produced or services rendered. The basic functions of cost accounting are to ascertain the cost of a product and to help the management in the control of cost. It is that branch of accounting which deals with the classification, recording, allocation, summarization and reporting of current and prospective costs. Through analysis of the expenses of operating a business, it helps in controlling the cost of products or services provided.

(iii) **Management Accounting :** Management accounting is concerned with the supply of information which is useful to management in decision-making for the efficient functioning of the enterprise and, thus, in maximising profits. It is the reproduction of financial statements (Profit and Loss Account and Balance Sheet) in such a way as will enable the management to take decisions and to control activities.

1.3 Basic Terms

(i) **Financial Transaction:** It is an event which involves the exchange or transfer of some value between two or more entities,for e.g, purchase of goods, sale of goods, amount lent to another firm, payment of expenses, receipt of commission, dividends etc. A transaction may be a credit transaction or a cash transaction. When the party does not give cash immediately on entering into a transaction but agrees to pay later, it is called a credit transaction. When the payment is received in cash immediately on entering into the transaction then it is called cash transaction.

(ii) **Capital:** It refers to the amount invested by the owner(s) in the enterprise. It may be brought by the owners in cash or in the from of assets. It indicates the interest of the owner(s) in the assets of the enterprise.

(iii) **Assets:** These are economic resources of an enterprise that can be usefully expressed in monetary terms. Assets consist of tangible objects or intangible rights owned by the enterprise and carrying probable future benefits. Examples of tangible assets are cash, bank balance, inventories, machinery, furniture, and building. Examples of intangible assets are goodwill, patents, copyrights, trade marks. Assets can also be broadly classified into two types: fixed assets and current assets. Fixed assets are held for long use in business itself for the purpose of providing or producing goods or services and are not held for re-sale purpose in the normal course of business, for e.g., land, building, machinery, furniture and fixtures. Current assets are held on a short-term basis; normally short-term refers to an accounting year. Examples of current assets are cash, bank balance, debtors, bills receivable, investment etc. These are expected to be converted into cash or consumed in the production of goods, or rendering of services in the normal course of business.

(iv) **Liability:** These are the obligations or debts that the enterprise must pay in money or services at some time in the future. Liabilities are debts, for e.g, amount due to creditors, bank overdrafts, bills payable, loans etc. Like assets, liabilities can also be broadly classified into two categories: fixed or long-term liabilities and current or short-term liabilities. Long-term liabilities are those that are payable after a period of one year, for e.g, a term loan from a financial institution, debentures etc. issued by a company. Short-term liabilities are such obligations of the enterprise that are payable within a year e.g. creditors (accounts payables), bills payable (notes payable), cash credit, overdraft, short-term loans etc.

(v) **Revenue:** These are the amounts that the business earns by selling its products or providing services to customers. Other items of revenue common to many businesses are commission, interest, dividends, royalties, rent received etc. Revenue is also called income. It is measured by the charges made to customers, or clients, for goods supplied and services rendered to them and by the charges and records arising from the use of resources of the enterprise by them.

(vi) **Debtors:** They are persons and/or other entities to whom goods have been sold or services provided on credit and who thus owe certain amount to the enterprise. They are also referred to as accounts receivable or trade debtors. Debtors are assets for an enterprise and the total of debtors on the closing date is shown on the assets side of the balance sheet as “sundry debtors”.

(vii) **Creditors:** These are persons and/or other entities who have to be paid by an enterprise an amount for providing goods and services on credit. They are also referred to as accounts receivable or trade creditors. The total amount standing to the favour of creditors on the closing date is shown in the balance sheet as ‘sundry creditors’ on the liability side.

(viii) **Goods :** Articles or items purshased for sales purpose at profit or procassing by the bussiness or for use in the manufacturing process as raw material are known as goods. In other words, goods are commodities in which the business deals, for e.g., tables, chairs, desks etc are goods for a firm dealing in furniture. Americans use the term ‘merchandise’ for goods.

(ix) **Expenses:** These are the costs incurred by a business in the process of earning revenues. Generally, expenses are the cost of assets consumed or service used during an accounting period. Some examples of expenses are wages, salary, rent, interest, depreciation, telephone charges etc.

(x) **Purchases:** These are the total amount of goods procured by a business on credit or for cash for use or for resale. In a trading concern goods are purchased for resale with or without processing whereas in a manufacturing concern, raw materials are purchased, processed further into finished goods, and then sold.

(xi) **Sales:** Total revenues from goods sold and/or services rendered to the customers are called sales. They may be in cash or on credit.

(xii) **Depreciation :** It is a measure of the wearing out, consumption or other loss of value of a fixed asset arising from use, afflux of time or obsolescence through technology and market changes. Depreciation is allocated so as to charge a fair proportion of the depreciable amount in each accounting period during the expected useful life of the asset.

1.4. Users of Accounting Information

The basic objective of accounting is to provide information to its users. These users of are classified into the following two categories.

(i) External users of accounting information

(ii) Internal users of accounting information.

1.4.1 External users of accounting information

External users are those persons or groups who are outside the organisation for whom the accounting function is being performed. Following are the important external users of accounting information.

(i) **Investors:** Those who are interested in investing money in an organisation are interested in knowing the financial health of the organisation, how safe the investment already made is, and how safe the future investment will be. Thus, investors, for making investment decisions, are dependent upon accounting information available in financial statements. They can know the profitability and financial position of the enterprise by making a study of the accounting information given in the financial statements of the enterprise.

(ii) **Creditors :** Suppliers of goods and services on credit, bankers and other lenders of money are creditors. They are interested in knowing the short-term financial position of the enterprise before giving loans or granting credit. They want to be sure that the enterprise will not experience difficulty in making their payment in time i.e. the liquid position of the concern is satisfactory. To know the liquid position, they need accounting information relating to current assets and current liabilities which is available in the financial statements.

(iii) **Government:** Central and state governments are interested in accounting information since they want to know the earnings or sales of a particular period for the purpose of taxation. Governments also require accounting information for compiling statistics concerning business which, in turn, helps in compiling national income account.

(iv) **Consumers:** Consumers need accounting information so as to know the cost of goods and to ascertain that they are being charged reasonable price of the goods they are buying for their satisfaction.

1.4.2. Internal users of accounting information

Internal users of accounting information are those persons or groups which are within the enterprise. Following are the important internal users of accounting information.

(i) **Owners:** Owners provide capital for the operations of the business and want to ascertain whether their funds are being properly used or not. They need accounting information to know the profitability and the financial position of the enterprise in which they have invested their funds. The financial statements provide such information for better investment and future planing.

(ii) **Management:** The most important function of management is decision making. Management needs accounting information in selecting alternative proposals, for e.g., whether to buy or produce a product. It also requires the same for controlling acquisition and maintenance of inventories, receipts and payments of cash, purchases of sales etc. Accounting information is also important for the management for planning or budgeting for the future. Managers require it for appraising performance and devising remedial measures for the deviations of the actual results from the budgeted targets.

(iii) **Employees:** Employees are interested in the financial position of the enterprise, particularly for the payment of bonus when it depends upon the amounts of profits earned. They require accounting information for settling disputes relating to their wages.

1.5 Generally Accepted Accounting Principles (GAAP) Concepts and Conventions

Evolution of accounting is spread over several centuries and during this period certain rules, procedures and conventions have come to be accepted as useful. These rules etc. represent a consensus view of the profession for good accounting practices and procedures and are commonly referred to as Generally Accepted Accounting Principles (GAAP). It means the set of rules and practices followed in recording transactions and preparing the financial statements (profit and loss account and balance sheet). The GAAP provide a set of guidelines to be observed by the accounting profession for preparing and reporting the accounting information and can be broadly classified into two categories – concepts and conventions.

1.5.1 Accounting concepts

Basic accounting concepts are referred to as the fundamental ideas or basic assumptions underlying the theory and practice of accounting and are broad working rules for all accounting activities. Accounting is the language of business and to make this language convey the same meaning to all people, as far as practicable, and to make it meaningful, accountants have agreed on a number of concepts which are followed in the preparations of financial statements. These concepts are discussed below.

(i) **Separate Entity Concept:** According to this concept, also known as business entity concept, business is treated as a separate unit or entity from its owners. This concept implies that a business is separate and distinct from the persons who supplied capital to it. All transactions of the business are recorded in the books of the firm. If the business affairs and the private affairs of the owners are mixed, the true picture of the business will not be available. The proprietor is treated as a creditor of the firm to the extent of his capital. Capital is thus a liability to the firm and the proprietor is the creditor as the business. The proprietors – sole trader, partners of a partnership firm etc. may draw an amount out of the business for their personal use and, to that extent, it reduces the liability of the firm. Because of this concept, financial position of the business can be easily found out and earning capacity of the firm can be easily ascertained. It is important to note that transactions of the business affairs and private affairs are separated for reporting only and in law no such distinction is recognised except of an incorporated company.

(ii) **Going Concern Concept:** This concept assumes that a business entity will continue to operate indefinitely and that it will not be liquidated in the immediate future and the financial statements are prepared on this assumption. The business is called 'going concern' which means that it will remain in operation in the foreseeable future unless it is to be liquidated in the near future. Since this concept believes in the continuity of the business over an indefinite period, it is also known as continuity concept. It is because of the going concern concept that distinction between (a) fixed assets and current assets (b) short-term and long-term liabilities and (c) capital and revenue expenditure is made.

(iii) **Money Measurement Concept:** This concept states that only those transactions which can be expressed in money terms are recorded in accounting though their quantitative records may also be kept. Thus means that all business transactions are expressed only in money. Thus, transactions which cannot be expressed in money will not be recorded in accounting books however important they may be for the business. For example, labour-management relations, sales policies, labour unrest, effectiveness of competition etc, which are of vital importance to the business enterprise, do not find any place in accounting. Since money is the only practical unit of measurement that can be employed to achieve homogeneity of financial data, money measurement concept helps in making the accounting records clear, simple, comparable and understandable.

The acceptability of money as a unit of measurement suffers from certain limitations such as the comparison of financial statements over a period of time because of difference in prices. It needs to be noted that the money measurement concept implies stability of measuring unit over a period of time. This may not be true because, over a period of time, prices of goods and services may change, and hence the purchasing power of money may undergo a change. But these changes are usually not recorded. This affects the comparability of financial statements at different time periods.

(iv) **Accounting Period Concept:** Accounting period refers to the time period at the end of which the financial statements of a business enterprise are prepared so as to know the amount of profit earned or loss incurred by it during that period of time as well as the position of its assets and liabilities at the end of that period of time. Normally, accounting period adopted is one year as it helps to take any corrective action, pay income tax, absorb the seasonal fluctuations, and for reporting to outsiders. The principle of segregating capital expenditure from revenue expenditure is based on the accounting period concept. The revenue expenditure for a particular period is transferred to the profit and loss account of that period whereas capital expenditure is carried forward to the extent that its benefits will be utilised in future accounting period and are shown as assets in the balance sheet of the enterprise prepared at the end of that period.

(v) **Dual Aspect Concept or Accounting Equation Concept:** This is the basic concept of accounting and provides the very basis of recording transactions in the books of accounts. According to this concept, every financial transaction involves a two-fold aspect (a) yielding of a benefit and (b) the giving of benefit. For example, if a business has acquired an asset, it must have given up an asset such as cash or incurred obligation to pay for it in the future. Thus a giver necessarily implies a receiver and a receiver necessarily implies a giver. There must be a double entry to have a complete record of each business transaction, an entry being made in the receiving account and an entry of the same amount in the giving account. The receiving account is called the 'debtor' and the giving account is called the 'creditor'. Thus every debit must have a corresponding credit and vice versa. It is upon the dual aspect concept that the whole superstructure of 'Double Entry System' of accounting has been raised. The 'accounting equation' (i.e. Assets = Capital+Liabilities) is based upon the dual aspect concept and that is why this concept is also called as accounting equations concept. The term 'assets' denotes the resources owned by the business while 'equities' (Capital + Liabilities) denotes the claims of various claimants including the proprietors of the business against assets. The accounting equation has been explained as follows: Suppose A (the proprietor) invested Rs 1,00,000 to start the business. The accounting equation will be as follows.

Assets = Capital + Laibilities

Cash(Rs1,00,000)=Capital(Rs1,00,000)+Liabilities (0)

Subsequently, if the business purchased machinery worth Rs 40,000 and furniture worth Rs 10,000, the accounting equation will be as follows

Cash	+	Machinery	+	Furniture	=	Capital	+	Liability
(Rs1,00,000)		Rs 40,000	+	Rs.10,000	=	(Rs 1,00,000)	+	(0)
(Rs 40,000)								
(Rs 10,000)								

or

Cash(Rs 50,000) + Machinary(Rs 40,000) + Furniture(Rs 10,000) = Capital(Rs 1,00,000) + Liabilities(0)

Thus the accounting equation demonstrates that for every debit there is an equal credit.

(vi) **Accrual Concept :** The essence of accrual concept is that revenue is recognised when it is occurred or realised i.e. when sale is complete or services are given and it is immaterial whether cash is received or not. Similarly, according to this concept, expenses are recognised in the accounting period in which they help in earning the revenues whether cash is paid or not. Thus, to ascertain correct profit or loss for an accounting period we must take into account all expenses and incomes relating to the accounting period whether actual cash has been paid or received or not. It is because of this concept that outstanding expenses and accrued incomes are taken into account.

(vii) **Matching Concept :** This concept requires that the expenses of a period must be matched with the revenues of that period for the ascertainment of the profit earned or loss suffered by the enterprise during that period. Matching concept is of great significance since the performance of a business enterprise in usually measured in terms of income earned by the enterprise. Expense is recognised not when cash is paid or when a product is produced but when the product actually contributes to the revenue. This concept requires that part of the cost of fixed assets consumed in the operations of the business, called depreciation, is treated as expense of the period. Similarly, revenues received in advance for which services have not been rendered will be treated as unearned income and therefore, will be carried forward to the next accounting period.

1.5.2 Accounting conventions

Accounting conventions have been evolved and developed to bring about uniformity in the maintenance of accounts. Convention denotes customs or traditions or usage which are in use since long. To be more precise accounting conventions are nothing but unwritten laws. The accountants have to adopt usage or customs which are used as a guide in the preparation of accounting reports and statements. Following are the important conventions.

(i) **Revenue Recognition Convention :** This convention helps in ascertaining the amount and time of recognising revenues from business activities. Revenue is said to have been earned in the period in which sales have taken place or services have been rendered to the satisfaction of the customers and the revenue has been received or has become receivable. However, there are some exceptions to this rule. For example, in case of contracts of construction works which take a long time 'say 2-5 years' to be completed, proportionate amount of revenue based on the part of contract completed by the end of the accounting period is considered as realised. Similarly, when goods are sold on hire purchase basis, the amount collected in installments is considered as revenue realised.

(ii) **Full Disclosure Convention:** According to this convention, all accounting statements should be honestly prepared and to that end full disclosure of all significant information should be made. All information which is of material interest to proprietors, creditors and investors should be disclosed in accounting statements. An obligation is placed on the accounting profession to see that the books of accounts prepared on behalf of others are as reliable and informative as circumstances permit. For example SEBI regulations require disclosures to be made by companies to potray true and fair view of business operations to ensure the discharge of accountability by those who prepare the various financial statements. Accountability is said to have been discharged when complete information is delivered with due diligence so that the economic interests of the users of the accounting information are not adversely affected.

(iii) **Conservatism Convention or Prudence:** "Anticipate no profit and provide for all possible losses" is the essence of this convention. Future is uncertain and uncertainties are not uncommon for a business enterprise also. Conservatism refers to the policy of choosing the procedure that leads to understatement of resources and income. The consequences of an error of understatement are likely to be less serious than that of an error of overstatement. For example, closing stock is valued at cost or market price whichever is less. This convention of caution of playing safe is adhered to while preparing financial statements. Showing a position better than what it is not permitted. Moreover, it is not proper to show a position substantially worse than what it is.

- The value of an asset should not be overestimated.
- The value of a liability should not be underestimated.
- Profit should not be overestimated.
- Loss should not be underestimated.

Convention of conservation is generally applied to present a true and fair value of the business in the financial statement.

1.6. Types of Accounts

Before understanding the different types of accounts one must know the meaning of 'account'. An account is the record of an individual, a firm, a thing, an item of expense, or an income. Therefore, an account is a summarized record of business transactions that affects a particular type of assets, liability or capital.

The transactions in which a business enterprise may enter can be classified into the following three categories.

(i) Transactions relating to persons or individuals

(ii) Transactions relating to property, assets or possessions, or

(iii) Transactions relating to expenses or income.

Corresponding to the above three categories of transactions, the accounts maintained by a business enterprise are classified into the following three types.

(i) Personal accounts

(ii) Real or property accounts

(iii) Nominal accounts

Real and nominal accounts taken together are also categorised as impersonal accounts.

1.6.1 Personal Accounts

Personal accounts record the dealings of the enterprise with persons or firm. These can be further sub-divided into the following types.

(i) **Natural Persons Accounts :** The accounts in the name of natural persons are called natural persons accounts. For proprietors' account, supplier,s account, receivers' account (like Ram's account, Shyam's account, Sohan's account).

(ii) **Artificial Persons and Body of Persons Accounts:** Accounts in the name of artificial persons and body of persons come under this category i.e. any limited company's accounts (like Relliance Ltd account, Maruti Udyog account), bank account (like State Bank of India account), insurance company's account (like LIC account), any firm's account (like Gopal Das Firm account), any government or institution's account, any clubs account (like Sports Club of New Delhi account).

(iii) **Representative Personal Accounts :** When an account represents a certain person or persons it is called a representative personal account. In such accounts, in the books of the firm, the names of actual individuals appear but since they are of the same nature and large in number, the balances standing in these accounts are added and put under one common head . For example, if a business is not able to pay the salary for the last one month to its employees, such employees will be treated as its creditors (since they have provided their service to the business but in exchange have not been paid for the same) The amount due to these employees will be put under one common head called 'Salaries Outstanding Account'. Thus salaries outstanding account is a personal account representing the employees of the enterprise. Similarly, we may have ' Rent Outstanding Account' 'Rent pre-paid Account', 'Interest Outstanding Account', 'Interest prepaid Account', 'Interest Received in Advance Account' 'Unearned Commission Account' etc.

1.6.2. Real Accounts

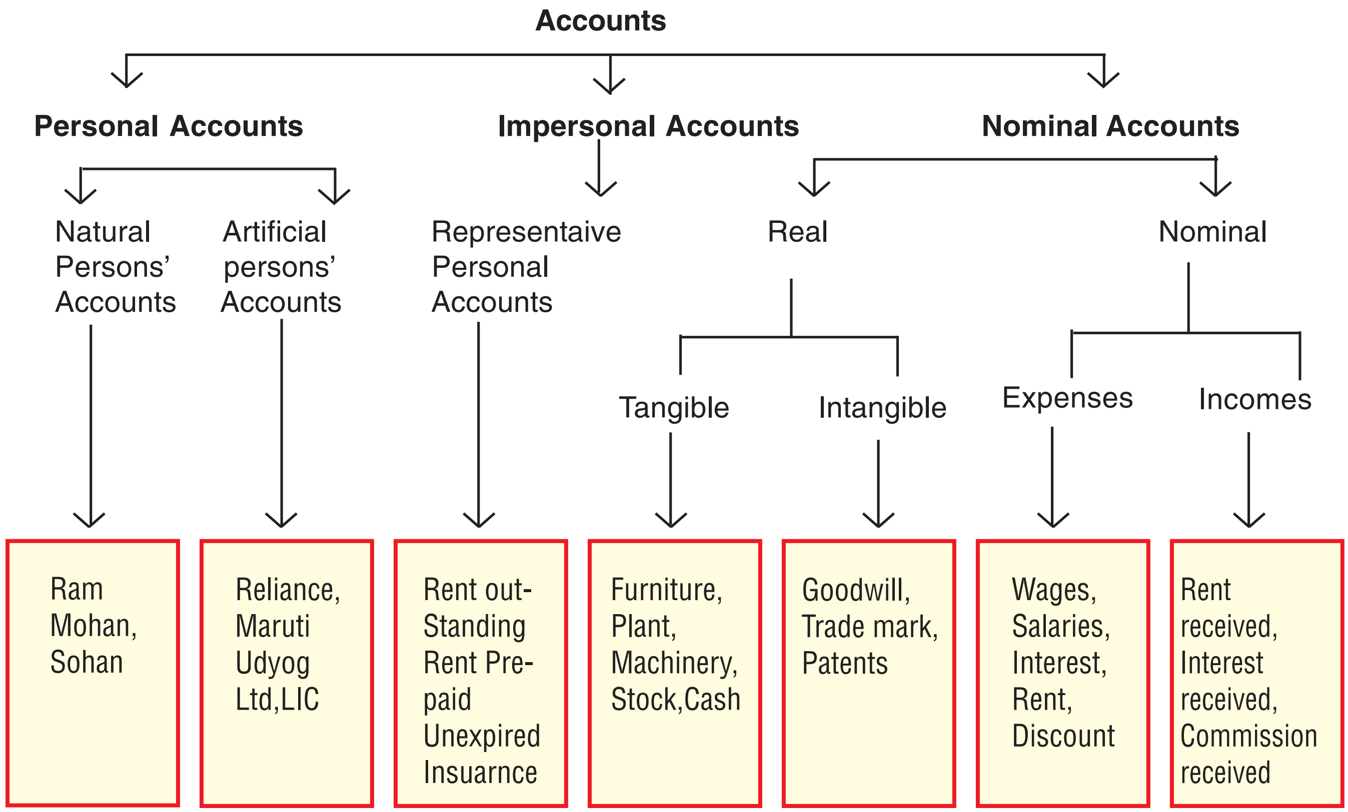
These are also called as property accounts as they are accounts of properties, assets or possessions. Real accounts represent items which are more or less permanent in nature. A separate account is kept for each type of asset such as land, building, furniture, plant and machinery, cash, stock etc. so that by recording each such asset received or disposed off, the firm can ascertain the value of a particular asset on a give date. Real accounts can be of the following two types.

(i) **Tangible Real Accounts:** These are accounts of such things which can be touched or felt, measured etc, for example, land, building, plant, machinery, cash, stock etc.

(ii) **Intangible Real Accounts:** These are accounts of such things which cannot be touched in the physical sense but can of course be measured in monetary terms such as goodwill, trade marks, patent rights etc.

1.6.3 Nominal Accounts

These are the accounts of expenses or losses and incomes and gains. These accounts are in name only and are also called as fictitious accounts, for e.g., wages account, salary account, rent account, interest account, commission account, discount account , insurance premium account, etc. The different types of accounts can be understood easily with the help of the following diagram.



1.7 Rules of Debit and Credit

Every business enterprise enters into a large number of transactions. These transactions are recorded in the books of accounts as per the rules of the system of double entry. According to double entry system, every transaction has two aspects. One aspect is the receiving or incoming aspect, also known as debit aspect. Another aspect is the giving or outgoing aspect, also known as the credit aspect. The debit and credit aspects form the basis of double entry system. There are two approaches for deciding when to debit an account and when to credit it.

(i) English Approach

(ii) American Approach.

1.7.1 English Approach

According to this approach there are three types of accounts – personal, real and nominal – as discussed under section 1.6 and there are three rules for recording transactions in them. These rules are as follows.

(i) For Personal Account: debit the receiver and credit the giver.

(ii) For Real Account : debit what comes in and credit what goes out.

(iii) For Nominal Account: debit all expenses and losses and credit all incomes and gains.

Rule for Personal Accounts: Suppose Ashok gives Rs 50,000/- to the business then it is said that he has some honour or reputation in the eyes of the business. His account, therefore, will be credited by Rs 50,000/

The word credit has been derived from the Latin word 'creder' which means to 'believe'. Now suppose Vanshaj received Rs 30,000/- from the business then it is clear that he owes Rs 30,000/- to the business. Therefore Vanshaj's account will be debited by Rs 30,000/-. The word debit has been derived from the Latin word *debere* which means 'to owe'. Thus from this example a simple rule can be derived – debit that person's account who received something from the business and credit that person's account who gives something to the business.

Rule for Real Accounts: Similarly, if the storekeeper of the business has received furniture, machinery, goods or some other real thing, then, in accordance with the above rule, storekeeper is the receiver and his account should be debited. But the storekeeper acts on behalf of the business and does not owe any amount to the business. Therefore, instead of debiting his personal account the account representing the thing is debited. A simple rule can thus be derived that in case of real things "debit what comes into the business and credit what goes out of the business".

Rules for Expenses and Incomes: Let us look at one more situation. Suppose the cashier pays salary to the employee Sohan of the enterprise. Then, as per the second rule, the cashier is not the giver of cash, he paid cash on behalf of the firm, therefore, instead of his account the cash account of the bussines will be credited. Further, the account of employee Sohan who has received salary should be debited but this would mean that Sohan is a debtor whereas actually he is not. Thus instead of debiting Sohan's account the expense on account of which cash has been paid will be debited. In this case the salary account will be debited. Similarly, when interest is received by the cashier the cash account (instead of cashier's account) will be debited and interest account will be credited instead of the persons account who paid it. We can thus derive a simple rule – debit all expenses and losses and credit all incomes and gains.

1.7.2 American Approach

According to this approach, in order to understand the rules of debit and credit, transactions are divided into the following five categories.

(i) Transactions relating to owner, e.g. capital.

(ii) Transactions relating to other liabilities, e.g. supplier of goods, bankers etc.

(iii) Transactions relating to assets, e.g. land, building, plant, machinery, cash, goodwill, trade marks etc.

(iv) Transactions relating to expenses, e.g. wages, salaries, commission, discount, purchase of goods.

(v) Transactions relating to revenues, e.g. sale of goods, interest received, dividend received, rent received etc.

The rules of debit and credit in relation to these accounts are given below.

- **For capital account:** Debit means decrease and credit means increase. This means that if by a transaction the capital of the proprietor increases, for e.g., introduction of capital, profit of the year etc., the capital account will be credited and if the capital decreases, for e.g., withdrawal of capital, loss of the year on any capital account will be debited.

- **For any liability account:** Increase in liability means credit and decrease in liability means debit. This means that if because of a transaction there is increase in a liability than liability account will be credited and if there is decrease in liability than that concerned liability account will be debited.

- **For any asset account:** Debit means increase and credit means decrease. This means that if due to a transaction there is increase in the value of an asset than the concerned asset account will be debited and if there is decrease in the value of an asset than the concerned asset account will be credited.

- **For any expense account:** Increase means debit and decrease means credit. This means that if by a transaction there is increase in the account of expense the expense account is debited and if there is decrease than expense account will be credited.

- **For any revenue account:** Debit means decrease and credit means increase. Thus means that if by transactions, the total of the revenue decreases then the concerned revenue account will be debited and if the amount of revenue increases then the concerned revenue accout will be credited.

These rules can be easily understood with the help of the following table.

Name of the Account	Debit	Credit
Capital	Decrease	Increase
Liability	Decrease	Increase
Assets	Increase	Decrease
Expense	Increase	Decrease
Revenue	Decrease	Increase

It may be noted that both, English and American, approaches give the same conclusion. For example, if a plant has been purchased by the enterprise the plant account will be debited. As per the English Approach, plant has been classified as a 'real thing' and the real account is debited when that 'thing' comes into the business. As per the American Approach, plant has been classified as an 'asset' and increase in asset is debited.

1.8 Importance of Accounting

Accounting is important as it provides information to interested users, helping them to make business decisions. The information contained in Income Statements and Position Statements is the outcome of accounting and is of great importance for external users. Besides this, accounting serves the internal users by providing additional information for business records.

Thus accounting is necessary for

- **Maintenance of business records:** Human memory is not adequately programmed to remember business operations. Business executives need not strain their memory if proper and complete businessrecords are kept. Proper records facilitate the process of decision-making.

- **Assistance in planning and decision-making:** Accounting assists the management in planning business activities for future and taking decisions like whether certain goods should be purchased from the open market and which goods should be manufactured. It also helps in controlling the business activities according to the time schedule and production targets.

- **Assessment of business results:** The main purpose of business is to earn profits. Accounting gives information about the profit and loss made by the business at the end of a year. The same is calculated by deducting expenses from associated revenues. Profit is crucial to the business information for the owner, managers and others.

- **Depiction of financial positions:** The position statement or balance sheet gives the financial position of the business by listing assets (possessed resources) and matching them with liabilities (claims) and capital (owner's equity). It evaluates the strengths and weaknesses of the business and its financial position in general. It also helps at the time of sale of assets in the realisation of reasonable prices.

- **Prevention of misuse of business properties:** Accounting provides protection to business properties from unjustified and unwarranted use. It also supplies up-to-date information of funds, payables, cash and bank balances etc. and helps the proprietors or managers in assuring that the funds of business are not unnecessarily kept idle or underutilised.
- **Realisation of debt:** Accounting proves useful in realising debt from other persons. The businessman can produce his accounting books in a court of law as a proof of debt.
- **Assistance in payment of taxes:** These days many types of taxes like income tax, sales tax, excise duty etc. are imposed upon business. Properly maintained accounts are important for accurate computation of taxes and their payment without any difficulty.
- **Proof in court of law:** When business accounts are kept according to the principles of accounting, they can be presented in a court of law for giving necessary documentary evidence at the time of disputes with suppliers, fellow businessmen, taxation authorities etc.

1.9 Role of Accountant

In recent years, evolution of complex and giant establishments has brought a remarkable change in the field of accounting. Large-scale enterprises have increased the responsibilities of accountants, they are now required to have a higher level of knowledge, conceptual understanding and analytical skills. The role of accountants in modern times is as under.

- **Protectors of business properties:** Accountants have to devise a system of records by which the assets of business are not put to any unjustified and unwarranted use.
- **Summarizers of information:** Accountants study a mass of data of an enterprise through measurement, classification and summarization and reduce it into reports, statements etc., to show the financial condition and results of the business operations effectively.
- **Communicators of business information:** Accountants have to collect and communicate economic information of the enterprise to a wide variety of interested persons according to their needs and levels of understanding.
- **Analysers and interpreters:** Recording of transactions is now the secondary function of accountants; their primary function is to analyse and interpret the business results.
- **Financial advisors:** The role of accountants these days is not only of a book-keeper and auditor but they also have to assume the responsibilities of financial advisor and guide to the management on financial matters and assist them in taking right decisions at the right time.
- **Legal advisors:** Accountants have to assume the responsibilities of filing various statements like income-tax returns, sales-tax papers etc., with different government authorities and assist in correct and timely payment of taxes. They have to fulfill all legal requirements of the business.

Accounting has now become a profession and the role of accountants has changed from that of a mere recorder of transactions to that of a member of the decision - making team in the management of business.

Key Terms Introduced in the Chapter

1.	Transaction	2.	Events
3.	Equity	4.	Debt
5.	Revenue	6.	Expenditure
7.	Expense	8.	Royalty
9.	Cost of goods sold	10.	Merchandise
11.	Concern	12.	Convention

Summary with reference to Learning Objectives

1. **Meaning of Accounting** - Accounting is the process of identifying, measuring and communicating economic information to permit informed judgements and decisions by users of the information.
2. **External Users of Accounting Information** - Investors, creditors, government, consumers.
3. **Internal Users of Accounting Information** - Owners, management, employees.
4. **GAAP** - Generally Accepted Accounting Principles.
5. **Accounting Concepts** - Separate entity concept, Going concern concept, Money measurement concept, Accounting period concept, Dual aspect concept or Accounting equation concept, Accrual concept, Matching concept.
6. **Accounting Conventions** - Revenue recognition convention, Full disclosure convention, conservation convention or prudence.
7. **Double Entry System** - Under this system both the aspects of a financial transaction are recorded.
8. **AICPA** - The American Institute of certified Public Accountants.
9. **AAA** - The American Accounting Associations.
10. **Accounting Equation** - Capital (+) Liabilities = Assets
11. **Personal Accounts** - These are made up of natural person's account, artificial person's account and representative personal account.
12. **Real Accounts** - It consists of tangible and intangible real accounts.
13. **Nominal Accounts** - It consists of income and expense accounts.

Questions for Practice

Short Answer questions

1. Define Accounting.
2. Who are the internal and external users of information?
3. Give any three examples of revenues.
4. Give the meaning of expenditure and expense.
5. State the different types of accounting.
6. State the types of accounts as per the English approach.
7. What are the general rules of revenue recognition?
8. Define the matching principle.
9. What are the rules of debiting and crediting of accounts as per the English approach?
10. What are the rules of debiting and crediting of accounts as per the American approach?

Long Answer questions

1. Explain the following terms

(i) Financial Transaction	(ii) Assets	(iii) Liabilities
(iv) Revenue	(v) Debtors	(vi) Creditors

2. Explain the role of accounting in the modern world.
3. Who are the external users of accounting information? Discuss.
4. Explain the following concepts.
   (i) Separate entity concept
   (ii) Going concern concept
   (iii) Money measurement concept
   (iv) Dual aspect concept
   (v) Full disclosure convention
   (vi) Conservatism convention
5. What are the different branches of Accounting? Explain.

CHAPTER 2

Recording of Transactions

Learning Objectives

After studying this chapter you will be able to

- understand the meaning of books of original entry
- record the transactions in the journal
- record the transactions in single, double and triple column cash book
- prepare a petty cash book
- understand the meaning, utility and format of ledger
- record the transactions in day books
- explain the posting of transactions from journal, cash book and day books into the ledger
- explain the concept of balancing of ledger accounts.

In Chapter 1 we discussed the meaning and importance of accounting, the basic terms used in accounting, the generally accepted accounting principles, the classification of accounts and the rules of debit and credit. It was also stated that accounting is the art of identifying, analysing and recording of the business transaction, classifying and summarizing their effects, and finally communicating it to the interested users of the accounting information.

In the present chapter, we will discuss the recording of transactions in the books of original entry, i.e. the journal, cash book and different day books, and the posting of these transactions from these books of original entry to the ledger which is the principle book, and also the balancing of the ledger accounts.

2.1 Books of Original Entry

The books of accounts where in transactions are recorded for the first time from a source document are called 'Books of Original Entry'. A document which provides evidence of the transactions is called a source document or voucher,for e.g. cash memo, invoice, sales bills, pay-in-slips, cheques, salary slips, debit notes, credit notes, receipts etc. We will discuss about vouchers in greater detail in Chapter 4. Journal is one of the basic books of original entry in which transactions are originally recorded in a chronological order, i.e. one after the other in order of their happening according to the principles of double entry system. When the size of the business is small then all its transactions can be recorded in a single journal. But as the size of the business grows, it no longer remains possible to record all the transactions in a single journal. In such a situation more than one journal may be used - each such journal is called a sub-journal. A particular type of transaction may be recorded in a sub-journal, or subsidiary book, for e.g., all credit purchases of goods may be recorded in one journal called the purchases book and all credit sales of goods may be recorded in another sub-journal called sales day book. These journals are called as 'Special purpose subsidiary books' or 'books of original entry'. The important types of subsidiary books are Cash Book, Purchases Book

Sales Book, Purchases Return Book, Sales Return Book, Bills Receivable Book, Bills Payable Book and Journal Proper.

These books are called books of original entry because transactions are first of all recorded in these books. An enterprise need not maintain all of the above books - it may maintain any of the above books, according to its needs and requirements.

2.2. Journal

Journal is the basic book of original entry. Transactions in the journal are recorded in chronological order, i.e., the transaction which happened first followed by the next transaction and so on. The journal provides a date-wise record of all the transactions with details of the amounts debited and credited and the amount of each transaction. The format of the journal is given below

JOURNAL

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

Maintenance of the different columns of the journal has been discussed below.

(i) **Date:** The first column in the journal is the date column. In this column the date on which the transaction took place is entered. The year and month is written only once till they change. First the year of the transaction is written followed by the month and lastly the date of the transaction is entered.

(ii) **Particular:** In the 'particular' column, the particulars of the transactions are recorded. We know that every transaction affects at least two accounts - one account is debited and the other account is credited. First the account to be debited is identified and the name of this account is recorded in the particulars column. After writing the name of the account to be debited in the first line in the particular column, in the second line we write the name of the account which is to be credited after its identification. Some space is to be left before we start writing the second line. This is done just to clearly distinguish between the account(s) to be debited and the account(s) to be credited. The word 'To' is prefixed to the name of the account to be credited. After writing the names of the accounts to be debited and credited a small explanation of the transaction called 'Narration' is written. Narration explains the reasons for the happening of the transactions. A line is drawn after the narration which touches both the date column on the one hand and ledger folio column on the other hand indicating that the recording of the transaction is completed.

(iii) **Ledge Folio or L.F. :** All entries from the journal are posted in the ledger which contains different accounts. In the L.F. column the folio number of the ledger where the posting has been done is recorded. For example, suppose the 'Machinery Account' in ledger appears at folio number 151, if by a journal entry Machinery Account has been debited than 151 will be written in the L.F. column against Machinery Account which will indicate that this transaction has been debited at folio number 151 in the ledger where 'Machinery Account' exists.

(iv) **Debit Amount Column:** In this column the amount of account being debited is written.

(v) **Credit amount Column:** In this column the amount of account being credited is written.

The process of recording the transactions in the journal is called journalisation and recording a single transaction is called journal entry. Journal entry is the basic record of a business transaction. When only two accounts are involved in recording a transaction then the entry is called a simple journal entry, and when more than two accounts are involved in recording a transaction than the entry is called a compound journal entry.

2.2.1 Steps in Journalising: The following steps may be taken for recording the transactions in the journal.

(i) Read the transaction carefully and identify the two aspects of the accounts which are affected by the transaction.

(ii) Find the category to which these accounts belong i.e. Personal, Real or Nominal.

(iii) Recall the rules of debit and credit and decide which rules will be applicable on these accounts. Here we must remember that every rule has two parts, i.e. - one debit part and the other credit part, for e.g., the rule for personal accounts is, 'Debit the receiver and credit the giver'. In this rule the first part states that if a person receives money, or something measurable in money, than his account should be debited whereas the second part of the rule states that if the person gives money or money's worth to the business than his account should be credited. Therefore, after identifying the rule which will be applicable we have to identify that part of the rule which will be applicable. This will help us in deciding whether the concerned account will be debited or credited.

(iv) In the date column write the year, month and date on which the transaction took place.

(v) In the particulars column first write the name of the account which has to be debited and then the word 'Dr' against it. The amount by which the account is to be debited will be written against this account in the 'Debit Amount' column.

(vi) Then before writing the next line leave some space and write the name of the account which is to be credited prefixed with the word 'To'. Against this account in the 'Credit Amount column' write the amount by which the account is to be credited.

vi) Now in the particulars column write the narration of the transaction which should be a brief explanation of the transaction.

(viii) After writing the explanation of the transaction, a line is drawn in the particulars column which separates the preceeding entry from the succeeding entry. In this way all transactions are recorded one after the other in chronological order in the journal. Once a page is complete the totals of both the columns, 'debit amount column' and 'credit amount column', are done and against these totals the word's 'balance carried forward' or 'balance C/F' are written. It must be noted that the totals of both the columns must be the same because totals of debits are always equal to totals of credits. Before recording the transactions in the next column, first, totals of the previous page are written in both the 'debit amount column' and the 'credit amount column' as 'Balance brought forward' or 'Balance b/f'.

Transaction1. Mahesh started business on 1.4.2007 with capital Rs 5,00,000.

Analysis of Transaction: This transaction affects Mahesh's capital account and cash account. Capital account is the proprietor's personal account and the rule 'Debit the receiver and credit the giver' will be applicable. Since Mahesh is the giver his capital account will be credited. Cash account is real account hence the rule 'Debit what comes in and credit what goes out' will be applicable. Since cash is coming into the business, cash account will be debited. Therefore, the journal entry for this transaction will be

		Rs.	Rs.
Cash Account	Dr	5,00,000	
To Mahesh's Capital Account (Mahesh started business with cash)			5,00,000

Transaction 2. April I 2007. He opened a savings bank account with State Bank of India with Rs 3,00,000.

Analysis of Transaction: The two accounts affected by this transaction are cash account and bank account. Cash a/c is real a/c and bank a/c is personal a/c The rule for real accounts is 'Debit what comes in and credit what goes out'. As bank is receiver of money, Bank account will be debited. Since cash from the business is going out cash account will be credited. Therefore, the journal entry will be

	Rs.	Rs.
Bank Account……………..Dr	3,00,000	
to Cash Account (deposited cash into bank)		3,00,000

Transaction 3. April 3, 2007. He purchased goods from Bhola Nath on Credit for Rs. 50,000.

Analysis of Transaction: The two accounts affected by the transaction are 'purchases account' and Bhola Nath's account. Purchases are expenses, hence, the rule 'debit all expenses and losses and credit all incomes and gains' will be applicable and 'Purchases Account' will be debited. Bhola Nath's account is a personal account, therefore, the rule 'Debit the receiver and Credit the giver' will be applicable. Since Bhola Nath is the supplier or giver of the goods to the business, therefore, his account will be credited. The journal entry will be as follows.

	Rs.	Rs.
Purchases Account……………..Dr	50,000	
To Bhola Nath's Account (purchased goods from Bhola Nath)		50,000

Transaction 4. April 4. 2007. He purchased goods from Ashraf and paid him by cheque Rs. 10,000**.**

Analysis of Transaction: The two accounts affected by this transaction are purchases account and bank account. It should be noted here that the transaction will not affect Ashraf's account because payment has been made simultaneously with purchase of goods therefore it is not credit purchase. Purchases account is an expense account, therefore, the rule 'debit all expenses and losses and credit all incomes and gains will be used here. Since purchases are expenses, purchases account will be debited. The second account affected is bank account. Cash at bank is an asset, therefore, the rule for real accounts i.e. 'debit what comes in and credit what goes out' is applicable. Since cash from the bank is going out, bank account will be credited. The transaction will be recorded as follows

	Rs.	Rs.
Purchases Account……………..Dr	10,000	
To Bank Account (purchased goods and paid by cheque)		10,000

Transaction 5. April 5. 2007. Mahesh purchased furniture for Cash Rs 7500.

Analysis of Transaction: The two accounts affected by the transaction are 'Furniture Account' and 'Cash Account'. Both are real accounts. Therefore, the rule 'debit what comes in and credit what goes out' will be applied. Since furniture is coming into the business furniture account will be debited, and cash is going out so cash account will be credited. The transaction will be recorded as follows.

	Rs.	Rs.
Furniture Account……………..Dr	7,500	
To Cash Account (purchased furniture for cash)		7,500

Transaction 6. April 6, 2007. He sold goods for cash to Vijay, Rs 12,500.

Analysis of Transaction: Since goods have been sold for cash the two accounts affected by the transaction will be 'cash account' and 'sales account'. When goods are sold for cash, buyer's account is not affected. Cash account is a real account, therefore, the rule 'debit what comes in and credit what goes out' will be applicable. As cash is coming into the business cash account will be debited. Sales is an income, hence, the rule 'debit all expenses and losses and credit all incomes and gains' will be applied, therefore, sales account will be credited. The transaction will be journalised as follows.

	Rs.	Rs.
Cash Account……………..Dr	12,500	
to Sales Account (sold goods for cash)		12,500

Transaction 7. April 9, 2007. Sold goods to Ravi Rs 8,000.

Analysis of Transaction: The two accounts affected by the transaction are Ravi's account and 'sales account'. Ravi's account is a personal account, therefore, the rule for personal accounts i.e. 'debit the receiver and credit the giver' will be applicable. Since Ravi is the receiver of goods from the business his account will be debited. Sales is an income. Therefore, the rule 'debit all expenses and losses and credit all incomes and gains' will be applied. As sales is an income sales account will be credited. The transaction will be journalised as follows.

	Rs.	Rs.
Ravi's Account……………..Dr	8,000	
To Sales Account (Sold goods to Ravi)		8,000

Transaction 8. April 10, 2007. Paid by cheque to Bholanath Rs 49,500 and he allowed discount Rs. 500.

Analysis of Transaction: Here the accounts affected by the transaction will be Bhola Nath's account, bank account and discount account. Bhola Nath's account is a personal account, therefore, the rule for personal accounts will be applied. Since Bhola Nath is the receiver, his account will be debited. Cash from bank is going out, therefore, bank account will be credited. Bhola Nath allowed a discount of Rs 500. This means that the business received a discount of Rs 500. Discount received is an income, therefore, discount account will be credited. The transaction will be journalised as follows

	Rs.	Rs.
Bhola Nath's Account……………..Dr	50,000	
To Bank Account		49,500
To Discount Account		500
(paid Bhola Nath and he allowed discount)		

Transaction 9. April 15, 2007. Received cash from Ravi Rs 14,400 and discount allowed to him Rs 100.

Analysis of Transaction: The accounts affected by the transactions are cash account, discount account and Ravi's account. Cash account is a real account and since cash is being received this account will be debited. Discount account is a nominal account. Discount received is an expense, therefore, discount account will be debited. Ravi's account is a personal account. Ravi is paying cash to the business. Therefore, his account will be credited. The transaction will be journalised as follows.

	Rs.	Rs.
Cash Account……………..Dr	12,400	
Discount Account……. Dr	100	
To Ravi's Account		12,500
(received cash from Ravi and discount allowed to him)		

Note: Since more that two accounts have been affected by the transaction, this entry will be called as 'Compound Entry'.

Transaction 10. April 30, 2007. Paid Rent Rs 5,000, Paid Salary Rs 10,000 by cheque.

Analysis of Transaction: The accounts affected by the transactions are rent account, salary account and bank account. Rent account and salary account are nominal accounts and since these are expenses, these accounts will be debited. Bank account is a personal a/c. Payment by cheques reduces the bank balance, therefore, bank account will be credited. The transaction will be journalised as follows.

	Rs.	Rs.
Rent Account……………..Dr	5,000	
Salary Account …………Dr	10,000	
to Bank Account		15,000
(paid rent and salary by cheques)		

Transaction 11. April 30, 2007. Wages outstanding Rs 7000.

Analysis of Transaction: This transaction will affect two accounts, wages account and outstanding wages account. Wages account is a nominal account. Since wages are an expense, wages account will be debited. Outstanding wages account is a representative personal account. The worker who has provided (sold) his labour has become due for payment. Since the worker is the giver, his account will be credited. The transaction will be journalised as follows.

	Rs.	Rs.
Wages Account……………..Dr	7,000	
To Outstanding wages Account (outstanding wages)		7,000

Transaction 12 April 30, 2007. Paid Insurance Premium in advance Rs 4,000.

Analysis of Transaction: The two accounts affected by the transactions are pre-paid insurance account and cash account. Pre-paid insurance account is a representative personal account since the insurance company is being paid before the service provided by it, hence its account, or pre-paid insurance account, will be debited. Cash account is a real account. Since cash is going out cash account will be credited. The transaction will be journalised as follows.

	Rs.	Rs.
Pre-paid Insurance Premium Account………Dr	4,000	
To Cash A/c (paid insurance premium in advance)		4,000

The above discussed transactions have been shown in the proper format of the journal as follows

MAHESH'S JOURNAL

Date	Particulars	L.F.	Debit Amount Rs.	Credit Amount Rs.
2007 April 1	Cash A/c…………………………….....…Dr. To Mahesh's Capital A/c (Started business with Cash) Balance C/F		5,00,000	 5,00,000
April 1	Bank A/c…………………………......…Dr. To Cash A/c (Deposited Cash into bank)		3,00,000	 3,00,000
April 3	Purchases A/c…………………………Dr. To Bhola Nath's A/c (Purchased goods from Bhola Nath)		50,000	 50,000
April 4	Purchase A/c…………………….……Dr. To Bank A/c (Purchased goods and paid by cheques)		10,000	 10,000

April 6	Furniture A/c.................................Dr. To Cash A/c (purchased furniture for cash)		7,500	 7,500
April 7	Cash A/c.....................................Dr. To Sales A/c (sold goods for cash)		12,500	 12,500
April 9	Ravi's A/c.................................. ....Dr. To Sales A/c (sold goods to Ravi)		8,000	 8,000
April 10	Bhola Nath A/c..............................Dr. To Bank A/c To Discount A/c (paid Bhola Nath and he allowed discount)		50,000	 49,500 500
2007 April 15	Cash A/c......................................Dr. Discount A/c................................Dr. To Ravi's A/c (received Cash from Ravi and allowed him discount)		12,400 100	 12,500
April 30	Rent A/c.......................................Dr. Salary A/c....................................Dr. To Bank A/c (paid rent and salary by cheques)		5,000 10,000	 15,000
April 30	Wages A/c.....................................Dr. To outstanding wages A/C (outstanding wages)		7,500	 7,500
April 30	Pre-paid Insurance Premium A/c........Dr. To Cash (paid insurance premium in advance)		4,000	 4,000
	Total		**9,77,000**	**9,77,000**

Illustration 1. Journalise the following transactions in the books of Subash Chander.

2007

April 1. Started business with Cash Rs. 7,00,000, Furniture worth Rs. 1,00,000 and Machinery worth Rs. 2,00,000.

" 2. Deposited Rs. 3,00,000 in bank.

" 3. Purchased goods from Vikram for Rs. 15,000 and from Sharma for Rs. 7,500.

" 4. Goods returned to Sharma worth Rs. 1000 since the same were not as per the sample.

" 5. Sold goods for cash worth Rs. 8,000.

" 6. Sold goods to Kiran worth Rs. 8,900.

" 7. Damanged goods returned by Kiran worth Rs. 900.

" 8. Purchased goods at list price for Rs. 18,000 from Rao at a trade discount of 10%.

" 9. Sold goods at list price of Rs. 6,000 to Sunil at a trade discount of 5%.

” 10. Received Rs. 6,000 from Kiran on account.
” 11. Paid to Vikram by cheque Rs. 14,900 and he allowed discount of Rs. 100.
‘ 12. Paid to Sharma Rs. 6450 in full settlement of his account.
” 13. Paid for repair of furniture Rs. 700.
” 14. Paid for insurance of machinery Rs.1,000.
” 15. Sold goods for Cash worth Rs. 3,400.
” 16. Purchased goods from Hari for Rs. 13,500.
” 17. Received from Sunil the full amount due to him.
” 18. Kiran became insoluent and a final payment of 50 paise in a rupee was received from her official receiver.
” 19. Paid wages Rs. 3,400.
” 20. Withdrew cash for personal use Rs. 5,000.
” 21. Depisited cash into bank Rs. 1,50,000.
” 22. Paid to Hari Rs. 10,000 on account.
” 23. Paid for petty expenses Rs. 200.
” 24. Paid trade expenses of Rs. 800.
” 25. Paid commission Rs. 1,200.
” 26. Withdrew goods of the cost price of Rs. 900 for personal use.
” 27. Withdrew cash from bank Rs. 5,000.
” 28. Purchased goods for cash Rs. 17,000.
” 29. Sold goods for cash Rs. 13,500.
” 30. Paid rent of Rs. 10,000 and salary, Rs. 28,000.

SUBASH CHANDER

JOURNAL

Date	Particulars	L.F.	Debit Amount Rs.	Credit Amount Rs.
2007				
April 1	Cash A/c..................................Dr.		7,00,000	
	Furniture A/c..............................Dr.		1,00,000	
	Machinery A/c.............................Dr		2,00,000	
	To Capital A/c			10,00,000
	(Started business)			
April 2	Bank A/c..................................Dr.		3,00,000	
	To Cash A/c			3,00,000
	(Deposited into bank)			
April 3	Purchases A/c.............................Dr.		22,500	
	To Vikram's A/c			15,000
	To Sharma's A/c			7,500
	(Purchased goods)			

April 4	Sharma's A/c...............................Dr. To Returns Outwards (Returned goods to Sharma)		1,000	 1,000
April 5	Cash A/c...................................Dr. To Sales (Sold goods for cash)		8,000	 8,000
April 6	Kiran's A/c................................Dr. To Sales A/c (Sold goods for cash)		8,900	 8,900
April 7	Returns Inward A/c..................... Dr. To Kiran A/c (Damaged goods returned by Kiran)		900	 900
April 8	Purchases A/c.............................Dr. To Rao (Purchased goods from Rao at 10% trade discount)		16,200	 16,200
April 9	Sunil's A/c.................................Dr. To Sales's A/c (Sold goods to Sunil at 5% Trade discount)		5,700	 5,700
April 10	Cash A/c...................................Dr. To Kiran A/c (Received from Kiran on account)		6,000	 6,000
April 11	Vikram's A/c...............................Dr. To Bank A/C To discount A/c (Paid to Vikram and he allowed discount)		15,000	 14,900 100
April 12	Sharma's A/c...............................Dr. To Cash To Discount (Paid to Sharma in full settlement)		6,500	 6,450 50
April 13	Repairs A/c.................................Dr. To Cash A/c (Paid for repair of furniture)		700	 700
April 14	Insurance for Machinery A/c...............Dr. To Cash (Paid for insurance of machinery)		 1,000	 1,000
April 15	Cash A/c...................................Dr. To Sales A/c (Sold goods for cash)		3,400	 3,400
April 16	Purchases A/c.............................Dr. To Hari's A/c (Purchased goods from Hari)		13,500	 13,500

April 17	Cash A/c..Dr. To Sunil's A/c (Received the full amount due from Sunil)		5,700	 5,700
April 18	Cash A/c..Dr. Bad Debts.......................................Dr. To Kiran A/c (Received 50 paise in a rupee from the official receiver of Kiran on her becoming insolvent and the balance will be bad debts)		1,000 1,000	 2,000
April 19	Wages A/c..Dr. To Cash (Paid wages)		3,400	 3,400
April 20	Drawing's A/c...................................Dr. To Cash (Withdrew cash for personal use)		5,000	 5,000
April 21	Bank A/c..Dr. To Cash A/c (Deposited cash into bank)		1,50,000	 1,50,000
April 22	Hari's A/c...Dr. To Cash A/c (Paid to Hari on account)		10000	 10000
April 23	Petty Expenses A/c...........................Dr. To Cash A/c (Paid petty expenses)		200	 200
April 24	Trade Expenses A/c...........................Dr. To Cash (Paid trade expenses)		800	 800
April 25	Commission A/c...............................Dr. To Cash (Paid commission)		1,200	 1,200
April 26	Drawings A/c....................................Dr. To Purchase A/c (Withdrew goods for personal use)		900	 900
April 27	Cash A/c..Dr. To Bank (Withdrew cash from bank)		5,000	 5,000
April 28	Purchase A/c...................................Dr. To cash (Purchased goods)		1,700	 1,700
April 29	Cash A/c..Dr. To cash A/c (Cash sales)		13,500	 13,500

April 30	Rent A/c.................................Dr. Salary A/c.................................Dr. To Cash (Paid Rent and Salary)		10,000 28,000	 38,000
	Total		**16,62,500**	**16,62,500**

2.3 Ledger

Ledger is the principal book of the accounting system. You know that all business transactions are recorded separately and date-wise in the journal in chronological order. The transactions pertaining to a particular person, asset, expense or income are recorded at different places in the journal as they occur on different dates. Hence, with the help of journal, it is not possible to bring the similar transactions together at one place. Thus, to have a consolidated view of similar transactions pertaining to a particular person, asset, expense or income, a ledger is used. In a ledger different accounts are prepared item-wise. A ledger account can be defined as a summary statement of all transactions relating to a person, asset, expense or income which have taken place during a given period of time and shows their net effect.

A ledger may be in the form of a bound register or loose leaf forms printed on paper or cards. The bound register is inflexible in that new accounts or additional space for old accounts must be placed where blank pages are available, whereas, loose-leaf ledger is more flexible in the sense that it permits rearrangement of the accounts and, if required, new accounts may be placed where desired and additional space may be provided to an account merely by inserting a new sheet alongwith the old. For easy posting and location accounts are opened in the ledger in a certain order. For example, the accounts in the ledger may be opened in the same order in which they appear in the final accounts. An index of various accounts opened in the ledger is given in the beginning for the purpose of easy reference. For easy identification, each account may also be allotted a code number if the organisation is big and the number of accounts are large. A ledger is called the principal book of accounts because it helps in achieving the objectives of accounting by providing the following types of information.

- The total sales to an individual customer
- The total purchases from an individual supplier
- How much amount is to be paid to others?
- How much amount is to be received from others?
- What is the position of different assets of the business?
- What is the amount of profit earned of loss suffered during a particular period?

Following is the format of a ledger account.

NAME OF ACCOUNT

Dr. Cr.

Date	Particulars	J.F	Amount Rs.	Date	Particulars	J.F.	Amount Rs.
	To Name of Credit Account				By Name of Debit Account		

As shown above, each account in the ledger is divided into two equal parts by a vertical line. The left hand side of the account is known as the 'debit side' and the right hand side is known as the 'credit side'. Each of the two sides is further divided into four columns of date, particulars, folio and amount. 'F' stands for the folio or page number of the journal from where posting has been made in the ledger.

2.3.1 Ledger Posting

The process of transferring the transactions from the journal and subsidiary books to the ledger is called posting. It results in the grouping of all transactions in respect of an account at one place for meaningful conclusion and to further the accounting process. The following are the guiding rules for posting transactions in the ledger.

i) In the date column the date of the transaction is recorded.

ii) Posting to the debit side of the account that has been debited by the journal entry is done in the ledger by writing the name of the account in the particulars column which has been credited. The amount by which the account has been debited is written in the amount column.

iii) Posting to the credit side of the account that has been credited by the journal entry is done in the ledger by writing the name of the account in the particulars column which has been debited. The amount by which the account has been credited is written in the amount column.

iv) The word 'To' may be suffixed before writing the name of account in the particulars column on the debit side. Similarly, the word 'By' is suffixed before writing the name of the account in the particulars column on the credit side.

v) In the folio column 'J.F.' the page number of the journal from where the entry is posted to ledger account is written.

This has been explaned with the help of the following examples.

Transaction. April 10, 2007. Sold goods for cash Rs. 7,400.

The journal entry will be as follows.

NAME OF ACCOUNT

Dr. Cr.

Date	Particulars	L.F.	Debit Amount Rs.	Credit Amount Rs.
2007 April 10	Cash A/c..................................Dr. To sales A/c (Sold goods for Cash)		7,400	 7,400

Two accounts which have been affected by this transaction are cash account and sales account. Cash account has been debited and sales account has been credited, therefore, at the time of ledger posting this transaction will be posted in cash account and sales account. Since cash account has been debited by the journal entry it will be posted to the debit side of the cash account. Sales account has been credited by the journal entry, therefore, while doing ledger posting in sales account it will be posted on the credit side of the sales account. The ledger posting in cash account and sales account has been shown as follows.

CASH ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 April 10	To Sales A/c		7,500				

SALES ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 April 10					By Cash A/c		7,400

It must be noted that a transaction is posted in as many accounts as are affected by it. By a simple journal entry two accounts are affected, therefore, the posting is done in two accounts as shown by the above example. Since more than two accounts are affected by a compound entry, therefore, posting for it will be done in more than two accounts. This has been shown with the help of the following example.

Transaction. April 30, 2007. Paid Salary Rs. 10,000; Wages Rs. 3,000; Commission Rs. 500; Charity Rs.501.

JOURNAL

Date	Particulars	L.F.	Debit Amount Rs.	Credit Amount Rs.
2007 April 30	Salary A/c................................Dr.		10,000	
	Wages A/c................................Dr.		3,000	
	Commission A/c..........................Dr.		500	
	Charity A/c................................Dr.		501	
	To Cash A/c			
	(Paid salary, wages, commission and charity)			14,001

SALARY ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 April 30	To Cash		10,000				

WAGES ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 April 30	To Cash A/c		3,000				

COMMISSION ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 April 31	To Cash A/c		500				

CHARITY ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 April 31	To Cash A/c		501				

Illustration 2. Pass journal entries for the following transactions and post them into the ledger.

2007		Rs.
Jan. 1.	Prakash started business with cash	10,00,000
Jan 3.	Purchased furniture for cash	70,000
Jan 4.	Purchased goods for cash	30,000
Jan 7.	Purchased goods from Sita Traders, Raja Bros	10,000 18,000
Jan 10.	Returned goods to Sita Traders	800
Jan 12.	Paid cash to Sita Traders in full settlement of their account and they allowed 10% discount.	
Jan 13.	Opened account in State Bank of India	5,00,000
Jan 14.	Paid Raja Bros. by cheques in full settlement of their account.	17,800
Jan 15.	Sold goods for cash	19,000

Jan 16.	Sold goods to Venkat at list price and offered 10% Trade Discount.	8000
Jan 17.	Purchased goods from Jyoti Bros.	3,400
Jan 18.	Sold goods to M/s Swami	14,000
Jan 19.	Received from Venkat by cheques on account	5,000
Jan 20.	Paid for furniture repair	500
Jan 21.	Purchased goods from Rajan	900
Jan 22.	Sold goods to Satish	2,050
Jan 25.	Sold goods to Poonam	4,000
Jan 31.	Paid Rent	5,000
	Salary	4,000

PRAKASH

JOURNAL

Date	Particulars	L.F.	Debit Amount Rs.	Credit Amount Rs.
2007	Cash A/c...............................Dr.		10,00,000	
Jan. 1	To Capital A/c			10,00,000
	(Started business)			
Jan. 3	Furniture A/c...............................Dr.		70,000	
	To Cash A/c			70,000
	(Purchased furniture)			
Jan. 4	Purchases A/c..............................Dr.		30,0000	
	To Cash A/c			30,000
	(Purchased goods for cash)			
Jan. 7	Purchases A/c...............................Dr.		28,000	
	To Sita Traders A/c			10,000
	To Raja Bros.			18,000
	(Purchased goods from Sita Traders & Raja Bros.)			
Jan. 10	Sita Traders A/c...........................Dr.		800	
	To Return outwards			800
	(Returned goods to Sita Traders)			
Jan. 12	Sita Traders A/c...........................Dr.		9,200	
	To Cash			8,280
	To Discount			920
	(Paid cash to Sita Traders in full settlement of their account and they allowed 10% discount)			

Jan. 13	Bank A/c……………………………………Dr. To Cash A/c (Opened bank account)		5,00,000	 5,00,000
Jan. 14	Raja Bros. A/c…………………………………Dr. To Bank To Discount (Paid to Raja Bros. & discount allowed by them)		18,000	 17,800 200
Jan. 15	Cash A/c……………………………………Dr To Sales's A/c (Sold goods)		19,000	 19,000
Jan. 16	Venkat A/c…………………………………Dr. To Sales A/C (Sold goods to Venkat)		7,200	 7,200
Jan. 17	Purchase A/c……………………………...Dr. To Jyoti Bros. (Purchased goods from Jyoti Bros.)		3,400	 3,400
Jan. 18	M/s Swami A/c……………………………..Dr. To Sales A/c (Sold goods to M/s Swami)		14,000	 14,000
Jan. 19	Bank A/c ………………………………Dr. To Venkat A/C (Paid Vanket on account)		5,000	 5,000
Jan. 20	Repair A/c……………………………….Dr. To Cash (Paid for furniture repair)		500	 500
Jan. 21	Purchase A/c………………………………Dr. To Rajan A/c (Purchased goods from Rajan)		9,000	 9,000
Jan. 22	Satish A/c……………………………….Dr. To Sales A/c (Sold goods to Satish)		2,050	 2,050
Jan. 25	Poonam A/c………………………………Dr. To Sales A/c (Sold goods to Poonam)		4,000	 4,000
Jan. 31	Rent A/c…………………………………Dr. Salary A/c………………………………Dr. To Cash A/c (Paid rent and salary)		5,000 4,000	 9,000

CASH ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Jan.1	To Capital A/c		10,00,000	Jan.3	By Furniture		70,000
Jan. 15	To Sales		19,000	Jan.4	By Purchases		30,000
				Jan.12	By Sita Traders		8,280
				Jan.13	By Bank		5,00,000
				Jan.20	By Repair		500
				Jan.31	By Rent		5000
				Jan.31	By Salary		4000

CAPITAL ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007			
				Jan.1	By Cash		10,00,000

FURNITURE ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007	To Cash		70,000				
Jan. 3							

PURCHASE ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Jan.4	To Cash		30,000				
Jan.7	To Sita Traders		10,000				
Jan.7	To Raj Bros.		18,000				
Jan.17	To Jyoti		3,400				
Jan.21	To Rajan		9,000				

SALES ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007			
				Jan.15	By Cash		19,000
				Jan.16	By Venkat		7,200
				Jan.18	By M/s Swami		14,000
				Jan.22	By Satish		2,050
				Jan.25	By Poonam		4000

SITA TRADERS ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Jan.10	To Return outward		800	Jan.07	By Purchases		10,000
Jan.12	To Cash		8,280				
Jan.12	To Discount		920				
	2007						

RAJ BROS. ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Jan.14	To Bank		17,800	Jan.7	By Purchases		18,000
	To Discount		200				

RETURNS OUTWARDS ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007			
				Jan.11	By Sita Traders		800

Dr. **DISCOUNT RECEIVED ACCOUNT** Cr.

Date	Particulars	J.F Rs.	Amount	Date	Particulars	J.F	Amount
2007 Jan.14				Jan.12	By Sita Traders		920
				Jan.14	By Raja Bros.		200

Dr. BANK ACCOUNT Cr.

Date	Particulars	J.F	Amount Rs.	Date	Particulars	J.F	Amount Rs.
2007 Jan.13	To Cash		5,00,000	2007 Jan.14	By Raja Bros.		17,800
	To Venkat		5,000				

Dr. JYOTI ACCOUNT Cr.

Date	Particulars	J.F	Amount Rs.	Date	Particulars	J.F	Amount Rs.
				2007 Jan.17	By Purchases		3,400

Dr. M/S SWAMI ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Jan.18	To Sales		14,000				

Dr. REPAIRS ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Jan.20	To Cash		500				

Dr. RAJAN ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007 Jan.21	By Purchases		9,000

Dr. SATISH ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Jan.22	To Sales		2,050				

Dr. RENT ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Jan.31	To Cash		5,000				

Dr. SALARY ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Jan.31	To Cash		4,000				

Dr. VENKAT ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Jan.16	To Sales		7,200	Jan.19	By Bank		5,000

Dr. POONAM ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Jan.25	To Sales		4,000				

2.3.2 Balancing of Accounts

The ledger accounts are periodically balanced, generally at the end of the accounting period, with the object of ascertaining the net position of each account and for preparing the final accounts. The procedure of balancing accounts is as follows.

(i) Take the total of the two sides of the concerned account.

(ii) Ascertain the difference between the totals of both sides.

(iii) If the debit side is more than the credit side it means the account has a debit balance and the difference is written on the credit side by writing 'By balance c/d' in the particulars column and the amount in the amount column. 'C/d' means 'carried down'. On the other hand, if the credit side is more than the debit side it means that the account has a credit balance and the difference is written on the debit side by writing the words 'To Balance c/d' in the particulars column and the amount in the amount column.

(iv) In the beginning of the next accounting period the 'balance c/d' is posted as 'balance b/d' on the other side as opening balance before posting any other transaction, for e.g., if in an account there is 'By balance c/d Rs. 6,000' then in the beginning of the next accounting period it will be shown as 'To balance b/d', 'Balance c/d' means 'Balance Carried down' and 'Balance b/d' means 'balance brought down'.

Illustration 3. Enter the following transactions in the journal of Jacob and post them into the ledger and balance the ledger accounts.

2007		Rs.
Feb. 1	Started business with cash	90,000
Feb 2.	Paid into Bank	50,000
Feb 3.	Purchased goods for cash	30,000
Feb 5.	Purchased furniture and paid by cheque	10,000
Feb 7.	Sold goods for cash	19,000
Feb 9	Sold goods to A.Khan	8,000
Feb 11.	Purchased goods from R.Rehman	14,000
Feb 14.	Goods returned by A.Khan	400
Feb 17.	Received cash from A.Khan.	7,400
	Discount allowed to him.	200
Feb 22.	Withdrew from bank for personal use,	2,000
	for Office use.	10,000
Feb 24.	Paid telephone bill	1,000
Feb 25.	Paid cash to R.Rahman on account	10,000
Feb 28.	Paid for : Stationery	2,000
	Salary	10,000
	Rent	4,000

JACOB
JOURNAL

Date	Particulars	L.F.	Debit Amount Rs.	Credit Amount Rs.
2007 Feb . 1	Cash A/c……………………...…………Dr. To Capital A/c (Started business)		90,000	 90,000
Feb . 2	Bank A/c…………………….... ………Dr. To Cash (Paid to bank)		50,000	 50,000
Feb . 3	Purchases A/c………………… ..………Dr. To Cash A/c (Purchased goods)		30,000	 30,000
Feb . 5	Furniture A/c………………… ....………Dr. To Bank (Purchased furniture)		10,000	 10,000
Feb . 7	Cash A/c………………… ……....……Dr. To Sales A/c (Sold goods for cash)		19,000	 19,000
Feb . 9	A.Khan A/c…………………… ......……Dr. To sales (Goods sold to A.Khan)		8,000	 8,000
Feb . 11	Purchase A/c…………….. ……...……Dr. To R. Rehamna (Goods purchased from R.Rehman)		14,000	 14,000
Feb . 14	Returned Inwards A/c……...……...…Dr. To A.Khan A/c (Goods returned by A.Khan)		400	 400
Feb . 17	Cash A/c…………………...…………Dr. Discount A/c……………………... ..……Dr. To A.Khan A/c (Cash received from A.Khan)		7,400 200	 7,600
Feb . 22	Drawings A/c………………….... ……Dr. To Bank A/C (Withdrew cash from Bank for personal use)		2,000	 2,000
Feb . 22	Cash A/c……………………………...……..Dr. To Bank. (Cash withdrew for office use.)		10,000	 10,000
Feb . 24	Telephone Charges A/c……….....……Dr. To cash (Paid telephone bill)		1,000	 1,000

Feb . 25	R.Rehaman A/c..........................Dr. To Cash (Paid R. Rehaman on account)		10,000	 10,000
Feb . 28	Stationery A/c..............................Dr. Salary A/c....................................Dr. Rent A/c.......................................Dr. To Cash (Paid for stationery, salary and rent)		2,000 10,000 4,000	 16,000

Dr. CASH ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Feb.1	To Capital A/c		90,000	Feb.2	By Bank		50,000
Feb.7	To Sales		19,000	Feb.3	By Purchase		30,000
Feb.17	To A. Khan		7,400	Feb.24	By Telephone Charges		1,000
Feb.22	To Bank		10,000	Feb.25	By R. Rehman		10,000
				Feb.28	By Stationery		2,000
				Feb.28	By Rent		10,000
				Feb.28	By Salary		4,000
				Feb.28	By Bal c/d		19,400
			1,26,000				1,26,000
March 1	To balance b/d		19,400				

Dr. BANK ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Feb .22	To Cash A/c		50,000	Feb. 5	By Furniture		10,000
				Feb. 5	By Drawings		2,000
				Feb. 22	By Cash		10,000
				Feb. 28	By Balance c/d		28,000
			50,000				50,000
March1	To balance b/d		19,400				

Dr. CAPITAL ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Feb .1	To balance c/d		90,000	Feb.1	By Cash A/c		90,000
			90,000				
				Mar. 1	By Balance old		90,000

Dr. PURCHASE ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Feb .3	To cash A/c		30,000	Feb.28	By balance c/d		44,000
	To R.Rehman		14,000	Mar. 1			
			44,000	2007	(Trading A/c)		44,000
March 1	To Balance old		44,000				

Dr. SALES ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Feb .1	To balance c/d		27,000	Feb .7	By Cash A/c		19,000
	(Trading A/c)			Feb .8	By A.Khan		8,000
			27,000				27,000
				Mar 1	By balance c/d		27,000

Dr. A. KHAN ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Feb .9	To Sales		8,000	Feb .14	By Returns		
					Inward		400
					By Cash		7,400
					By Discount		200
			8,000				8,000

Dr. R. REHAMAN ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Feb.25	To Cash		10,000	Feb.11	By Purchases		14,000
	To balance c/d		4,000				
			14,000				14,000
					By Balance b/d		4,000

Dr. FURNITURE ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Feb.5	To Bank		10,000	Feb. 28	By Balance c/d		10,000
			10,000				10,000
March 1	To balance b/d		10,000				

Dr. RETURN INWARD ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Feb.12	To A.Khan		400	Feb. 1	By Balance c/d (Trading A/c)		400
			400				400
	To balance b/d		400				

Dr. DISCOUNT ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Feb.17	To A.Khan		200	March 1	By Balance c/d (Profit & Loss A/c)		200
			200				200
	To balance b/d		200				

Dr. DRAWINGS ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Feb.22	To Bank		2,000	Feb. 28	By Balance c/d		2,000
			2,000				2,000
Mar. 1	To balance b/d		2,000				

Dr. TELEPHONE CHARGES ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Feb.24	To Cash		1,000	Feb. 28	By Balance c/d (Profit & Loss A/c)		1,000
			1,000				1,000
Mar. 1	To balance b/d		1,000				

Dr. STATIONERY ACCOUNT Cr.

Date	Particulars	F Rs.	Amount	Date	Particulars	F	Amount Rs.
2007 Feb.24	To Cash		2,000	Feb 28	By Balance c/d (Profit & Loss A/c)		2,000
Mar. 1	To balance b/d		2,000				
			2,000				

Dr. RENT ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Feb.28	To Cash		10,000	2007 Feb.28	By Balance c/d (Profit & Loss A/c)		10,000
			10,000				10,000
Mar. 1	To balance b/d		10,000				

Dr. SALARY ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007 Feb.28	To Cash		4,000	2007 Feb.28	By Bal c/d (P/L A/c)		4,000
			4,000				4,000
	To bal b/d		4,000				

2.4 Cash Book

Cash book is a special purpose subsidiary book. This book is used for recording cash transactions i.e. the transactions involving the receipt of cash and the payment of cash. When a business enterprise maintains a cash book then the cash transactions are not recorded in the journal. It serves the purpose of journal as well as ledger. It means in the ledger a separate cash account is not opened when a business maintains a cash book. There are different types of cash books. A business enterprise may maintain the following types of cash books;

- Simple cash book or single column cash book
- Double column cash book
- Triple column cash book
- Petty cash book.

2.4.1 Single Colume Cash Book

The format of a single column cash book is similar to that of an account. On its debit side receipts of cash are recorded and on its credit side cash payments are recorded. The debit side is also called the receipts side and the credit side is also called the payment side. The format of a single column cash book is given below.

CASH BOOK

Dr. Receipts Payments Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.

In the date column the date of the transaction is recorded. In the particulars column on the receipt side the name of the account on account of which cash is received is written. The word 'To' is pre-fixed before writing the name of the account. On the payment side in the particulars column the name of the account on account of which payment is made is written. The word 'By' is pre-fixed before this name. In the 'L.F.' column the folio or page number on which the transaction has been posted in the ledger is written.

Illustration 4: Enter the following transactions in a single column Cash Book.

2007		
Jan	1	Shyam started business with cash Rs.1,00,000.
Jan	2	He2000 deposited Rs. 30,000 into the bank.
Jan	5	He purchased furniture for office use for Rs. 10,000.
Jan	10	He purchased goods worth Rs. 12,000.
Jan	15	Sold goods for Cash worth Rs. 8,000.
Jan	20	Sold goods for cash worth Rs. 9,000.
Jan	25	Paid wages Rs. 500.
Jan	31	Withdrew cash for personal use Rs. 2,000.
Jan	31	Paid rent of Rs. 2,000, Salary Rs. 3,500.
Jan	31	Withdrew cash from bank for office use Rs. 5,000.

Solution:

IN THE BOOK OF SYHAM
CASH BOOK

Dr. Receipts Payments Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs
2007							
Jan 1	To Capital A/c		1,00,000	Jan. 2	By Bank		30,000
Jan 15	To Sales A/c		8,000	Jan. 5	By Furniture		10,000
Jan 20	ToSales A/c		9,000	Jan 10	By Purchases A/c		12,000
Jan 31	ToBank		5,000	Jan 25	By Wages A/c		500
				Jan 31	By Drawings A/c		2000
				Jan 31	By Rent A/c		2000
				Jan 31	By Salary		3500
				Jan 31	By balance c/d		62,000
			1,22,000				1,22,000
Feb. 1	To balance b/d		62,000				

Balancing of Single Column Cash Book

The balancing of the simple cash book, or single column cash book, is done periodically, generally at the end of the month in the same manner in which the balancing of a ledger account is done. First the total of the debit/receipt side is done, then the total of the credit/payment side of the amount column is ascertained. From the total of the debit amount column the total of the credit amount column is deducted to find out the cash balance and this is written in the amount column against the words 'By balance c/d' in the particulars column. This balance indicates that at the time of balancing the cash book there must be cash in the hand of the business equal to the balance indicated by the cash book.

It must be noted that while balancing the simple cash book the total of the debit/receipt column is ascertained first because of the simple reason that the cash receipts are always more than the cash payments. In other words we cannot make more payments than the amount of cash received. In the beginning of the next period the balance carried down is first brought down to the debit/receipt side as opening balance before recording the other transactions as 'balance b/d' of the period.

Ledger Posting from Single Column Cash Book

Ledger posting from the single column cash book is done into those ledger accounts whose names appear in the particulars column on both the side i.e. the receipt side and the payment side. Posting in the ledger of those accounts which appear on the debit side of the cash book is done on the credit side and the posting in ledger of those accounts which appear on the credit side of the cash book is done on the debit side by writing 'By cash' and 'To Cash, respectively'. Here it is once again emphasised that when a business maintains a single column cash book then cash account is not opened in the ledger because for cash transactions cash book works as a journal as well as a ledger.

Illustration 5. Enter the following transactions in the Cash Book of John, post them into the ledger and balance the cash book.

2007

March 1	Started business by introducing Capital in Cash	Rs.2,40,000
March 2	Opened bank account with ICICI Bank	Rs.1,00,000
March 3	Purchased computer for office	Rs. 40,000
March 4	Purchased office furniture	Rs. 20,000
March 5	Purchased goods	Rs. 50,000
March 7	Purchased goods of list price Rs. 20,000 at 10% Trade Discount.	
March 15	Sold Goods for Cash	Rs. 30,000
March 18	Sold goods of the list price of Rs. 15,000 at 5% trade discount.	
March 25	Paid wages	Rs. 1,000
March 26	Sold goods	Rs. 2,000
March 29	Sold goods	Rs. 5,000
March 31	Paid- Rent	Rs. 5,000
March 31	Salary	Rs. 5,000
March 31	Withdrew Cash for office use	Rs. 7,000

IN THE BOOK OF JOHN

CASH BOOK

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
2007							
March 1	To Capital A/c		2,40,000	Mar 2	By Bank A/c		1,00,000
March 15	To Sales A/c		30,000	Mar 3	By Computer A/c		40,000
March 18	To Sales A/c		14,250	Mar 4	By Office Furniture A/c		20,000
March 26	To Sales A/c		2,000	Mar 5	By Purchases A/c		50,000
March 29	To Sales A/c		5,000	Mar 7	By Purchases A/c		18,000
March 31	To Bank		7,000	Mar 25	By Wages A/c		1,000
				Mar 31	By Rent A/c		5,000
				Mar 31	By Salary A/c		5,000
				Mar 31	By Balance c/d		59,250
			2,98,250				2,98,250
	To balance b/d		59,250				

CAPITAL ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
				2007 Mar 1	By Cash		2,40,000

BANK ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
2007 Mar 2	To Cash		1,00,000	2007 Mar 31	By Cash		7,000

COMPUTER ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
2007 Mar 3	To Cash		40,000				

FURNITURE ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
2007 Mar 4	To Cash A/c		20,000				

PURCHASES ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
2007 Mar 7 Mar 15	To Cash A/c To Cash A/c		50,000 18,000				

SALES ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
				2007 Mar 15	By Cash A/c By Cash A/c By Cash A/c		30,000 14,250 2,000

WAGES ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
2007 Mar 18	To Cash A/c		1,000				

RENT ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
2007 Mar 31	To Cash A/c	5,000					

SALARY ACCOUNT

Dr. Cr.

Date	Particulars	LF	Amount Rs.	Date	Particulars	LF	Amount Rs.
2007 Mar 31	To Cash A/c		5,000				

2.4.2 Double Column Cash Book

When, to a single column cash book, discount column is added on both sides alongwith the amount column then this cash book becomes a double column cash book. A double column cash book is an improvement over a single column cash book in the sense that many times different transactions of discount take place and just by glancing at the discount column the management is able to know the amount of discount allowed to different parties and the amount of discount allowed by different parties. The format of a double column cash book is given below.

Receipt CASH BOOK Payments

Dr. Cr.

Date	Particulars	LF	Discount	Cash	Date	Particulars	LF	Discount	Cash

The recording of the transaction in a double column cash book is similar to that in a single column cash book except that the discount allowed is entered in the debit discount column and the discount received in entered in the credit discount column. This has been shown with the help of the following illustration.

Illustration 6 : Fair Deals had an opening balance of Cash Rs. 21,340 on 1.1.2007. The following transactions took place in the month of January. Enter these transactions in a double column cash book.

2007		
Jan	1	Received cash from Bobby Rs.5,070 and allowed him discount Rs. 30.
Jan	2	Paid to Zahir Cash Rs. 3,980 and he allowed discount Rs. 20.
Jan	8	Cash Sales of Rs. 10,000.
Jan	9	Cash purchases of Rs. 15,000.
Jan	12	Paid to Vikram Rs. 14,900 in full settlement of his account of Rs. 15,000.
Jan	17	Received from Munish Rs. 7,490 in full settlement of his account which had a debit balance of Rs. 7,500.
Jan	19	Purchased on credit from Rajan goods worth Rs. 2,000.
Jan	20	Sold goods to Ravi on credit worth Rs. 3,000.
Jan	25	Paid to Rajan Rs. 1,950 in full settlement of his claim.
Jan	26	Received from Ravi Rs. 2,990 and allowed him discount of Rs. 10.
Jan	31	Withdrew cash from bank for office use Rs. 14,000.
Jan	31	Withdrew cash for personal use Rs. 5,000.
Jan	31	Paid telephone bill of Rs. 2,000; Rent Rs. 6,000 and Salary Rs. 9,000.

M/S FAIR DEALS

CASH BOOK

Receipt Dr. | Payments Cr.

Date	Particulars	LF	Discount Rs.	Cash Rs.	Date	Particulars	LF	Discount Rs.	Cash Rs.
2007									
Jan 1	To bal b/d			21,340	Jan 2	By Zahir		20	3,980
Jan 1	To Boby		30	5,070	Jan 9	By Purchases			15,000
Jan 8	To Sales			10,000	Jan 12	By Vikram		100	14,900
Jan 17	To Manish		10	7,490	Jan 25	By Rajan		50	1,950
Jan 26	To Ravi		10	2,990	Jan 31	By Drawings			5,000
Jan 31	To Bank			14,000	Jan 31	By Telephone Charges			2,000
					Jan 31	By Rent			6,000
					Jan 31	By Salary			9,000

Note: Transactions dated 19.1.2007 and 20.1.2007 will not be entered in the cash book because these are credit transactions.

Balancing of Double Column Cash Book

While balancing the double column cash book, the balancing of the discount column is not done. Only the total of both the discount columns, i.e. debit discount column and credit discount column, is done. The balancing of the cash column is done in the same way in which the balancing of the cash column of the single column cash book is done. First the total of the debit side of the cash column is found out. From this total the total of the credit side of the cash column is subtracted and the difference is entered in the credit side as 'By balance c/d'. This 'balance c/d' is shown as opening balance on the debit side as 'To balance b/d'.

Ledger Posting from Double Column Cash Book: Ledger posting from the double column cash book is done in the same way as the ledger posting from the single column cash book. Ledger posting is done on the credit side of those accounts which appear on the debit/receipt side of the double column cash book. Similarly, ledger posting is done on the debit side of those accounts which appear on the credit/ payment side of the double column cash book. However, the totalof the discount column is posted on the same side of the discount account indicating the total amount of discount allowed and discount received. The total of the debit discount column is posted on the debit of the discount account by writing 'To Sundry Debtors' in the particulars column. The total of the credit discount column is posted on the credit side of the discount account by writing 'By Sundry Creditors' in the particulars column. This has been demonstrated with the help of the following illustration.

Illustration 7 : Enter the following transactions in the double column Cash Book of M/s Kalu Ram and Sons.

2007			Rs.
April	1	Opening balance	8,950
April	1	Paid to Karim	500
April	3	Received from Koshi	4,000
		Discount allowed to him	10
April	4	Cash Sales	16,000
April	7	Paid for stationery	200
April	10	Received from Dina Nath in full settlement of his account of Rs. 530	520
April	15	Paid to Gopal	1,980
		Discount allowed by him	20
April	18	Purchased goods for cash on list price at 5% trade discount	4,000
April	20	Purchased goods on credit from Vakil	6,000
April	22	Purchased goods from Khushal on list price at 10% Trade Discount	6,000
April	26	Paid to Vakil in full settlement of his claim	5,790
April	27	Withdrew cash from bank for office use	2,000
April	28	Withdrew for personal use	200
April	29	Sold goods to Sunil	2,700
April	30	Paid rent	6,000
		Salary	2,000
April	30	Received from Sunil on account	

Any income should also be taken as a transaction.

M/S KALU RAM & SONS

CASH BOOK

Dr. Cr.

Date 2007	Receipt	LF	Discount Rs.	Cash Rs.	Date 2007	Payment	LF	Discount Rs.	Cash Rs.
Apr. 1	To bal b/d			8,950	Apr. 1	By Karim A/c			500
Apr 3	To Koshi A/c		10	4,000	Apr. 7	By Stationery A/c			200
Apr 4	To Sales A/c			16,000	Apr. 15	By Gopal A/c		20	1,980
Apr 10	To Dina Nath A/c		10	520	Apr. 18	By Purchases A/c			3,800
Apr 27	To Bank A/c			2,000	Apr. 26	By Vakil A/c		210	5,790
Apr 30	To Sunil A/c			1,000	Apr. 27	By Drawings			200
					Apr. 30	By Rent			6,000
					Apr. 30	By Salary			2,000
					Apr. 30	By bal c/d			12,000
			20	32,470				230	32,470
May 1	To bal b/d			12,000					

Note: Transactions dated 20 and 22 April will not be entered in the cash book since these are credit transactions.

Dr. BANK ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007			
				Apr.30	By Cash		2000

Dr. DISCOUNT ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Apr.30	To Sundry Debtors		20	Apr. 30	By P/I A/c		20

Dr. KOSHI ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007			
				Apr. 3	By Cash		4,000
					By Discount		10

Dr. STATIONERY ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Apr. 1	To Cash		200				

Dr. PURCHASE ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Apr. 18	To Cash		3,800				
Apr. 20	To Vakil		6,000				
Apr. 22	To Khushal		5,400				

Dr. SALES ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007			
				Apr. 14	By Cash		16,000
				Apr. 29	By Sunil		2,700

Dr. KARIM ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Apr. 1	To Cash		500				

Dr. GOPAL ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Apr. 15	To Cash		1,980				
Apr. 15	To Discount		20				

Dr. VAKIL ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Apr. 26	To Cash		5,790	Apr. 20	By Purchase		6,000
	To Discount		210				

Dr. DRAWINGS ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Apr. 27	To Cash		200				

Dr. RENT ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Apr. 30	To Cash		6,000				

Dr. KHUSHAL ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007			
				Apr. 22	By Purchase		5,400

Dr. SALARY ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007							
Apr. 30	To Cash		2,000				

Dr. DINANATH ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
				2007			
				Apr. 10	By Cash		520
				Apr. 11	By Discount		10

Dr. SUNIL ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs.
2007				2007			
Apr. 29	To Sales		2,700	Apr. 30	By Cash		1,000

2.4.3 Triple Column Cash Book

When bank column is added on both the sides of a double column cash book then it becomes a triple column cash book. A triple column cash book, besides having date, particulars, LF, discount and cash also has a bank column on both the sides, i.e. the debit / receipt and credit / payment sides. In such a cash book the transactions with the bank are also recorded and separate bank account is not opened in the ledger because both debit/receipt and credit/payment of cash into bank or out of bank are recorded in it. When, by a single transaction, both cash and bank accounts are affected such a transaction is called a contra entry and no ledger posting of such an entry is done because both the aspects of the transaction, i.e. the debit aspect and the credit aspect, are completed in the cash book itself. Contra entries pertain to the deposit of cash into bank or withdrawal of cash from the bank for office use. To make such entries distinct from the remaining entries letter 'C' is written against such transactions in the folio column. 'C' means 'Contra' and no ledger postings for such entries are required.

Balancing of Triple Column Cash Book

The balancing of a triple column cash book is similar to the balancing of the double column cash book. The discount columns are not balanced rather the totals of the discount columns is done. The total of the cash column debit side is obtained first and from this total the total of the credit cash column is deducted to ascertain the cash balance. But while balancing the bank column first we have to see whether the total of the debit bank column or the total of the credit bank column is more. From the total of the greater side the total of the shorter side is subtracted to find out the balance and this balance is written on the shorter side as 'To balance c/d' or 'By bal c/d'. If the total of the debit bank column is more than it indicates a balance with the bank, i.e. the amounts deposited into the bank have been more than the amounts withdrawn. But at times the total of the credit bank column may be more than the total of the debit bank column which means the total amount withdrawn from the bank is more than deposited; this is a situation of bank overdraft. Therefore, a business enterprise is said to have a situation of bank overdraft when the amounts withdrawn from the bank are more than the amounts deposited. This can happen only when a special permission to do so is given by the bank.

Ledger Posting From Triple Column Cash Book

Besides Cash Account we also do not open bank account when the enterprise maintains a triple column Cash Book. Since both the debit and credit aspect of a transaction in the case of a contra entry are completed in the cash book itself, such entries do not require ledger posting. Like a double column cash book, in case of a triple column cash book, the total of the discount columns are posted on the same side of the discount account as the side they appear in the triple column cash book. It means the total of the debit discount column is posted in the debit side of the discount account by writing 'To Sundry Debtors A/c' in the particulars column and the amount in the amounts column. Similarly, the total of the credit/discount column of the cash book is posted in the credit side of the discount account by writing 'By Sundry Creditors' in the particulars column of the discount account and the amount in the amounts column. The remaining accounts which appear in the debit/receipt side, posting to the credit side of these accounts is done and the accounts which appear in the credit/payment side of the cash book, posting in the debit side of these accounts is done.

Illustration 7: Enter the following transaction in a triple column cash book of M/s Ram Krishan for the month of Jan. 2007.

2007			
			Rs.
Jan 1	Opening balance	Cash Dr	7,850
		Bank Cr	3,000
Jan 2	Sold goods for cash		5,000
Jan 3	Deposited cash into bank		10,000
Jan 4	Received cheque from Ashok		9,000
	Discount allowed		50
Jan 5	Cheque received from Ashok Deposited into bank		
Jan 6	Paid to Ravi by Cheque		2,000
	He allowed discount		10
Jan 11	Sold goods for cash		7,300
Jan 11	Paid to Mohan		400
Jan 11	Received cheque from Vinod		7,000
	Discount allowed to him		60

Jan 11	Cheque received from Vinod Endorsed in favour of Gopal In full settlement of his claim	7,100
Jan 11	Purchased goods for cash	2,400
Jan 13	Kumar who owned us Rs.8,000 paid 90 paise in a rupee	
Jan 14	Received cheque from Karan and banked immediately	15,400
	Discount allowed to him	100
Jan 18	Withdrawn Cash from Bank	10,000
Jan 20	Withdrawn cash for personal use	5,000
Jan 25	Cash sales	18,000
Jan 26	Deposited cash into bank	7,000
Jan 27	Sold goods for cash to Sant	6,000
Jan 29	purchased goods and issued cheque	3,000
Jan 30	Received cheque from Balwant and sent to bank immediately	10,000
	Discount allowed to him	500
Jan 31	Withdrawn cash from bank	9,000
Jan 31	Paid Salary	2,000
	Rent	3,000

M/S RAM KRISHAN

TRIPLE COLUMN CASH BOOK

Dr. Receipts Payments Cr.

Date	Particulars	F	Discount Rs.	Cash	Bank Rs.	Date Rs.	Particulars	F	Discount Rs.	Cash Rs.	Bank Rs.
2007						2007					
Jan 1	To bal b/d			7,850		Jan 1	By Bal B/d				3,000
Jan 2	To Sales			5,000		Jan 3	By Bank	C		10,000	
Jan 3	To Cash	C			10,000	Jan 5	By Bank	C		9,000	
Jan 4	To Ashok		50	9,000		Jan 6	By Ravi		10		2,000
Jan 5	To Cash	C			9,000	Jan 8	By Mohan			400	
Jan 7	To Sales			7,300		Jan 10	By Gopal		100	7,000	
Jan 9	To Vinod		60	7,000		Jan 11	By Cash			2,400	
Jan 13	To Kumar			7,200		Jan 18	By Cash	C			10,000
Jan 14	To Karan		100		15,400	Jan 20	By Drawings			5,000	
Jan 18	To Bank	C		10,000		Jan 26	By Bank			7,000	
Jan 25	To Sales			18,000		Jan 27	By Purchases				3,000
Jan 26	To Cash	C			7,000	Jan 31	By Cash	C			9,000
Jan 27	To Sales			6,000		Jan 31	By Salary			2,000	
Jan 30	To Balwant		500		10,000	Jan 31	By Rent			3,000	
Jan 31	To Bank	C		9,000		Jan 31	By balance b/d			40,550	24,400
			700	86,350	51,400				110	86,350	51,400
Feb 1	To bal b/d			40550	24400						

Petty Cash Book

A business, irrespective of its size, has to make a large number of small payments like bus fare, cartage, collieage, postage, stationery, taxi charges etc. These payments are generally repetitive in nature. If all these payments are recorded in the Cash Book, it will become very bulky. Usually, these payments are made by a person other than the main cashier called the Petty Cashier. The Petty Cashier is given a certain sum of money and then all small payments, say below Rs 100, are made by him. He records all such payments in a separate and special cash book called Petty Cash Book. Petty Cashier produces all the vouchers concerning the payments made by him before the main cashier. The main cashier checks these vouchers and hands over the necessary cash equal to the payments made by the petty cashier to him.

The system which is adopted for recording the petty cash transactions by the petty cashier in the petty cash book is called the imprest system. Under this system, in the beginning, a fixed sum of money is given to the petty cashier who makes payments out of it. This amount is called imprest money. The petty cashier makes all small payments out of this imprest amount and once he spends a large amount out of its say Rs 4,900, he gets this amount reimbursed from the main cashier. For this purpose he produces all the payment vouchers before the main cashier who, after verifying the same, reimburses the amount. Thus, the petty cashier again has the same amount in the beginning of the next period. The reimbursement by the main cashier may be made on checking fortnightly, or on a monthly basis, depending on the frequency of the small payment.

The format of the petty cash book

Amount Received Rs.	Date	Vr. No.	Particulars	Total Amount	Convey-ance	Cartage & Collieage	Postage	Refresh-ment	misc-expenses	Remarks

Illustration 8: A Petty Cashier was paid Rs 2,500 as Petty Cash imprest money on March 1, 2007. During the fortnight ended March 15 his expenses were as under.

March 2	Taxi fare for the manager	Rs. 150
March 3	Wages to casual worker	Rs. 125
March 4	Stationery	Rs. 280
March 5	Bus fair	Rs. 10
March 6	Courier charges	Rs. 105
March 7	Cartage	Rs. 115
March 8	Refreshment	Rs. 450
March 9	Cartage	Rs. 135
March 10	Repairs to furniture	Rs. 200
March 11	Taxi fare to salesmen	Rs. 200
March 12	Refreshment	Rs. 275
March 13	Conveyance	Rs. 85
March 14	Courier charges	Rs. 117
March 15	Cartage	Rs. 107

Record these translationin the Petty Cash book.

PETTY CASH BOOK

Amt. Received Rs.	Date	Vr. No.	Particulars	Total Amount	Conveyance Rs.	Courier Charges	Cartage & Colliage	Refreshment	Misc. Expenses	Remarks
	2007									
2,500	Mar. 1	1	Cash received							
	Mar. 2	2	Taxi fare for Manager	150	150					
	Mar. 3	3	Wages to casual workers	125					125	
	Mar. 4	4	Stationery	280					280	
	Mar. 5	5	Bus fare	10	10					
	Mar. 6	6	Courier charges	105		105				
	Mar. 7	7	Cartage	115			15			
	Mar. 8	8	Refreshment	450				450		
	Mar. 9	9	Cartage	135			135			
	Mar. 10	10	Repair to furniture	200					200	
	Mar. 11	11	Taxi fare to	200	200					
	Mar. 12	12	salesman					275		
			Refreshment	275						
	Mar. 13	13	Conveyance	85	85					
	Mar. 14	14	Courier charges	117		117				
	Mar. 15	15	Cartage	107			107			
			Total	2,354	445	222	357	725	605	
			Balance c/d	146						
2,500				2,500						
	2007									
146	March 16,		Balance b/d							
2354	2007		Cash Received							

2.5 Purchase Book

All credit purchases of goods are recorded in this book. Which is also called as 'Purchases Journal' or 'Purchase day Book'. We have already discussed that in the Cash Book all cash transactions are recorded. Similarly, when the number of credit transactions pertaining to purchases of merchandise or goods are very large than the business may use a subsidiary book to record such transactions and such a subsidiary book is called the purchases book. The source documents for recording transactions in this book are the invoices on the bills received by the firm from the suppliers. Entries in this book are recorded with net amount of the invoice. In this book only credit purchases are recorded and cash purchases are recorded in cash book. The format of the purchases book can be understood from illustraton 10.

Illustration 10. Prepare Purchases Book of M/s Amar Electrical for Dec. 2006.

2006

Dec. 18 Purchased on credit from Patil & Co. 10 Waterheaters @ Rs. 600 each, 20 Electric kettle @ Rs. 300 each. Trade discount 10%.

Dec. 20 Purchased on credit from M/s IMI 15 Water heaters @ Rs. 500 each, 10 Toasters @ Rs. 200 each. Trade discount 15%.

Dec. 25 Purchased on credit from Raghu 12 Electric Irons @ Rs. 230 each, 20 Toasters @ Rs. 300 each.

M/S AMAR ELECTRICALS
PURCHASES BOOK

Date	Particulars	Voucher No,	L.F.	Details Rs.	Amount Rs.
2006 Dec.15	Patel & Co. Vide invoice No.________. 10 Water Heaters @ Rs.600 each less 10% trade discount.			5,400	
	20 Electric Kettles @ Rs.300 each less 10% trade discount.			5,400	10,800
Dec.20	M/s IMI vide invoice No._________ 15 Water Heaters @ Rs.500 each less 15% trade discount			6,375	
	10 Toasters @ Rs.200 each less 15% trade discount.			2,700	9,075
Dec.25	Raghu vide invoice No.________ 12 Electric Irons @ Rs. 230 each.			2,760	
	20 Toasters @ Rs. 300 each.			6,000	8,760
	Purchases A/c Dr. **Total**				29,635

Note (i) Transactions of different dealings are not taken.
(ii) Cash Transactions are taken in the cash book.

2.5.1 Posting from the Purchases Book

The total of the purchases book is periodically posted to the debit of the purchases account by writing 'To Sundries Account' in the particulars column and the accounts of the individual suppliers are credited by writing 'By Purchases Account' in the particulars column. The posting from the purchases book of M/s Amar Electricals of Illustration 10 has been shown in the ledger as follows.

Dr. PURCHASES ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs
2006 Dec.31	To Sundries A/c		29,635				

Dr. PATEL & CO. ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs
				2006 Dec.5	By Purchases A/c		10,800

Dr. M/S I.M.I. ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs
				2006 Dec.20	By Purchases A/c		9,075

Dr. RAGHU ACCOUNT Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs
				2006 Dec.25	By Purchases A/c		8,760

2.6 Sales Book.

The credit sales of goods to customers are recorded in this book. We have already discussed that all cash transactions including cash sales of goods are recorded in the cash book. When the number of transactions relating to credit sales of goods is very large, for recording such transactions a special journal called Sales Book/Sales Day Book/Sales Journal may be used by the enterprise. In this journal only credit sales of goods is recorded. The format of the Sales Book is given below.

SALES BOOK

Date	Particulars	Invoice No.	L.F.	Details Rs.	Amount Rs.

2.6.1 Ledger Posting from the Sales Book

The total of the sales book is credited to the sales account by writing 'By Sundries' in the particulars column and the accounts of the individual debtors / customers are debited by writing 'To Sales A/c' in their respective accounts.

Illustration 11 : Enter the following transactions in the sales book of M/s Amar Electricals and post the same in ledger.

2006

Dec.12	Sold on credit to Ram Nath 5 Water Heaters @ Rs. 1,000 each 6 Electric Kettles @ Rs. 400 each Trade discount 5%.
Dec. 18	Sold on credit to Vishwa Nath 2 Toasters @ Rs. 350 each 2 Water heaters @ Rs. 1,100 each Trade discount 10%.
Dec. 25	Sold on credit to Rameshwar 5 Electric Irons @ Rs. 400 each Trade discount 5%.

M/S AMAR ELECTRICALS
0

Date	Particulars	Voucher No,	L.F.	Details Rs.	Amount Rs.
2006 Dec. 12	Ram Nath 5 Water Heaters @ Rs. 1,000 each less 5% Trade Discount. 6 Electric Kettles @ Rs. 400 each.Trade Discount 5%.			4,750 2,280	7,030
Dec. 18	Vishwa Nath 2 Toasters @ Rs. 350 each less 10% Trade Discount. 2 Water Heaters @ Rs. 1,100 each less 10%Trade Discount.			630 1,980	2,610
Dec. 25	Rameshwar 5 Electric irons @ Rs. 400 each less 5% Trade Discount.			1,900	1,900
	Sales A/c Cr. **Total**				11,540

Note (i) Transactions of different dealing are not taken.
(ii) Cash Transactions are taken in the Cash book.

LEDGER

SALES ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs
				2006 Dec.31	By Sundries		11,540

RAMANATH ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs
2006 Dec.12	To Sales A/c		7,030				

VISHWANATH ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs
2006 Dec.18	To Sales A/c		2,610				

RAMESHWAR ACCOUNT

Dr. Cr.

Date	Particulars	F	Amount Rs.	Date	Particulars	F	Amount Rs
2006 Dec.20	To Sales A/c		1,900				

2.7 Purchases Return Book

Sometimes goods purchased are returned to the suppliers. This may be done because the goods are not of the required quality, or as per the specifications of the sample sent by the supplier, or are defective etc. The return of such goods to the suppliers is recorded in the purchases returns book. When the goods are returned, a debit note is prepared in which the details of the goods returned are mentioned. The debit note is sent to the supplier. On the basis of the information given in the debit note the supplier makes necessary entries in his books. The format of the purchases returns journal is similar to the purchases book as given below.

PURCHASES RETURNS BOOK

Date	Particulars	Invoice No.	L.F.	Details Rs.	Amount Rs.

Illustration:12 Record the following transactions in the proper subsidiary books and post them into ledger of Vivek.

Jan. 1	Assets: Cash in hand Rs. 18,000; cash at bank Rs. 2,00,000; stock in hand Rs. 1,60,000; Bheem Rs. 60,000; Gullu Rs. 1,20,000 and furniture Rs. 1,40,000. Liabilities: Prakash Rs. 1,80,000.	(Rs.)
Jan. 2	Purchased a Motor Cycle from Bajaj Co. on credit	40,000
Jan. 3	Cash purchases	10,000
Jan. 4	Bought goods from Prakash Bill No. 314 20 Vests @ Rs. 50 each 30 Shirts @ Rs. 250 each	
Jan. 5	Goods sold for cash	36,000
Jan. 6	Received cash from Bheem Discount allowed him Sold goods to Mohan Bill No. 412 1000 Trousers @ Rs. 300 each 500 Cardigans @ Rs. 500 each	39, 500 500
Jan. 7	Paid cash into bank Received cash from Gullu Allowed him discount	60,000 20,600 400
Jan. 8	Paid salaries to staff	50,000
Jan. 9	Cash withdrawn from Bank	25,000
Jan. 10	Paid to Prakash by cheque Discount allowed by him	88,000 2,000
Jan.11	Raised a loan at 12% p.a. from Gobind and Deposited in Bank	1,50,00
Jan. 13	Purchased a Machine and paid by cheque	60,000

Jan. 15	Purchased goods from S.K.Singh & Co. Bill No. 6105 10 black shirts @ Rs. 300 each 20 black pullovers @ Rs. 400 each	
Jan. 16	Sold goods to Gullu on credit bill No. 413 5 sweaters @ Rs. 200 each 15 Sarees @ Rs. 300 each	
Jan. 17	Goods returned to S.K.Singh & Co. Debit Note 130 2 black shirts @ 300 each 5 black Pullovers @ Rs. 400 each	
Jan. 17	Received Cheque from Gullu & Banked Allowed him discount	19,800 200
Jan. 18	Goods returned by Gullu Credit Note. 201 5 Sarees @ Rs. 300 each 1 sweater @ Rs. 200 each	
Jan. 19	Prakash gives a special allowance on some defective goods purchased from him	3,500
Jan. 21	Cash sales to Rakesh Sharma Cash Purchases from Vinod Gupta through bank	15,000 1,20,000
Jan. 22	Sale of Old Newspaper	1,500
Jan. 23	Two old tables sold	5,500
Jan. 24	Paid rent by cheque	6,600
Jan. 25	Cash drawn from bank for personal use	10,000
Jan. 26	Two shirts costing Rs. 500 each taken for personal use	
Jan. 27	Cash paid for stationery	2,000
Jan. 28	Postage expenses paid	200
Jan. 31	Interest on Gobind's Loan due @ 6% Salaries outstanding Depreciation on furniture Cash paid into bank	1,500 6,500 1,000 15,000
Jan. 31	Bheem is insolvent and nothing received from his estate, it is a bad debt	

Solution :

Book Of Vivek

Cashbook (Three column)

Dr. Receipts Cr.

Date	Particulars	F	Discount Rs.	Cash	Bank Rs.	Date Rs.	Particulars	F	Discount	Cash Rs.	Bank Rs.
Rs. **2004**											
Jan. 1	To Bal b/d			18,000	2,00,000	Jan. 3	By Purchase A/c			10,000	
Jan. 5	To sales A/c			36,000		Jan. 7	By Bank A/c	C		60,000	
Jan. 6	To Bheem		500	39,500		Jan. 8	By Salaries A/c			50,000	
Jan. 7	To cash	C			60,000	Jan. 9	By Cash	C			25,000
	To Gullu		400	20,600		Jan.10	By Prakash		2,000		88,000
Jan. 9	To Bank	C		25,000		Jan.13	By Machine A/c				60,000
Jan. 11						Jan.21	By Purchase A/c				1,20,000
	12% Loan A/c				1,50,000	Jan.24	By Rent A/c				6,600
Jan. 17	To Gullu		200		19,800	Jan.24	By Drawing				10,000
Jan. 21	To Sales A/c			15,000		Jan.27	By Stationery A/c			2,000	
Jan. 22	To Sale of old newspaper			1,500		Jan.28	By Postage A/c			200	
Jan. 23	To Furniture A/c (Sold)			5,500		Jan.31	By bank	C		15,000	
Jan. 31	To Cash	C			15,000	Jan.31	By bal. C/d			23,900	1,35,200
			1,100	**1,61,100**	**4,44,800**				**2,000**	**1,61,100**	**4,44,800**
Feb. 1	**To bal b/d**			**23,900**	**1,35,200**						

Purchases Book

Date	Invoice Bill No.	Particulars (Supplier's Name)	L.F.	Details	Amount
2004				(Rs.)	(Rs.)
Jan. 4	314	**Prakash** 20 Vests @ Rs. 50 each 30 Shirts @ Rs. 250 each		 1,000 7,500	 8,500
Jan. 15	6105	**M/s S.K.Singh & Co.** 10 Black Shirts @ Rs. 300 each 20 Black Pullovers @ Rs. 400 each		 3,000 8,000	 11,000
Jan. 31		Purchase A/c-Dr. Total			19,500

Purchases Returns Book

Date	Debit Note No.	Particulars (Supplier's Name)	L.F.	Details	Amount
2004				(Rs.)	(Rs.)
Jan. 17	130	M/s S.K.Singh & Co. 2 Black Shirts @ Rs. 300 each 5 Black Pullovers @ Rs. 400 each		 600 2,000	 2,600
Jan. 31		Purchase Return A/c-Dr. Total			2,600

Sales Book

Date	Invoice Note No.	Particulars (Name of Customer)	L.F.	Details	Amount
2004				(Rs.)	(Rs.)
Jan. 6	412	Mohan 1000 Trousers @ Rs. 300 each 500 Cardigans @ Rs. 500 each		 3,00,000 2,50,000	 5,50,000
Jan. 16	413	Gullu 5 Sweaters @ Rs. 200 each 15 Sweaters @ Rs. 300 each		 1,000 4,500	 5,500
Jan. 31		Sales A/c-Dr. Total			5,55,500

Sales Return Book

Date	Credit Note No.	Particulars (Name of customer)	L.F.	Details	Amount
2004				(Rs.)	(Rs.)
Jan. 18	201	Gullu 5 Sarees @ Rs. 300 each 1 Sweater @ Rs. 200 each		 1,500 200	 1,700
Jan. 31		Sales Return A/c-Dr. Total			1,700

Journal Proper

Date	Particulars		L.F.	Debit Amount	Credit Amount
Jan. 1	Cash Account (Cash Book)	Dr.		18,000	
	Bank Account (Cash Book)	Dr.		2,00,000	
	Stock in hand	Dr.		1,60,000	
	Bheem	Dr.		60,000	
	Gullu	Dr.		1,20,000	
	Furniture	Dr.		1,40,000	
	To Capital Account (Balancing figure)				5,18,000
	To Prakash (Creditor)				1,80,000
	(Being the opening entry for the year 2005)				

Jan. 2	Motorcycle Account Dr. To M/s Bajaj Company (Being a MotorCycle purchased from Bajaj Co. on credit)		40,000	40,000
Jan. 19	Prakash Dr. To Special Allowance (gain) (Being a special allowance given by Prakash for defective goods)		3,500	3,500
Jan. 26	Drawings Account Dr. To Purchases Account (Being two shirts taken for personal use by Gopi Nath)		1,000	1,000
Jan. 31	Interest on Loan Account Dr. To Interest Due Account (Being interest due on Loan)		1,500	1,500
Jan. 31	Salaries Account Dr. To Salaries Outstanding Account (Being salaries due to be paid)		6,500	6,500
Jan. 31	Depreciation Account Dr. To Furniture Account (Being Depreciation charged on furniture)		1,000	1,000
Jan. 31	Bad debts Account To Bheem (Bheem is insolvent and the entire debit is a bad debt)		20,000	20,000

Dr. **Purchases Account** Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 3	To Cash Book To Cash Book (Bank) To Sundries as per Purchases Book		10,000 1,20,000 19,500	Jan 26 Jan 31	By Drawing Account		1,000

Dr. **Sales Account** Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
				Jan. 5 Jan 21 Jan 31	By Cash Book By Cash Book By Sundries as per Sales Book		36,000 15,000 5,55,500

Dr. Purchases Return Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
				Jan. 31	By Sundries as per Purchases Returns Book		2,600

Dr. Sales Return Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 31	By Sundries as per Purchases Returns Book		1,700				

Dr. Stock – in – Hand Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 1	To Balance b/d		1,60,000				

Dr. Bheem Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 1	To Balance b/d		60,000	Jan. 6	By Cash Book		39,500
					By Discount		500
					By Bad Debts		20,000
			60,000				60,000

Dr. / Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 2	To M/s Bajaj Co.		40,000	Jan 31	By Balance b/d		40,000
			40,000				40,000
Feb 1	To Balance b/d		40,000				

Dr. Furniture Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 1	To Balance b/d		1,40,000	Jan 23	By Cash Book (Sold)		5500
				Jan 31	By Depreciation		1000
				Jan 31	By Balance C/d		1,33,500
			1,40,000				1,40,000

Dr. Prakash Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 10	To Cash Book(Bank)		88,000	Jan. 1	By Balance b/d		1,80,000
	To Discount		2,000	Jan. 4	By Purchases Book		8,500
Jan 19	To Special Allowance		3,500				
Jan 31	To Balance c/d		95,000				
			1,88,500				1,88,500
				Feb. 1	By Balance b/d		95,000

Dr. Capital Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 31	To Balance c/d		5,18,000	Jan. 1	By Balance b/d		5,18,000
			5,18,000				5,18,000
				Feb. 1	By Balance b/d		5,18,000

Dr. **Gulu Account** Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 1	To Balance b/d		1,20,000	Jan. 7	By Cash Book		20,600
Jan 16	To Sales Book		5,500	Jan. 7	By Discount Amt.		400
				Jan. 17	By Cash Book		19,800
				Jan. 17	(Bank)		
				Jan. 18	By Discount		200
				Jan. 31	Account		
					By Sales Returns		1,700
					A/c		
					By Balance c/d		82,800
Feb 1.			1,25,500				1,25,500
	To Balance b/d		82,800				

Dr. **Bajaj Co.** Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 31	To Balance c/d		40,000	Jan. 2	By Motor cycle A/c		40,000
			40,000				40,000
				Feb. 1	By Balance b/d		40,000

Dr. **M/S N. K. Singh & Co.** Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 17	To Puchases Return A/c		2,600	Jan. 15	By Purchase Book		11,000
	To Balance c/d		8,400				
			11,000	Feb. 1	By Balance b/d		11,000

Dr. Mohan Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 6	To Sales Book		5,50,000	Jan. 31	By Balance c/d		5,50,000
			5,50,000				5,50,000
	To Balance b/d		5,50,000				

Dr. Salaries Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 8	To Cash A/c		50,000	Jan. 11	By Balance b/d		50,000
			50,000				50,000
					By		
Feb 1	TO Balance b/d		50,000	Feb. 1			

Dr. Depreciation Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 31	To Furniture Account		1,000				

Dr. Machine Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 13	To Cash Book (Bank)		60,000	Jan. 31	By Balance c/d		60,000
			60,000				60,000
Feb 1	To Balance b/d		60,000				

Dr. Special Allowance Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
				Jan 19.	By Prakash		3,500

Dr. Old Newspaper Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
				Jan 22.	By Cash Book		1,500

Dr. Rent Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan. 24	To Cash Book (Bank)		6,000				

Dr. Drawings Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan 25.	To Cash Book (Bank)		10,000	Jan. 31	By Balance c/d		11,000
Jan 26.	To Purchases A/c		1,000				
			11,000				11,000
Feb. 1	To Balance b/d		11,000	Feb. 1	By Balance b/d		

Dr. Stationery Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan 27.	To Cash Book		2,000				

Dr. Postage Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan 28.	To Cash Book		200				

Dr. Interest on Loan Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan 31.	To Interest Due Account		1,500				

Dr. Interest Due Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan 31.	To Balance b/d		1,500	Jan. 3	By Interest on Loan		1,500
			1,500				1,500
				Feb. 1	By Balance b/d		1,500

Dr. Salaries Outstanding Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan 31.	To Balance b/d		6,500	Jan. 3	By Interest on Loan		6,500
			6,500				6,500
				Feb. 1	By Balance b/d		6,500

Dr. Bad Debts Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan 31.	To Bheem		20,000				

Dr. Discount Allowed Account Cr.

Date 2004	Particulars	F.	Amount Rs.	Date 2004	Particulars	F.	Amount Rs.
Jan 31.	To Cash Book (Total)		1,100				

Dr. Discount Received Account Cr.

Date 2004	**Particulars**	**F.**	**Amount** Rs.	**Date** 2004	**Particulars**	**F.**	**Amount** Rs.
				Jan 31.	By Cash Book (Total)		2,000

Key Terms Introduced in the Chapter

- Books of Original Entry
- Source Documents
- Journal
- Ledger
- Posting
- Petty Cash Book
- Cash Book
- Sale Return Book
- Sales Book
- Balancing of Accounts
- Purchase Book
- Purchase Return Book

Summary with Reference to Learning Objectives

1. **Source Document :** A Document which provides evidence of transactions.
2. **Journal :** Basic book of original entry.
3. **Cash Book :** A book used to record all cash receipts and payments.
4. **Petty Cash Book :** A book used to record small cash payments.
5. **Ledger :** Principal book of accounting system, may be in the form of a bound register or loose leaf forms printed on papers or cards.

Questions for Practice

Short Answer-Question

1. What is a Journal? Give a specimen.
2. What is a Cash Book? How is it prepared?
3. Why does the Cash Book always show a balance?
4. How does a Cash Book serve a dual purpose?
5. Name the various types of Cash Books.
6. What is the meaning of contra entry?
7. What are the special Purpose Books?
8. What do you mean by Imprest System of Petty Cash Book?
9. What do you mean by Balancing of Accounts?
10. What is a journal folio?

Long Answer-Question

1. Explain how debits and credits are used to analyse a transaction.
2. State the main advantages of subdivision of journal.
3. What are 'Books of Original Entry' ? What are the rules of Journalisng of different types of accounts?
4. Explain the form and advantage of keeping a three column cash book.
5. What do you understand by Ledger? Explain its utility and importance.
6. What is Petty Cash Book? What are its advantages ?

Numerical Questions

Journalising

1. Journalise the following transactions of Mr. Ramesh.

2000		Rs.
Feb 1	Ramesh started business with cash	10,000
Feb 3	Paid into bank	6,000
Feb 4	Brought goods from M/s R. Singh & Co. on Credit	2,000
Feb 5	Purchased Furniture	200
Feb 5	Purchased adding machine	800
Feb 5	Purchased Typewriter	
	(Payment in all cases made by cheque)	600
Feb 7	Paid for postage	15
Feb 9	Sold goods for cash	400
Feb 10	Sold goods on credit to M/s M.Sharda & Co.	1,000
Feb 11	Paid to M/s R. Singh & Co.	1,950
	Discount allowed by them	50
Feb 14	Sold goods to M/S Rai & Co.	560
Feb 25	Received cheque from M/s M. Sharda & Co.	
	In full settlement of amount due from them	975
Feb 28	Paid salary	150
Feb 28	Paid rent by cheque	200
Feb 28	Drew for private use	350

2. The following are the transactions of P.Singh & Co. for the month of August. You are required to Journalise them.

2001		Rs.
Aug 1	Capital paid into bank	5,000
Aug 2	Bought stationery for cash	30
Aug 3	Bought goods for cash	2,000
Aug. 4	Bought postage stamps	2,100
Aug. 6	Sold goods for cash	750
Aug. 7	Bought office furniture from Mamta	500
Aug.12	Sold goods to Rajendra	1,000
Aug 13	Received cheque from Rajendra	1,000
Aug.15	Paid Mamta. by Cheque	500
Aug 17	Sold goods to Suresh & Co.	500
Aug 21	Bought goods from K.Seth & Bros.	700
Aug 24	Bought goods for cash from S.Verma & Co.	225

Aug 25	Sold goods to K.Kumar	350
Aug 27	Suresh & Co. Paid on account	250
Aug 29	Paid K.Seth & Bros. By cheque in full settlement	685
Aug 31	Rent is due to S.Verma but not yet paid	100

3. S. K. Singh commenced business on 1 March 2006. His transactions for the month are given below. Journalise them.

2006		Rs.
Mar 1	Commenced business with cash capital	25,000
Mar 2	Paid into bank	23,500
Mar 3	Brought goods from R & Co.	5,400
Mar 3	Sold goods to Manjeet	4,800
Mar 7	Bought goods from S. Chand	6,450
Mar 8	Paid wages in cash	80
Mar 8	Sold goods to M. Chand	5,350
Mar 10	Received cheque from Manjeet (Discount allowed Rs 120)	4,680
Mar 11	Paid to R & Co. (Discount received Rs 270)	5,130
Mar 12	Paid rent for three months up to March	400
Mar 13	Bought from C.Hajara	7,400
Mar 15	Paid wages in cash	80
Mar 15	Paid office expenses in cash	70
Mar 16	Sold goods to Jagdish	3,200
Mar 17	Sold goods to Manjeet	1,600
Mar 21	Sold goods to M. Chand	2,500
Mar 21	Payment received by cheque from Jagdish	3,200
Mar 22	Paid wages in cash	80
Mar 22	Paid office expenses in cash	50
Mar 22	Paid S. Chand by cheque (discount Rs 320)	6,130
Mar 26	Received cheque from M. Chand (discount Rs 150)	5,200
Mar 27	M. Chand returned goods(not up to sample)	200
Mar 29	Paid wages in cash	80
Mar 31	Paid office expenses in cash	40
Mar 31	Paid salaries for the month	300

4. Enter the following transactions in journal of Anil who trades in readymade garments.

2006		Rs.
June 1	Anil Paid into bank as Capital	6,000
June 2	He Bought goods for cheque	2,400
June 3	Sold to M & Co.	670

June 4	Sold goods for cash	1,090
June 5	Paid sundry expenses in cash	300
June 6	Cash sent to bank	1,500
June 7	Received cheque from M & Co.	650
	Discount allowed	20
June 8	Paid wages in cash	100
June 8	Paid for office furniture and fittings by cheque	400
June 9	Bought goods from Ramesh	1,060
June10	Sold to Kiran	1,870
June11	Returned goods to Ramesh	150
June12	Sent cheque to Ramesh. In full settlement	900
June 14	Sold goods for cash	490
June 14	Paid into bank	400
June 15	Drew cash from office for personal use	50
June 30	Paid cash for stationery	30
June 30	Bought goods from Sohan & Co. Ltd	1,000
June 30	Received from Kiran on account	600
June 30	Banked (Cash sent to bank)	650

Simple Cash Book

5 Enter the following transactions in a single column Cash Book.

2004	Rs.	
May 1	Commenced business with cash	25,000
3	Bought goods for cash	10,000
3	Paid Carriage	200
4	Sold goods for cash Received from Ram	6,000
10	Received from Ram	1,000
12	Paid to Shiv Kumar	2,600
15	Cash Sales	8,400
18	Purchased Furniture for cash for office	5,000
20	Paid for Advertisement	500
20	Purchased goods from Mahesh on Credit	6,000
24	Paid to Mahesh	4,000
25	Paid Wages	400
27	Received from Commission	1,500
28	Withdrew for personel use	2,200
31	Paid salary	700

Ans. Cash Balance Rs. 16,300

6. Prepare a Simple cash book from the following transactions of Mr. Gopal of Delhi.

2006		Rs.
April 1	Mr. Gopal commenced business with cash	8,000
April 3	He bought goods for cash	5,000
April 5	Sold goods for cash	100
April 6	Received cash from Mr. Lal	360
April 9	Paid into bank	3,000
April 13	Paid cash to Hari	215
April 16	Sold goods for cash	1,500
April 17	Paid for stationery	15
April 18	Paid for office furniture	185
April 21	Received from Mr. Kailash	680
April 22	Paid for advertising	90
April 25	Purchased postage stamps	20
April 28	Paid rent	100
April 30	Paid electricity charges	15

Ans. : Cash Balance Rs. 2,000

7. Compile Cash Book from the following transactions given to you.

2005		Rs.
Mar 1	Mr. M. Lal commenced business with cash	8,500
Mar 2	Bought goods for cash	685
Mar 4	Paid Mr. Sohan Lal cash	145
	Discount allowed	5
Mar 6	Deposited in bank	4,000
Mar 6	Paid for office furniture in cash	465
Mar 8	Sold goods for cash	3,000
Mar 12	Paid wages in cash	130
Mar 13	Paid for stationery	50
Mar 14	Sold goods for cash	2,500
Mar 16	Paid for miscellaneous expenses	65
Mar 19	Received cash from Mr. S. Chand	485
	Allowed him discount	15
Mar 22	Purchased a radio set	250
Mar 22	Paid salary	300
Mar 25	Paid rent	100
Mar 28	Paid electricity bill	55
Mar 29	Paid for advertising	40
Mar 31	Paid into bank	4,500

Ans. Cash Balance Rs. 3,700

8. Enter the following transactions in a Two Column Cash Book having Cash and Discount Columns.

2003		Rs.
Dec 1	Cash in Hand	15,000
Dec 2	Cash Sales	12,000
Dec 4	Received from X on Behalf of Y	4,000
Dec 7	Bought goods for cash	10,000
Dec 9	Paid to Som Pal	4,900
	Discount Received	100
Dec 11	Received from Vijay Kumar	7,800
	And discount allowed	200
Dec 15	Sold goods in cash	6,500
Dec 16	Sold goods to Kabir on credit, the terms being 2 ½ % cash discount , If payment is received within one week	10,000
Dec 18	Paid Telephone expenses	450
Dec 20	Cash Purchase	9,000
Dec 21	Paid Cartage	200
Dec 22	Received cash from Kabir for the goods sold on 16 th Dec	1,880
Dec 23	Remmitted to Dharamvir and discount allowed by him	120
Dec 25	Received M.O. from Mohan	500
Dec 27	Borrowed from Mahabir	7,500
Dec 29	Received from Bhushan	3,900
	Discount allowed	100
Dec 31	Received dividend on shares	400
	Paid to Lalit Rs. 2,700 in full settlement of his account of Rs. 3,000.	

Ans. : Cash Balance Rs. 38,220; Discount Dr. Rs.550 and Cr. Rs.520

9. Enter the following transactions in Cash Book having discount and Cash Columns.

2006.		Rs.
March 1	Cash in hand	30,000
March 4	Paid for cash purchases	5,000
March 5	Received from cash sales	17,000
March 7	Prakash Paid us cash	3,950
	We allowed him discount	50
March 11	Paid Satish & Co.	4,400
	They allowed us discount	100
March 13	Received Commission	200
March 15	Issued a Cheque to Dinesh towards an account of Rs. 10,000 less 5% cash discount	
March 17	Issued a cheque for Rs. 3,800 to Faquir Chand in full settlement of his account for Rs. 4,000	
March 21	Bought goods for cash	9,200
March 25	A cheque issued by the proprietor for gift at the marriage of his wife's friend	500

March 28	Purchased filing Cabinet for office	4,500
March 29	Drew Cheque for petty expenses	400
March 31	Paid office rent	1,500
	Paid sales tax	3,000
	Received interest	250

Ans. : Cash Balance Rs. 9,600; Discount Dr. Rs. 50 and Cr. Rs. 800.

10. Write up Cash Book of Bhanu Pratap with Cash and Bank Columns from the following transactions.

2000		Rs.
March 1	Cash in Hand	2,710
	Cash at bank	27,500
March 3	Received from Subhash	3,500
March 4	Sold goods for cash	10,000
March 7	Paid rent by Cheque	800
March 8	Paid Sohan By cheque	3,000
March 10	Bought goods for cash	15,000
March 12	Paid cash for stationery	200
	Drew from bank for office use	8,000
March 15	Received cheque from Vinod and sent it to bank	6,600
March 16	Paid for advertisement	750
March 18	Issued cheque in favour of Nath Brothers	4,300
March 19	Cash sales	13,000
	Paid into bank	
March 20	Received cheque from Vinod and sent it to bank	16,000
March 22	Bought Scooter and paid for the same by cheque	2,400
March 25	Bank returned Surendra's Cheque dishonoured	18,000
March 28	Paid salary by cheque	7,200
	Paid trade expenses	2,000
March 29	Cash sales	95,00
March 30	Paid into Bank	10,000

Ans. : Cash Balance Rs. 2,760 and Bank Balance 14,600.

11. Enter the following transactions in Cash Book with discount columns.

2006		Rs.
Jan 1	Cash in hand	1,500
Jan 5	Paid to Ram	300
	Discount allowed by him	
Jan 8	Purchased goods	400
Jan 11	Received from S. Gupta	980
	Discount allowed	20

Jan 16	Sold goods	400
Jan 21	Paid to M. Sharma	300
	Discount received	5
Jan 25	Paid wages	50
Jan 31	Paid to Shiv in full settlement of his account which shows a credit balance of Rs. 400	390

Ans.: Cash Balance Rs. 1,440

Triple Column Cash Book

12. Prepare a three- column cashbook.

2007		Rs.
Jan 1	Cash in hand	5,000
Jan 1	Bank overdraft	1,000
Jan 2	Paid wages	1,500
Jan 3	Deposited into bank	2,000
Jan 4	Cash sales	7,500
Jan 5	Sold goods for cheque which was deposited in bank on the same day	5,000
Jan 6	Purchased goods from Shivam on credit	4,000
Jan 7	Drew from bank for personal use	1,000
Jan 8	Paid to Shivam in full settlement	3,500
Jan 9	Received from Ram, who owes Rs. 5,000, Rs. 2,000 only on account.	

Ans.: Cash in hand Rs. 7,500; Bank Balance Rs. 5,000

13. Enter the following transactions in Triple column Cash book of Raj Traders.

2006		Rs.
Dec 1	Started business with cash	9,000
Dec 1	Deposited in the bank	4,000
Dec 2	Purchased office equipment	1,000
Dec 4	Cash Purchases, issued cheque	2,500
Dec 8	Received cheque from Anuj on account	3,250
Dec 10	Cash sales, received cheque	1,300
Dec 15	Office expenses	275
Dec 25	Office rent paid by cheque	300
Dec 28	Received cheque from Raju and endorsed the same to Rohit	400
Dec 30	Paid advance income tax by cheque	575
Dec 31	Deposited into bank, balance of cash in excess of Rs. 300	

Ans. Cash balance Rs. 300; Bank Balance Rs. 8,600

14 . Enter the following transactions in the Cash Book with Discount, Cash and Bank Columns.

2006

April	1	Balance of cash in hands Rs. 400 , overdraft at bank Rs. 5,000
	4	Invested further capital of Rs. 10,000 out of which Rs. 6,000 deposited into the bank
	5	Sold goods for cash Rs. 3,000
	6	Received from Ghanshyam Rs. 8,000 ; discount allowed to him Rs. 200
	10	Purchased goods for cash Rs. 5,500
	11	Paid to Ram Vilas ,our creditor, Rs. 2,500; discount allowed by him Rs.65
	13	Commission paid to our agent Rs. 530
	14	Office furniture purchased from Keshav in cash Rs. 200
	14	Rent paid Rs. 50
	16	Drew cheque for personal use Rs. 850
	17	Cash sales of Rs. 2,500.
	18	Collection from Atul Rs. 4,000, deposited in the bank on 19 April
	19	Drew from the bank for office use Rs. 500.
	24	Dividend received by cheque Rs. 50, deposited in the bank on the same day
	25	Commission received by cheque Rs. 230, deposited in the bank on 28th April
	29	Drew from the bank for salary of office staff Rs. 1,500
	29	Paid salary of the manager by cheque Rs. 500
	30	Deposited cash in the banks Rs. 1,000

Ans. Cash Balance(Dr.) Rs. 8,610 and Bank Balance (Dr.) Rs. 2,930; Discount (Dr.) Rs. 200;and Discount (Cr.) Rs. 65.

15. Prepare Triple Column Cash Book from the following transactions.

2007

Jan	1	Cash at office Rs. 72
		Bank overdraft Rs. 1,250
	4	Received from Prem Chand a cheque for Rs. 1,875 in full settlement of his account of Rs. 1,900 . The Cheque was banked on the same day.
	5	Bought goods and paid by cheque Rs.500
	6	Narinder settled his account of Rs. 700 by Cheque . This was banked on the same day.
	9	Paid to Manohar Lal by cheque for Rs. 420 . Discount received Rs.80.
	12	Cash sales to date Rs.400 of which Rs.300 were banked.
	17	Sold old typewriter for cash Rs.320.
	20	Received a cheque for Rs.400 from Naresh in full settlement of his account of Rs.460. The cheque was endorsed to suresh in full settlement of his account of Rs. 420.
	25	Received a cheque from Hari Prakash for Rs. 150.
	27	Cheque of hari Prakash was endorsed to Raj Prakash. Discount received Rs.30.
	28	Withdrew from bank for office use Rs. 100 and for personal use Rs . 100.
	29	Withdrew (from office) for payment of private bills Rs. 425.

30	Paid by cheque salaries Rs. 160 and rent 100	
31	Bank Charges as per Pass Book Rs. 5	

Ans. Cash balance Rs. 167 ; Bank Balance (Dr.) Rs. 240;
Discount (Dr.) Rs. 85 ; (Cr.) Rs. 130 .

16. Enter the following transactions in the cash book with Discount , Cash and Bank Columns.

2007		Rs.
Jan 1	Cash in hand	4,800
	Bank overdraft	30,400
Jan 2	Fresh Capital introduced	20,000
Jan 3	Deposited into bank	15,000
Jan 4	Sold goods to Mahesh on credit	6,200
Jan 5	An Amount of Rs. 4,200 due from Ashok written off as bad debts in the previous year , now recovered	
Jan 6	Withdrew from bank for the payment of Life Insurance Premium	3,000
Jan 8	Received a cheque from Mahesh for Rs. 6,000 in full settlement of his account and deposited the same into the bank	
Jan 10	Sold goods to Varun on Credit	30,000
Jan 12	Received a Cheque for Rs. 28,000 from Varun in Full Settlement	
Jan 15	Cheque received from Varun sent to bank	
Jan 18	Varun,s cheque returned by Bank Dishonoured. Bank Charged Rs. 25 on this Cheque	
Jan 20	Received a cheque of Rs. 6,800 from Vijay which was endorsed to Amrit Raj on the same day	
Jan 25	Withdrew cash from Bank Rs.5,000 for paying gift to his daughter on her birthday	
Jan 26	Bought goods from Gupta General Store for Rs.10,000 on credit and they allowed us trade discount of 25%	
Jan 28	Paid to Gupta General Stores in cash, full Settement	7,000
Jan 28	Sale of Old Machinery , payment received in cash Rs.7,700	
Jan 30	Paid salary by cheque Rs.1,500. Paid Rent in cash Rs. 2,200	
Jan 31	Paid into current Account the entire balance after retaining Rs. 5,000 at office	

Ans. Discount (Dr.) Rs. 2,200 ; (Cr.) Rs. 2,500; Cash balance (Dr.) Rs.5,000; Bank Overdraft Rs. 11,425; Excess Cash deposited into Bank on 31 May Rs. 7,500.

17. Compile a triple column cash book from the following transaction's of Kavita Garments.

2003	
Feb 1	Cash in Hand Rs. 7,500; Cash at bank Rs. 8,000.
Feb 2	Discounted a bill receivable for Rs. 6,000 at 2% through bank
Feb 3	Received two cheques from Kalpana each of Rs. 10,000
Feb 4	First cheque received from Kalpana is endorsed to Sunita in full settlement

	of Rs. 10,200. Second cheque is sent to bank for collection
Feb 5	Second cheque received from Kalpana is returned as dishonoured by the bank. The bank has debited our account with Rs. 20 as bank charges on this cheque
Feb 6	Received cheque from sale of old furniture for Rs.1,950 . Cheque is endorsed to a creditor Ramesh in full settlement of Rs. 2,000 due to him
Feb 8	Purchased goods from Mohan on credit for Rs. 8,000
Feb 10	Settled Mohan's account by giving a cheque for Rs.4,000 and cash Rs. 3,900
Feb 12	Goods sold to Pawan for Rs. 6,000. He paid the amount in cash immediately after deducting 2 ½ % cash discount
Feb 15	A bill payable fro Rs. 5,000 paid by Cheque
Feb 18	Cash sale to date Rs. 50,000 of which Rs. 40,000 banked .
Feb 20	Paid electric bill of Rs.2,000 for Jan 2003 by cheque . paid rent for Jan 1998 Rs. 15,00
Feb 25	Cash purchases Rs. 5,000 , Issued a Cheque
26	Deposited into bank cash retaining Rs. 7,500

Ans. Discount (Dr.) Rs. 270 ; (Cr.) Rs. 350 ;cash in hand Rs. 7500 ; Cash at bank Rs. 48,310. Excess cas deposited into bank on 28 Feb. Rs. 10,450

18. Write out the following transaction's in Cashbook with discount and bank columns.

2006	
Jan 1	Champa commences business with Rs. 20,000 in cash
Jan 3	He pays Rs. 19,000 into Bank Current A/c
Jan 4	He receives cheque for Rs. 600 from Riti & co. on account
Jan 10	He pays R & Co. by cheque Rs. 330 and is allowed discount Rs. 20
Jan 12	T & Co. pays into his bank A/c Rs. 475
Jan 15	He receives cheque for Rs. 450 from Wasi and allows him discount of Rs. 35
Jan 20	He receives cash Rs. 75 and cheque Rs. 100 for cash sales
Jan 27	He pays by cheque for cash purchases Rs. 275
Jan 30	He pays sundry expenses in cash Rs. 50
Jan 30	He pays S & Co. Rs. 375 in cash and is allowed discount of Rs. 35
Jan 31	He pays office rent by cheque Rs. 200
Jan 31	He draws a cheque for personal use of Rs. 250
Jan 31	He pays staff salaries by cheque Rs. 300
Jan 31	He draws a cheque for office use Rs. 400
Jan 31	He pays cash for stationery Rs. 25
Jan 31	He purchases goods for cash Rs. 125
Jan 31	He pays Pal by cheque for commission Rs. 300
Jan 31	He gives cheque to Saran for cash purchase of furniture for office of Rs. 1,575
Jan 31	He receives cheque for commission Rs. 500 from Rohan & Co.
Jan 31	He receives cheque from K & Co. for Rs. 450

Ans. Cash balance Rs. 900; Bank Balance Rs. 17,945

19. A Petty cashier in a firm received Rs. 150 as the petty cash imprest on 4 June 2006. During the week, his expenses were as follows.

2006		Rs.
Jane 4	Tonga charges for managers trip to the city	5
Jan 4	Wages to casual labourers	15
Jan 5	Bus fare to workmen sent to customers premises	2
Jan 5	Stationery purchased	10
Jan 6	Sent telegram to Head office	4
Jan 6	Postage stamps purchased	10
Jan 6	Revenue stamps for payment of wages	5
Jan 7	Repair of typewriter	4
Jan 7	Paid electric lighting bill	17
Jan 8	Wages paid to coolies for shifting furniture etc.	4
Jan 8	Taxi fare to assistant manager	5
Jan 8	Locks purchased	8
Jan 8	Stationery purchased	4
Jan 9	Refreshments to customers	2

Write up the Petty cashbook and draft the necessary Journal entry for the payments made.

Ans. Petty Cash Balance Rs. 55

20. Prepare an Analytical Petty Cash Book on the imprest system from the following.

2006	
June 1	Received Rs 400 for Petty Cash.
June 3	Paid Cartage Rs 10.
June 4	Paid Bus Fare Rs 5; Postage Rs 12
June 6	Paid for Stationery Rs. 8
June 7	Paid for Postage Rs. 6
June 9	Paid for Taxi Fare Rs. 25;
June 10	Paid for Telegram Rs. 15; charity Rs. 21
June 11	Paid for Newspaper Rs. 20
June 12	Paid for Soap Rs 10; Printing Rs 30
June 13	Paid for Postage Rs 15
June 14	Paid for Repairs of Chairs Rs 20
June 15	Paid for Refreshment to customers Rs 10

Ans. Petty Cash balance Rs 203; Postage and Telegram Rs 48; Printing and Stationery Rs 38; Traveling Rs 30; Cartage and Carriage Rs 10; Sundry expense Rs 81.

21. Record the following transactions in a Petty cash book with suitable columns. The book is kept on imprest system, amount of imprest being Rs 500.

2006

April 1	Petty cash in hand Rs. 54. Received cash to make up the imprest.
	Paid for office cleaning Rs 10.
April 4	Paid railway fare Rs 32, bus fare Rs 28, Telegram Rs. 25
April 5	Bought shorthand note books for office Rs 37
April 7	Paid carriage on Parcels Rs 15, paid for telegram Rs 22
April 10	Bought stamps for Rs 30, Envelopes for Rs 45 and an accounts register for Rs 40
April 12	Paid for repairs Rs 20, gave tip to office peon Rs 15
April 12	Paid for repairs Rs 20, gave tips to office peon Rs 15
April 13	Gave charity Rs 10, served tea to customers Rs 25
April 15	Paid for telephone calls Rs 16, Coolie, carriage Rs 15; Sundry exp. Rs 90

Ans. : Petty Cash balance Rs 120; Postage and Telegram Rs 93; Printing and Stationery Rs 122; Travelling Rs 122; Coolie, Cartage and Carriage Rs 15; Sundry expense Rs 90.

Other Subsidiary Books

22. Prepare Pruchases Book of Mangat Traders dealing in readymade garments, from the following information.

2004

Feb. 10 Purchased from Sita Sons
20 Shirts @ Rs. 500 each
30 Shirts @ Rs. 500 each
15 Shirts @ Rs. 1,000 each

Feb. 15 Bought of Happy Garments
150 Vests @ Rs. 45 each
200 Ties @ Rs. 100 each
150 Skirts @ Rs. 250 each
Less: 15% Discount

Feb. 25 Bought of Laxmi Stores
70 Pairs of Socks @ Rs.100 each
90 Pairs of Socks @ Rs.150 each
110 undergarments @ Rs. 200 each
Less: 5% Discount

23. Record the following transactions in the Purchase Book of Silver Furnishers.

2004

Mar. 3 Purchased from Haryana Furnishers
3 Chairs @ Rs. 600 each
2 Tables @ Rs. 2,500 each
1 Showcase @ Rs. 4,000 each
Less: 10% Discount

Mar. 13 Purchased from Star Furniture Store
5 Dining Sets @ Rs. 8,500 each
3 Double Beds @ Rs. 6,000 each
2 Dressing Tables @ Rs. 2,000 each
4 Writing Tables @ Rs 3,200 each

Mar. 28 Purchased from Chandigarh Furniture House
10 Folding Chairs @ Rs 400
20 Desks @ Rs 2,500
15 Beds @ Rs. 3,600
10 Computer Tables @ Rs. 4,000
25 Tables @ Rs 3,000
Less: 10% Discount

24. Enter the following transactions in the Books of Cheap Cloth House.

2004
June. 2 Purchased from Royal Silk Store
10 Sarees @ Rs. 1,300 each
20 Meters long cloth @ Rs. 100 per metre
30 Shirting @ Rs. 500 each
Less: 10% Discount

June. 10 Purchased from Zohra Fabrics
5 Nylone Sarees @ Rs. 500 each
20 Pant Pieces @ Rs. 300 each
30 Turbans @ Rs. 300 each

June. 20 Purchased from Delhi Cloth Mills
20 Metres Poplin @ Rs. 120 per metre
15 Metres Rough Cloth @ Rs. 20 per metre
10 Bundles of Muslin @ Rs. 1,200 each
Less: 10% Discount

25. Enter the following transactions in the Books of Bhushan Steel Co.

2004
Dec. 1 Purchased from Gupta Iron Merchants
10 tons of Steel Rods @ Rs. 1,200 per ton
15 Sheets of Black Iron @ Rs. 500 each
10 tons of Gill Iron @ Rs. 1,500 per ton
Less: 11% Discount

Dec. 10 Purchased from Raunaq Steel Co.
10 Corrugated Sheets @ Rs. 800 each
20 tons of pig iron @ Rs. 2,000 per ton
30 tons of Building iron rods @ Rs. 1,200
25 Galvanised Sheets @ Rs 800 each

Dec. 26 Purchased from Handa Steel House
20 Tata Steel Sheets @ Rs. 800 each
10 White Sheets @ Rs. 900 each
20 Corrugated Sheets @Rs. 800 each
Less: 20% Discount

Dec. 28 Purchased goods for cash for Rs 16,000.

Sales Book

26. Enter the following transactions in the Books of Bombay Selections.

2004

Mar. 4 Sold to Sohan of Shimla
20 Trousers @ Rs. 850 each
10 Black Sweaters @ Rs. 700 each
30 Woolen Pairs of Socks @ Rs.200 each
30 Cardigans @ Rs 900 each
Less: 15% Discount

Mar. 12 Sold to Darshan of Delhi
12 Black Shirts @ Rs. 450 each
20 Blue Shirts @ Rs. 500 each
40 Dark Brown Shirts @ Rs. 425 each
30 Neck Ties @ Rs 250 each

27. Enter the following transactions in the Sale Book of Master Book Store.

2004

July 5 Sold to New Public School
50 Books on English @ Rs 60
25 Mathematics Books @ Rs 70
30 English Reading Books @ Rs 50
30 Grammar Books @ Rs 80

July. 12 Sold to K.V. School
40 Accountancy Books @ Rs 220
30 Business Studies Book @ Rs 150
40 Social Studies Books @ Rs 80
30 Economics Books @ Rs 170
Less: 20% Discount

Purchase Return Books

28 Enter the following transactions in the books of Mann Stationers.

2006

Jan. 1 Returned Goods to Fine Paper Stores
15 Registers @ Rs 40 Each
20 Note Pads @ Rs 15 each

Jan. 2 Returned Goods to Sunil Tata
25 File Covers @ Rs 40 Each
10 Packets of Envelopes @ Rs 30

29. Prepare Purchase Return Books of Nirman Steel Store.

2006

Mar. 5	Returned Goods to Super Steel of Chandigarh	
	10 Corrugated sheets @ Rs 200 Each	
5	Tons of Brass Sheets @ Rs 300 Each	
Mar. 20	Returned to Suraj Steel of Delhi	
	10 tons of Rod Bar @ Rs 2,000 Each	
	2 tons of Almunium Bars @ Rs 3000	
	Less: 15% Discount	

Sale Return Books

30. Prepare the Sale Return Book of Anita Bakers from the following Information.

2006

June 10 Goods returned to Verma of Ambala
25 Brown Breads @ Rs 20 each
10 Packets of Salt Cookies @ 15 each

June 19 Goods returned by Kiran of Agra
25 White Breads @ Rs 10 each
20 Packs of Choeo Bar @ Rs 40 each

June 21 Sold to Polka Bakery
20 Garlic Bread @ Rs 25
15 White Bread @ Rs 40
40 Packets of Sweet Choco Bar @ Rs 40

31. Enter the Following Transactions in the Sale Return Book of Lee Shoes.

2004

July 10 Goods returned by Boston Bros
25 Pairs of Kids Shoes @ Rs 200
10 Pairs of Ladies Shoes @ Rs 400
20 Pairs of Gents Shoes @ Rs 900
Less : 20% Discount

July 19 Goods returned by German Shoes
5 Pairs of Cotton Socks @ Rs 80
10 Pairs of Woolen Socks @ Rs 200
10 Pairs of Ladies Shoes @ Rs 400
10 Pairs of Black Shoes @ Rs 700
Less : 10% Discount

Cash Book and its Posting

32. Enter the following transactions in Triple columns cash book and post them into Ledger.

2006

May 1	Balance of cash in hands Rs. 14,400 , overdraft at bank Rs. 26,000.
May 3	Direct deposit by Mr. Ghosh in our bank account Rs 10,000. Discount allowed Rs 200.
May 5	Issued a cheque of Rs 7,700 to Mr. Suresh in full settlement of his account of Rs 8,000.
May 6	Received a cheque from X for Rs 12,000. Discount allowed Rs 500. This cheque was deposited into bank on 7 May.
May 8	Received Cash Rs 22,000 and cheque of Rs 8,000 for cash sale.
May 12	Cash sale Rs. 70,000 of which Rs. 55,000 banked.
May 15	Cheque received on 8 May endorsed to Mr. Sunil. Discount received Rs 150.
May 20	Discounted a B/R of Rs 10,000 at 1% through bank.
May 24	Cheque received from X dishonoured, Bank debits Rs 20 in respect of bank charges.
May 25	Purchased goods for Rs 50,000 at a trade discount of 10%. Payment was made in cash
May 26	Withdrew from bank Rs 10,000 for office use and Rs. 2,000 for personal use
May 31	Interest debited by Bank Rs 4,500

Ans. Cash Balance Rs. 16,400; Bank Balance (Dr.) Rs.4,680;Discount (Dr.) Rs. 800; and Discount (Cr.) Rs. 950.

Purchase Book and its Posting

33. Record the following transactions in Purchase Book of Modern.

2006

Nov 3 Purchased goods from Sachdeva Furniture Store
100 Chairs @ Rs 100 each
10 Tables @ Rs1,500 each
Less : 10% Discount

10 Purchased furniture from Mohan & Co valued at Rs. 20,000, Less 12 ½ % Trade Discount 18
Purchased furniture from Fashion Furniture House of the List Price of Rs 25,000.
Less 15%

20 Purchased furniture from India Furniture House 150 Chairs @100 Each

25 Purchased from Mohan Lal & Sons furniture of the value of Rs 8,000 each

Ans. Total of Purchase Book Rs. 76,250

SALE BOOK AND ITS POSTING

34. Record the following transaction in Sale Book of sh. Vivek Jain and Post them into Ledger.

2006

Dec 5 Sold to M/s Vikram & Sons
Goods valued at Rs 20,000 Less : Trade Discount 10%

10	Sold to M/s Sohan Lal & Sons. Karol Bagh 60 Electric Fans @ Rs 800 each 40 Room Coolers @ Rs 1,250 each Less : Trade Discount 8%
16	Manesh & Co. purchased from us goods of Rs 12,000, Less : 5%
24	Sold goods for cash Rs 16,000
Ans.	Total of Sale Book Rs. 1,19,560

Purchase Return Book and its Posting

35. Record the following transaction in Sales Book of sh. Jain Dass and Post them into Ledger.

2006	
Nov 7	Returned to Sachdeva Furniture Store 10 Chairs @ Rs 100 each 2 Tables @ Rs 750 each Less : 10% Discount
22	Returned 8 chairs to India Furniture House @ Rs 150 Each being not of specified quality
24	Returned one Dining Table to Arora & Co., being not according to sample Rs 5,000
28	Allowance claimed from Delhi Furniture shop, on account of mistake in the invoice Rs 1,600.
Ans.	Total of Purchase Return Book Rs. 10,050

Sale Return Book and its Posting

36. Record the following transaction in Return inward Book and Post it into Ledger.

2006	
Jan 5	Goods returned to us by Grish & Co. worth Rs 8,000, Less 10% trade discount.
10	Shah Brothers, Jaipur, returned goods, being not according to sample worth Rs 6,000
16	Allowance claimed by Jai Singh & Co., Mathura, on account of a mistake in the invoice Rs 500
20	Goods returned by Mohan sons, being defective Rs 4,000
Ans.:	Total of Sale Return Book Rs. 17,700

RECORDING, POSTING AND BALANCING
Proper Subsidiary Book

37. Enter the following transactions in proper subsidary book.

2007	
Jan 1	Started business with cash Rs 80,000.
2	Deposited into bank Rs 50,000
3	Purchased from Sunil Lal Sons goods of the list price of Rs 20,000 at 10% trade discount
5	Returned to Sunil Lal & Sons goods of the list price of Rs 2,000
10	Issued a cheque to Sunil Lal & Sons in full settlement of their account
12	Sold to Sri. Krishan, goods worth Rs 25,000
15	Received Cash Rs 10,000 and a cheque for Rs. 8,000 from Sri. Krishan. The cheque was immediately sent to bank
17	Sold to Ram Brothers, goods valued at Rs 16,000

20 Cash Purchases Rs 15,000.

22 Withdrew from bank for office use Rs 10,000

23 Purchased from Bombay Trading Co. goods valued at Rs 24,000

24 Sri. Krishan returned goods worth Rs 2,000

25 Received from Ram Brothers Rs 9,800

27 Paid Rent by cheque Rs 2,800

Received commission in cash Rs 8,00

30 Paid salaries worth Rs 5, 000

Ans. Cash Balance Rs 40,600; Bank Balance 29,000; Total of Purchase Book Rs. 42,000; Sales Book Rs 41,000; Purchase Return Book Rs 1,800; Sales Return Book Rs 2,000;Trial Balance Total Rs. 1,47600

Dr. Balance: Cash Rs 30,600 ; Bank Rs 39,000; Purchases Rs 57,000

Sri Kirshan Rs 5,000 ; Ram Brothers Rs 6,000

Sales Returns Rs 2,000; Discount Rs 200; Rent Rs 2,800 and Salaries Rs 5,000.

Cr. Balances: Capital Rs 80,000; Purchases Return Rs 1,800; Sale Rs 41,000; Bombay Trading Co. Rs 24,000 and commission Rs 800.

CHAPTER 3 Banking Transactions

Learning Objectives

After studying this chapter you will be able to

- understand the meaning of 'bank',
- understand the functions of a bank
- know the meaning of RBI
- describe the function of RBI
- know the procedure of opening an account with a bank
- know the various banking documents
- know the process of transferring an account from one bank to another bank
- deal with the bank for individual as well as firms transactions
- understand the meaning and need of a bank reconciliation statement
- prepare a bank reconciliation statement.

3.1 Meaning of Bank

Bank is a German word which means 'to collect'. The main function of the banks is collection of funds as deposit's. with time bank have started performing other functions such as lending money, etc.

Banks have now occupied a very important place in the economic structure of the country. After independence, in order to achieve the social objectives of the country, banks were nationallised. According to the 20 Point Programme of then government, banks were entrusted with the responsibility of developing the undeveloped regions of the country. With time, the functions of banks have evolved may be defined as they financial institutions dealing in money and credit to achieve the economic and social objectives of the business.

According to the Indian Banking Companies Act 1949, "A bank is an institution accepting, for the purpose of lending or investment, in deposit money from public repayable on demand or otherwise, withdrawal by cheque, drafts, order or otherwise".

In the words of R.S. Mayers, "Banks are institutions whose debts are referred to as 'bank deposits' and they are commonly accepted in final settlement of other peoples debts".

According to Justice Homes, "The real business of a banker is to obtain deposits of money which he may use for his own profit by lending it out again".

3.2 Types of Banks

There are various types of banks as shown below.

Types of Banks

1. Commercial Banks
2. Agricultural Banks
3. Industrial Banks
4. Exchange Banks
5. Indigenous Banks
6. Cooperative Banks
7. Central Bank - Reserve Bank of India

- Commercial Banks – These banks have been established to assist trade, commerce and industry in their efforts towords development. Commercial banks assist their customers by depositing their funds in various accounts and releasing them as per their requirement. In current account overdraft facilities are also granted. Assistance is also provided by financing trade, commerce and industry. Individual persons can also open their account in commercial banks. In addition to the main functions of accepting deposits and lending money, commercial banks render various agency and other services.

- Agricultural Banks – Agriculture needs both short-term and long-term loans. The former loans are required for purchasing seeds, manure, oxen and plough etc. These short-term needs are met by cooperative banks. Long-term financial needs are regarding purchase of land, tractor, other equipments and for installation of tubewells. These needs are met by land mortgage to banks also known as agricultural banks.

- Industrial Banks – Industry needs long-term funds and this requirement cannot be effectively met by commercial banks. It is, therefore, necessary that industrial banks, be set up to meet the financial requirements of industrial enterprises. Unfortunately, in India, we do not have sufficient number of industrial banks. Instead, we haveIndustrial Development Bank of India and various financial corporate to meet the financial needs of industrial enterprises. In western countries like UK and USA, there are a large number of industrial banks.

- Exchange Banks – These banks help in the payments and financing of foreign trade. Many Indian commercial banks provide exchange services also. Mostly foreign banks work as exchange banks in India. Such banks are Citibank, Bank of Tokyo, Grindlays Bank, Chartered Bank etc. These banks deal in foreign exchange.

- Indigenous Banks – Before Independence, the financial needs of farmers and small business units were met by indigenous banks in rural areas. These banks were operated by *seths, sahukars, mahajans, sardars* etc. The special feature of these banks to advance loans at a very high rate of interest. Farmers and borrowers may approach them at any time. However, they have to pledge their ornaments, land or valuables. These banks are virtually exploiters of poor rural people. In spite of our development in financial fields by establishing big banks and financial corporations, indigenous banks are still serving the needs of the poor masses.

- Cooperative Banks – These banks are formed on a cooperative basis to meet the financial requirements of their members . The rate of interest is very low. The idea behind formation of these banks is to provide financial assistance to the weaker sections of the society. The government makes funds available to these banks at concessional rates.

- Central Bank – Every country has a central bank which is responsible for the overall control of cash and credit money. In India, Reserve Bank of India works as the central bank of the country.

3.2.1 The Reserve Bank of India

Genesis

The Reserve Bank of India was established on April 1, 1935 in accordance with the provisions of the Reserve Bank of India Act, 1934. Since nationalisation in 1949, the Reserve Bank is fully owned by the Government of India. The central office where the RBI governor sits and policy decisions are taken is located in Mumbai.

Governance

The Reserve Banks affairs are governed by the central board of directors which is appointed by the Government of India. The Reserve bank of India Act, 1934 governs Reserve Bank functions.

Functions

The basic functions of the Reserve Bank are to regulate the issue of bank notes, keep the reserves with a view to securing monetary stability in India, and generally to operate the currency and credit system of the country to its advantage.

Main functions of the RBI are as follows.

1. Monetary authority
   - Formulates, implements and monitors the monetary policy.
   - Objective : maintaining price stability and ensuring adequate flow of credit to productive sectors.
2. Regulator and supervisor of the financial system
   - Prescribes broad parameters of banking operations within which the countrys banking and financial system functions.
   - Objective : to maintain public confidence in the system, protect depositors interest and provide cost-effective banking services to the public.
3. Manager of foreign exchange
   - Manages the Foreign Exchange Management Act, 1999.
   - Objective : to facilitate external trade and payment, and promote orderly development and maintenance of foreign exchange market in India.
4. Issuer of currency
   - Issues and exchanges, or destroys, currency and coins not fit for circulation.
   - Objective : to give the public adequate supplies of currency notes and coins in good quality.
5. Development role
   - Performs a wide range of promotional functions to support national objectives.
6. Related functions
   - Banker to the government : performs merchant banking function for the central and the state governments; also acts as their banker.
   - Banker to banks : maintains banking accounts of all scheduled banks.

3.3 Functions of Commercial Banks

One of the essential functions of a banker, as defined in Banking Regulation Act, 1949, is to accept deposits from the public for the purpose of lending or investment. As a matter of fact, the relationship between a banker and its customer begins with the opening of an account by a banker in the name of his customer by accepting deposit of money. Hence such accounts are called Deposit Accounts.

The extensive lending operations undertaken by banks are not possible with the banks owned funds. They have to raise resources by way of deposits that can be made available to those who need funds for profitable deployments as well as for the purpose of lending. Deposits are, therefore, the basic resources, on which all their operations depend they are essential for the growth and profitability of the bank. All banks, therefore, strive to raise deposits. As a marketing strategy banks have devised various types of deposits which appeal to different strata of society with different needs and preferences. A person engaged with a firm which needs to we the account frequently prefers to open a current account in which there are no restrictions of depositing & withdrawls money regarding the number of times the account can be operated, but the account holder has to forgo an interest on the balance in his account. Over and above, bank also charge some amount by way of incidental charges on half yearly basis. Persons who don't need to operate the account that frequently would like to earn some interest on the balance held by them. For such persons banks have devised, savings bank account, which offer the facility of withdrawls (with moderate rate) on the balance held in the account. Taking the concept of interest further, banks have devised fixed deposits to cater to the needs of those persons who are prepared to leave their funds with the bank for a fixed period, at a higher rate of interest.

Deposits such as savings or current, as explained above, are by nature such which can be withdrawn any time, when required or demanded by depositors. These constitute 'demand' deposits of the bank. On the other hand, funds invested in fixed deposits cannot, as the term itself indicates, be normally withdrawn but can be available to the depositor only after the expiry of a specified period or term. These are classified as 'term deposits'.

Recurring deposits are meant for those who may not be in a position to put large amounts in the bank, but are desirous to save small amounts regularly every month. In view of the stiff competition among banks for attracting deposits, every bank branch has to adopt strategies for marketing its services and attract deposits. A planned approach to attract deposits, therefore, is called marketing of banking or deposit mobilisation. In order to extend the services of the bank to a large number of bank's clients, and to provide them with efficient service, every employee from top to bottom has to understand the importance of bank-marketing and take active part in it.

Marketing for deposits at the branch level, basically, depends upon two factors.

(i) Degree of customer satisfaction and documentary credits. This offer is a safeguard for exporters provided that the documents of the title of the goods are released to the importer only when bank has agreed to pay the agreed sum. From the importer's viewpoint, he knows that his bank will only take this liability on his behalf provided the documents of title are in accordance with his instructions to the bank. A confirmed undertaking is to be given by another bank, that if the issuing bank fails to honour its irrevocable undertaking, the payment to the exporter will be made by the confirming bank.

(ii) Image of the branch. Where the degree of customer satisfaction is high, the mobilisation of deposits becomes a comparatively easier task. Similarly, in an environment where the branch enjoys the image of being helpful to its customers, it is in a position to attract deposits with comparatively lesser effort. Where customer satisfaction is low and the branch also does not enjoy a good image, deposit mobilisation is a stupendous task. Even where customer satisfaction is high, and the image is good, the branch has to contend with

- competition from other banks, especially those which enjoy the same or higher level of customer satisfaction and image.
- competition from many other instruments of savings, for e.g., goverment securities, bonds and certificates, postal savings, company deposits, and financial institutions, mutual funds, shares and other capital market instruments.
- interest rates that are fixed by the Reserve Bank of India. There is no liberty to offer higher rates of interest.

All these factors constitute major constraints for a banker. The branch has therefore to plan its own strategy of deposit mobilisation. This has to be done in the following steps.

i) Identify and understand the area of operation of the branch. This can be determined both geographically, and according to the type of customers to whom it caters (e.g. special branches catering to non resident Indians, industrialists, agriculturists).

(ii) Prepare a list of existing as well as potentially important customers. This information can be procured by interacting with the various trade / professional associations, and also from directories, particularly telephone directories.

(iii) Analyse past performance, business mix, growth trends in the past few years, deposits etc. i.e. percentage of savings bank, current deposits and term deposit accounts, past trend of credit expansion and growth in the number of borrowers, alongwith the number of borrowers having deposit accounts.

(iv) Assessment of future potential, growth of industrial/ commercial activities in the area served by the branch, construction activities, scope for deposit oriented credit,etc.

3.3.1 Saving Bank Account

Savings bank accounts have been designed to inculcate the habit of 'thrift' i.e. saving. These accounts cater to the needs of those whose requirements for drawing the funds are limited and also not frequent. The savings bank account, in other words, is a thrift deposit that offers the facility of drawing funds whenever required and, at the same time, it enables the depositor to earn a moderate interest on the balance held in the account as stipulated by the Reserve Bank of India. From the banks point of view saving banks accounts offer stable deposits, with no wider fluctuations. Banks are in a position to deploy these funds profitably without any apprehension of sudden heavy withdrawals.

Who can open an account?

(i) Any person approved by the bank may open a saving account by agreeing to comply with rules provided by the bank.

(ii) A savings account may be opened

- by person in his/her own name
- by two or more persons in their joint names payable to
  - both or all of them or the survivor or survivors of them, or
  - either or any one or more of them or the survivor or survivors of them, or
  - former / latter or survivor or a particular person during his lifetime or survivors jointly or survivor.

(iii) Accounts may be opened in the names of illiterate or blind persons or in the names of, or on behalf of, minors either singly or jointly.

(iv) Accounts may, in approved cases, be opened in the names of associations, clubs, regimental funds of military units, or similar other non-trading institutions for purposes of depositing savings, provided the relevant bye-laws, rules etc., are found acceptable to the bank and the rules are strictly adhered to.

(v) Reserve Bank of India has prohibited banks to open savings bank account in the name of any trading or business concerns, whether such concern is proprietary, or partnership firm, or a company, or association as detailed out subsequently.

Type of Accounts

Different banks have laid down their own stipulations regarding minimum balance to be maintained in saving bank account for operations in the account with or without cheque book facility.

(i) Cheque operated account : A minimum balance of Rs.1000 and Rs. 500 should be maintained in such account if back is situated in urban areas and rural areas respectively.

(ii) Non-cheque operated account : A minimum balance of Rs. 500 and Rs.250 should be maintained in such account if bank is situated in urban areas and rural areas respectively.

How to Open an Account

The applicant is required to complete and sign the prescribed form of application. Appropriate declaration (s) thereon in respect of accounts in joint names are also to be completed. The application should be presented to the bank with an initial deposit in cash. As per recent guidelines, an introduction is compulsory in all the savings bank accounts, even when no cheque-book facility is sought.

Each account should be given a distinctive number which is mentioned in the pass-book supplied to the account holder. This number must invariably be quoted in all pay-in-slips, cheques / withdrawals and correspondence with the bank.

Procedure to open an Account

Individual Account

when completed account opening form and specimen signature sheet (attested by supervising official) along with minimum deposit are received and the account is opened, pass book is issued. In case a cheque book facility is required by a depositor, the stipulation of a minimum balance needs to be complied with and then a cheque book should be issued after obtaining an acknowledgment. If it is a cheque-book facility account then the cheque-book is issued after getting the acknowledgment.

Savings accounts are balanced once a month. Immediate credit is provided for cheques upto Rs 2,500/-. The account can also be transferred from one branch to another on request without any charge. All related papers, such as account opening form, S.S. card, standing instruction sheets and passbook may be handed over to the customer if he so desires in a sealed cover. Alternatively, it may be sent by registered post.

Joint Account

Procedure is the same as in individual account, except that instructions about operation of the account should be obtained. If no instructions are given about the operation of the account, it will have to be operated jointly.

Account in the Names of Minors

A person under the age of 18 years is a minor. If a guardian of his person, or property, or both has been appointed by a court, or if the superintendence of his property has been assumed by a Court of words before the minor assumed the age of 18 years, he remains minor till he completes the age of 21 years. All contracts by minors are void ab-initial expecting contracts for necessities of life such as food, clothing and accommodation for his benefit. His estate becomes liable for contracts in respect of his necessaries and other benefits. In case of all other contracts a minor may repudiate his promise or contracts.

Banks do not open current accounts in the names of minors. However, savings, fixed and recurring deposit accounts are freely opened.

A bank account in the name of the minor may be opened in one of the following ways.

(a) In the name of minor himself / herself.

(b) In the joint names of minor with his/her guardian.

(c) In the name of the minor under the natural guardianship of his/her father, and if he is dead, under the natural guardianship of mother, and if both are dead, under the guardianship of a person appointed by a competent court.

In Case of (a) an account can be operated by minor himself / herself whereas in case of (b) minor can operate the account only jointly with his/her guardian while in case of (c) the account will be operated by guardian on behalf of minor.

In case of (a) and (b) minor must have obtained the age of 12 years and should be in a position to read or write English, Hindi or regional language.

The date of birth of a minor, as stated by his guardian, is recorded by the bank. On becoming a major, the minor's account is transferred to a new account in the sole name of the minor. Money lent to a minor cannot be recovered from him even after he attains majority.

Account in the name of Married Woman

(i) Hindu married women are governed by Hindu Succession Act, 1956. The women relating to other religions are governed by

- The Married Women's Property Act, 1874
- The Indian Succession Act, 1925.

If the women are not prohibited from opening accounts by the above acts, they may be permitted to open deposit accounts with the bank.

(ii) A contract entered into by a *purdanashin* woman is not a contract free from all defects as she observes complete seclusion. Photographs may be waived but independent witness is necessary to authenticate each transaction. Formalities to open the account are the same as for individual accounts. Since it is very difficult to determine the identity of such women, banks should avoid opening such accounts.

Account in the Names of Lunatics

As per Indian Contract Act, a person with an unsound mind cannot enter into a contract. Hence no account can be opened in the name of a lunatic.

Account in the Names of Drunkards

A person with an unsound mind cannot enter into a contract. A drunkard being a person with unsound mind, should not be allowed to open any account.

Account in the Name of Insolvent Persons

No account should be opened in the name of a person who is declared an Insolvent. If a person is declared insolvent subsequently, such account should be allowed to be operated only by

- Official receiver
- Liquidators : Persons appointed to wind up the joint stock company.

Account in the Names of Blind Persons

A blind person is not legally incompetent to enter into a contract and therefore he can open and operate an account with the bank. Due to the physical infirmity, however, banks finds it difficult to open an account although there is no legal bar.

If the account of a blind person is opened, he may be permitted to sign withdrawals etc., if his signature is uniform. Otherwise, his left hand thumb impression may be obtained on the withdrawal. While signing the cheque, his signature should be witnessed by other person besides bank official and payment should also be witnessed by other person besides the passing officer.

Account in the Names of Illiterate Persons

- An illiterate person is not permitted to open a current account. He may however, open all other types of deposit accounts.
- An illiterate person may open an ordinary savings bank account in his sole name or jointly with other persons(s).

  Where one of the depositors is literate, and survivors or 'either or survivor' etc. may be opened, only the literate depositor will be allowed to withdraw money from the account by means of cheque. In case of the account of an ittiterate depositer the relative cash deposit voucher should be filled in by the savings bank clerk.
- The left hand thumb impression of the depositor should be obtained on the account opening form in the place provided for signature of the depositor and on the specimen signature sheets in the presence of a supervising official authorised to sanction opening of accounts. He should attest the thumb impression in the same manner as in the case of specimen signature. In case of females, right hand thumb impression should be taken.

  Brief details of one or two identification marks, if any, of the depositor, such as a mole or scar, should be noted on the account opening form and the specimen signature sheet under authentication of the authorised official.

Photograph

Arrangements should be made to take, at the bank's cost, a passport-size photograph (two copies) of the depositor.

- The photograph should be renewed every three years.
- Where arrangement cannot be made for taking photographs immediately, the account may be opened subject to the photograph being taken within a few days after opening of the account.

If it is difficult, for any reason, for the branch to make arrangements for taking a photograph, the depositor should be advised to submit two copies of his photograph to the bank, and the cost of the photographs submitted should be reimbursed to the depositor on his producing the paid bill from the photographer. In such cases, the authorised official must satisfy himself that the copies of photographs submitted by the prospective depositor are identical in all respects and that they, in fact, are his photographs.

One copy of the photograph should be pasted on the account opening form, and the other on the specimen signature sheet which should be authenticated by the authorised official in the same manner as in the case of specimen signature. Care is to be taken to see that part of the authenticating signature appears on the account opening form/the specimen signature sheet and part on the photograph. Thereafter, the photographs should be covered by fixing a piece of transparent paper over them with the help of cello tape to prevent their being soiled or disfigured due to frequent handling. Where it is not possible to obtain a photograph due to want of facilities for taking photographs or for other reasons, for e.g. when a lady depositor resents being photographed, the branch manager or manager of division, at his discretion, may waive this depositor on the account opening form, the specimen signature sheets and the cash voucher, and instead should get all documents witnessed by a respectable outsider acceptable to the bank.

The authorised officials should explain the implications and conditions for the operation of the account to the illiterate depositor and append a certificate to the account opening form for having done so. A remark in red ink, or by means of rubber stamp, to indicate that the depositor is illiterate should be prominently made on the account opening form, specimen signature sheet and the ledger account under the initials of a supervising official.

Operations of the Account of Illiterate Persons

(a) **Receipts :** When an illiterate depositor calls on the bank for depositing money into his account, the savings bank clerk should fill in the pay-in-slip. The depositor should affix his left hand thumb impression in the place provided for his signature. The chief cash officer/cash officer should sign the pay-in-slip after personally ascertaining from the depositor the amount deposited in the account and, in token of having done so, affix his initials against the amount mentioned in the pay-in-slip.

(b) **Withdrawals :** Ordinarily, only personal withdrawals against production of the relative passbook will be allowed to an illiterate depositor. When he desires to effect a withdrawal, he should call at the bank and present his passbook to the savings bank clerk. After the depositor is identified on the basis of the photograph on the bank's record and/or the identification marks, if any, it should be ensured that the withdrawal is being made by the depositor himself. The amount of withdrawal should also be ascertained from the depositor and, in token of having done so, the clerk should affix his initials against the amount mentioned in the withdrawal order form. In case the depositor's photograph is not recorded, his thumb impression on the withdrawl order form should be attested by an independent witness acceptable to the bank. The name and address of the witness should be recorded on the withdrawal order form below his signature. When the depositor is unable to the present personally to withdraw the amount, he may tender a letter of authority in the prescribed form of the savings bank rules with his left hand thumb impression duly attested by 'two' persons known to the bank or a magistrate under his court seal. The passbook should accompany the letter of authority and, where necessary, the presenter must be identified to the bank's satisfaction.

(c) **Closing of Account :** The thumb impression of the depositor on the savings bank account closing form should, in all cases, be witnessed by an independent witness acceptable to the bank. Also, the passing official should explain to the depositor, in the presence of the witness, that no more money is due to the depositor from the bank as the entire balance including interest, if any, has been paid to him and the depositor ceases to have any claim on the bank in regard to his deposit.

Transfer of Account (Non-cheque Book holder's account)

Accounts of illiterate depositors may be transferred at their request from one branch to another like other accounts.

Banks are also permitted to open saving bank accounts in the name of the following

- Associations, clubs or similar non-trading institutions provided they are exempt from payment of income-tax
- Regimental funds of military
- Individual employees of schools and colleges with the employers for depositing provident fund money
- Primary cooperative credit society which is being financed by the bank
- Small Farmers Development Agency (SFDA)
- Marginal Farmers and Agricultural Laborers Agencies
- Drought Prone Areas Programme
- District Development Authority
- District Rural Development Agency/Society
- Integrated Rural Development Programme
- Integrated Tribal Development Agency
- Agricultural Produce Market Committees
- Khadi and Village Industries Boards
- Societies registered under the Societies Registration Act, 1860 or any other corresponding law on force in state or union territory
- Companies permitted not to add to their names the word ‘Limited’ or the word ‘Private Limited’
- Institutions whose entire income is exempted from payment of income tax.

However, no bank should open a saving bank account in the name of government departments / bodies dependent upon budgetary allocations for performance of their functions / municipal corporations or municipal committees / panchyat samities / state housing boards / water & sewage/ drainage boards / state textbook -publishing corporations/ societies/ metropolitan development authority/ state district level housing cooperative societies etc. or any trading or business concern, whether such concern is preparatory or a partnership firm or a company or any association.

Loss of Passbook

No charge is made for the passbook first supplied to a depositor or for any passbook in continuation of the original passbook. If lost or spoilt (except in circumstances over which the depositor had no control), the depositor is charged one rupee for issue of a duplicate passbook, after inquiry is made.

Standing/ Special Instructions

Standing instructions for payment of insurance premium, club membership etc. are accepted on savings bank accounts also. Standing instructions for transferring fixed sums on a regular basis to recurring deposit accounts in the name of the account / holder himself or in the name of any other person are also accepted.

Transfer of Account (Cheque book holder's account)

Accounts may be transferred to any other office of the bank, free of charge. Should the depositor wish to transfer his account, he should make a written application for the transfer to the office where he maintains his account and send it along with his passbook, either to that office or to the office to which he wishes his account to be transferred. If the depositor maintains a cheque-operated account, he may, on receipt of an advice that the account has been duly transferred, continue to use the unused cheque forms in his possession after altering the name of office and account number and further authenticating the alteration under his signature.

Closing of an Account

A depositor wishing to close his account should present his passbook in order that the amount of interest due on the account may be entered therein and a final balance struck. The amount will then be paid to the depositor and his receipt taken; the passbook will be returned to the depositor after cancellation. The unused cheque forms, in his possession should also be returned to the bank.

Payment of Interest to Account Holders

Interest on savings bank account is paid as per rate of interest as specified by Reserve Bank of India on half yearly basis or annually as per practice prevailing in various banks. In savings bank account interest is paid on the basis of monthly product. The minimum balance kept in saving bank account, between the tenth and last day of the month, constitute products for that particular month. Products for all the six months, or 12 months as per practice, are totalled and it is on this total amount that interest amount is calculated. Interest is payable only if the amount of interest is not less than Rs1/-. There is no ceiling for amount of interest payable to depositor. As per practice, members of staff enjoy the benefit of one percent higher rate of interest on their balance in saving account. Practice of leaving incidental charges on these accounts, which violate rules regarding minimum balance and number of withdrawals is also balanced by almost all the banks.

Settlement of Balance in Deceaseds Account

On the death of the customer, the contractual relationship stands terminated and hence the operations on the account should be stopped. On receipt of the notice of death of the customer, stop-payment-note should be made in the relative account in the ledger and the original death certificate should be called for, as early as possible. Brief contents of the original death certificate should be entered in Sundry Documents Register before the death certificate is returned.

If the customer dies leaving a Will, the bank should insist that the Will be probated from a competent court of law in terms of the Indian Succession Act. Where succession certificate is produced, the relevant portion of the court order must be entered in Sundry Documents Register and the balance in the deceaseds account paid to the successors as directed by the court.

Depending upon the circumstances of each case, bank may also decide to waive the operation of succession certificate, at its discretion. In that case the bank must be satisfied, through independent discreet inquiries, that the deceased died intestate and the legal heirs are not required to obtain succession certificate for disposal of other assets, if any, left by the deceased. The legal heirs are required to execute a stamped indemnity letter alongwith two sureties, each good for the amount invited, before the bank can pay the balance in the deceaseds account to the legal heirs. The legal heirs must also submit an affidavit sworn in by an independent person in the locality unconnected with the deceased, stating the names of the legal heirs. Where necessary, heirship certificate can also be called for.

3.3.2 Current Account

Meaning of Current Account

A current account is a running account, which can be operated upon any number of times during a working day, and thus there is no restriction on the number and amount of withdrawals from it. Since the banker is under obligation to repay these deposits on demand, they are called demand liabilities. the bank has to keep sufficient cash reserves to meet such liabilities. Thus, bank cannot utilise these funds and as such no interest is payable on current deposits. These accounts meet the requirements of businessmen, joint stock companies, institutions and other profit-making bodies. Thus current deposits which are non-bearing form a major source of interest free funds for bank. Opening of current deposits creates a contractual relationship between banker and customer, respectively.

Opening of Current Account

(i) Before opening an account, the respectability and identity of the person opening the account should be ascertained. Opening of an account without proper and acceptable introduction amounts to negligence on the part of the banker. In such an event, the bank loses the legal protection available to a collecting banker under Sections 131 and 131A of the Negotiable instrument Act.

(ii) Introduction for opening a current account may be given by any one of the following

- Any constituent whose account has been satisfactorily conducted
- Any respectable person of the locality known to the bank
- Any member of the supervising staff confirmed in bank's service
- Any confirmed awarded staff employee
- Another branch
- Another bank

As far as possible, the introducer should be present in the bank to give the introduction and sign on the account opening form. Where it is not possible, he may do it on the application form or by means of a letter which should be attached to the account opening form. A letter of thanks has to be sent to him to ensure that the signature of the introducer is not forged. Also, a separate letter of thanks has to be sent to the depositor for extending patronage to verify the bonafides of the depositor.

In case of introduction by another bank/ branch, as an additional precaution, introduction by means of a separate letter has to be taken.

The introducer will not be liable to the bank unless there in a criminal conspiracy between the depositor and the introducer. The advantage of introduction is that the bank may persuade the account holder through the introducer of recovery of any dues, where necessary.

Who can open current Account

The following can open current account

- Individuals - singly or jointly

  (An individual who is not competent to enter into contract such as minor illiterate, insolvent, lunatic, drunkard etc. cannot be allowed to open current acccount.)
- Sole proprietry concern
- Partnership firms
- Clubs, associations or other benefitiary bodies
- Joint hindu family
- Limited companies: private and public
- Corporations and registered societies etc.
- Trust accounts
- Executors / administrators.

Interest

As explained earlier, no interest is payable on the balance in current accounts. However, Since May 1983, banks have been permitted to pay interest on balances lying in current accounts in the name of deceased depositor from the date of death of depositor till payment to its legal heirs. Interest on such accounts is payable at saving bank rates. Similarly, banks have been permitted to pay interest on balances in current accounts maintained by Regional Rural Banks.

Basic Document for Opening a Current Account

For a current account, the basic document to be taken from a customer is the appropriate account opening cum specimen signature form.

Formalities

The formalities to be complied with and the documents to be obtained for opening current account for various types of customers are as under.

(i) Single individual

Only the account opening cum specimen signature form are needed.

(ii) Two or more Persons

Account opening form should be signed by all the persons in whose names the account is to be opened. The specimen signature of all persons also has to be obtained there on.

(iii) Firms

- Account opening form has to be signed by the sole proprietor partners who will be operating the account.
- In case of partnership firm, a partnership letter has to be obtained in all cases signed by all the partners.

  The partnership letter stipulates that notice of change in partnership will be advised to the bank. It binds the partners jointly and severally. When minors are admitted to the benefits of the partnership, the guardians will sign the partnership letter on their behalf. Names of minors with their dates of birth are to be mentioned in the partnership letter.
- Specimens of signatures of the proprietor / all the partners who are allowed to operate on the account are mandetary.
- In case of partnership firm a copy of the partnership deed (if available) has to be submitted.

Note:

- Registration of a partnership firm need not be insisted upon for opening an account as registration does not make partnership a legal entity and does not affect the relationship with the bank.
- In case of individuals or firms trading under impersonal names or under names other than their own, it is desirable that the same accounts as entered in the ledgers show the connection of the proprietors / partners with the concerns.

(iv) Joint Hindu Families

- Account opening form.
- Joint Hindu Family letter signed by all the adult Coparceners(Joint Hindu Family letter stipulates notice of any changes to be advised that fresh letter may be obtained). It also presumes that the business carried on by the firm is ancestral. If the business is later on found to be not ancestral, the Coparceners will also be personally liable to the bank in respect of the debts due by the firm to the bank. If ancestral, the Coparceners are liable to the extent of their share in the family property.
- Specimen signature of the person authorised to operate on the account.

(v) Liquidators

- Account Opening form
- Order of appointment as liquidators issued by a competent court.
- Specimen signature on the form for private individuals.

Every official liquidator is required to maintain a personal ledger account with the Reserve Bank of India or where it is not established, with the State Bank of India or any of its associates, or any nationalised bank acting as the agent of the Reserve Bank of India terms of the court order.

Liquidators cannot delegate their powers to third parties. When more than one liquidators is appointed, they may not authorise less than two of their number to sign generally, unless empowered to do so at the time of their appointment although they may all authorise one of their number or a third party to sign a particular document.

(vi) Limited Liability Companies

(a) Private Limited Companies

- Account opening form
- A copy of the company's Memorandum and Articles of Association (to be filed at the branch) updated and certified as such
- Certificate of incorporation-for-inspection and return

Note: The particulars of Certificate of Incorporation have to be entered in the power of attorney register.

- Certified copy of the resolution of the board of directors for opening the account and for the conduct of the account the specimens signatures of persons authorised to operate the account.

(b) Public Limited Companies

In addition to the five documents detailed above, the original Certificate of Commencement of Business must also be submitted to the bank in the case of public limited companies. The particulars of this certificate will be scrutinized and entered in the Power of Attorney Register and the certificate will be returned to the company.

The Certificate of Commencement of Business certifies that the company is entitled to commence business. This certificate is issued by the Registrar of Joint Stock Companies on filing a declaration that the minimum subscription declared in the prospectus has been raised by the issue of shares within the statutory limit of 120 from the first issue of prospectus.

A private company is not required to obtain a Certificate of Commencement of Business as no public issue of shares is involved.

Accounts in the names of new public companies can be opened in anticipation of the receipt of the Certificate of Commencement of Business provided

- The accounts are to be used for the deposit of moneys received from the applicants for shares.
- Only where the local head office has agreed to the bank acting as the company's bankers.
- Cheque books are not supplied unless and until the certificate to commence business is received.

(vii) Military Funds

Public funds of defence services may not be deposited with any bank other than the Reserve Bank of India or the State Bank of India or one of its Associates. This restriction does not apply to 'Regimental Fund's. Only 'Order' cheque is not issued on 'public fund account'. Even temporary overdrafts are strictly prohibited on such accounts.

(viii) Firms/ Clubs / Associations

- Account opening form
- A copy of bye-laws of the club or association or its rules and regulations
- A copy of the resolution passed by the club or association or society governing the conduct of the account together with the specimen signatures of the authorised signatories
- Whenever there is a change in the person occupying a post (office bearers post), a certified copy of the resolution regarding the new appointment of the office bearer is obtained and noted in the ledger head.

Note:

Accounts in the names of funds, associations and societies, whether registered under the Societies Registration Act or not, are in the nature of fiduciary accounts. Therefore, the precautions to be taken in the conduct of trust accounts apply equally to the above accounts.

Accounts in the name of certain funds, mostly connected with recreation and usually of temporary nature which are not registered and have rules drawn up, may also be opened

- only in the case of undoubtedly reliable constituents.
- in the personal names of constituents, with additions such as Police Account, Sports Accounts, etc.

Accounts may be opened in the name of individuals with additions like 'Sports Account' indicating that the funds are held in fiduciary capacity. Full inquiry regarding the existence of the files, resolutions of the meetings, etc., should therefore be made and the results of the inquiries should be noted at the head of the accounts, when they are opened. In the absence of any rules or resolutions of meetings to define their powers, parties holding such funds may be presumed to have full control over them.

(ix) Cooperative Societies:

- Account opening from
- The society must have been registered under the Cooperative Societies Act
- A copy of the bye-laws of the society, duly updated and certified
- A copy of the resolution passed by the board of directors governing the conduct of accounts
- Specimen signatures of the authorised signatories, and
- Permission by the Registrar of Cooperative Societies for opening of an account with the bank.

Note:

A Cooperative society is a body corporate of individuals or other bodies formed for the fulfillment of certain social and economic objectives.

(x) Minors:

- Minor becomes a major at the age of twenty one when
  - He/she is of foreign domicile
  - A guardian of his/her property or person has been appointed by court, or
  - His/her property is under the superintendence of a court of wards.

  In other cases, minority ceases to be a minor after the age of eighteen in terms of the Indian Majors Act.
- No current account should be opened in the name of, or on behalf of, a minor without the prior permission of the Local Head Office unless a guardian of the property (not merely of the person) of the minor is appointed under the Guardian and Wards Act. It will not be possible to recover the overdrafts created inadvertently in the minors account through a court of law.

Note:

The guardian must not be allowed to draw on the account after the minor has come of age or after the minor's death.

(xi) Executors/ Administrators

Executors and administrators are the persons who are appointed to conduct the affairs of a person after his death. A person who makes his will is known as ‘testator’. He appoints another person through his ‘will’, known as ‘Executor’. If the person appointed as executor refuses to accept his assignment or dies then the court appoints a person for this purpose, who is known as 'administrator'. Thus, while an executor is appointed by 'will' the administrator is appointed by a court through a letter or probate.

To open such an account, the balance in the account of deceased person is transferred to it.

ABC Executors (or Administrators) to the Estate of XYZ - deceased.

The banker should be very particular in conducting the account. The executor should be permitted to operate the account of the deceased only after he has obtained the 'Probate' from the court, whereas the administrator is authorised to do so only after he has secured the Letter of Administration. The banker should not permit the transfer of funds from such an account to the personal account of executor/administrator.

(xii) Trust Account

A trust is generally formed by means of document called Trust deed. while opening the account in the name of persons in their capacity as a trustee, the banker should thoroughly examine the trust deed and examine the particulars such as names of trustees, their powers and functions. The banker should not allow diversion of funds from Trust Account to the Personal Account of trustees. Every care should be taken to safeguard the interest of beneficiaries of Trust.

3.4 Cheque Book

A cheque book is issued only on completion of all the formalities connected with the opening of the account. The constituent has to give his receipt for the cheque book in the Cheque Book Register. Further cheque books will be issued on receipt of the requisition slip attached to every cheque book, duly signed by him. When a cheque book is issued to an authorised person of the account holder, or is sent by post, he will be advised separately and his acknowledgement will be obtained to ensure that the cheque book has actually been received by him. When an acknowledgement is not received, the first cheque presented by the bearer should be referred to the manager and only then paid.

3.4.1 Statement of Accounts

A monthly statement of accounts is supplied to every current account holder. The statement is copied from the ledger neatly after the daily checking is completed and dispatched promptly in order to help the customers to know the state of their accounts. Daily/weekly/fortnightly statements can also be issued if required. A duplicate statement of accounts may be issued and a charge of Rs 2/- per ledger folio levied. Passbooks may be supplied to customers on their request.

3.4.2 Stopping Payment of Cheque

Immediately on receipt of instructions to stop payment of a cheque, the banker should firstly verify if the cheque is paid or not. It is absolutely necessary to note the time and date of receipt of cheque. Then the particulars of the cheque should be entered in the Stopped Cheque Register and in the list of Stop Payment Cheque supplied to the other officials, ledger keepers, tellers etc. The word 'stop' must be written in the ledger in red ink. In addition, a special adhesive label with the word 'STOP' should be pasted on the edge. This will be carried forward in all pages. The constituents should be advised that the bank will be responsible if a stopped cheque is paid after receiving the instructions to stop payment. The actual date and time of the receipt of such a notice must be recorded in the ledge. The loss of the blank cheque form issued to constituents must be recorded in the Lost Document Register instead of Stopped Cheque Register.

3.4.3 Loss of cheque Book

The loss of a cheque book must be recorded in the Lost Documents Register and in the ledger accounts in red ink. No cheque drawn on a lost form should be paid without the drawers consent.

3.4.4 Change of Address

When a change of address is received, an acknowledgement should be sent to the customer at the old address as well as at the new address, just to ensure that the customers address is not fake or fictitious.

3.4.5 Irregular Accounts

When an account holder does not conduct his account properly (when cheques have to be returned frequently for lack of funds etc.) his attention should be drawn to this fact. If there is no improvement, he should be advised to close his account. If he fails to do so, no credit is to be accepted in the account and no fresh cheque book will be issued to him.

3.4.6 Cheque Referred and Returned Register

All debits to account which exceed the credit balance or the debit balance in excess of the drawing power must be entered in this register. The register and the cheque is then sent to the branch manger or manager of the division for his instructions. Such cheques have to be registered and sent to an official not below the rank of an accountant.

3.4.7 Overdrafts in Current Account

Constituents should not overdraw their accounts even for small amounts without having made previous arrangement. Clean overdrafts may be granted in current accounts in special cases and secured overdrafts against approved securities. A letter requesting for a clean overdraft will be taken from the account holder before it is sanctioned. Suitable repayment arrangement is to be insisted upon. A clean overdraft should be repaid within a year.

3.4.8 Balancing

The current account ledgers are balanced every week on different dates by employees selected by drawing ballots. The balances as on the close of business on the balancing day are jotted down in separate books. The total of credit balances and debit balances is arrived at and the difference between the two totals is the balance of current accounts. As on that date, the balance should tally with the balance as per the general ledger. The purpose of balancing is to locate mistakes, if any, in the balances. Ledger wise balances are maintained through Progressive Balance Books.

3.4.9 Transfer of an Account

Accounts may be transferred to any branch of the bank or associate bank free of charge.

3.4.10 Dormant Account

A current account becomes Dormant when there are no transactions in the account continuously for six months. The ledger keeper should scrutinise all accounts monthly and brand such accounts where there are no transactions for the previous six months with a rubber stamp reading 'Dormant Account to refer first withdrawal to the branch manager/ manager (accounts)'. A debit to that account will be referred to the concerned official in the 'Cheque Referred and Returned Register' for his instructions. A specimen signature will be verified before passing the debit. After payment of the cheque/debit the account becomes a running account and the 'Dormant Account' stamp affixed earlier is cancelled. Where cheques drawn on dormant accounts are presented for payment in cash, the presenter should be interviewed by an official, just to satisfy ourselves that the presenter is the account holder or his representative.

3.4.11 Inoperative Accounts

At the time of transfer of transaction sheets from a ledger binder, on 31 December, a list of current accounts that have not been operated during the past 12 months, excepting those which have remained inoperative for special reasons, should be prepared and approved by the branch manager/manger of division.

The relative ledger sheets are thereafter removed from the operative ledgers and placed in a separate ledger to be styled as Inoperative Current Accounts Ledger.

It is not necessary to transfer balances of these accounts to inoperative current accounts nor necessary to record the particulars of the accounts in Inoperative Accounts Register. When the ledger sheets pertaining to such accounts have to be transferred from the operative ledger, and vice-versa, i.e. when the inoperative accounts have to be reactivated, usual debit and credit vouchers will have to be prepared, and the inoperative ledger will be treated like any other ordinary ledger.

3.5 TERM DEPOSIT

Deposits which are repayable after the expiry of a fixed period ranging from 46 to120 days are classified as 'term deposits'. The period is agreed upon by the bank and the customer at the time of deposit and may later be varied by mutual consent. The rate of interest is determined by the directives of the Reserve Bank of India issued from time to time.

3.5.1 Interest

Rates of interest payable on term deposits are stipulated by the Reserve Bank of India, through its directives issued from time to time. No bank can pay interest at the rate higher than what is prescribed by RBI. However, Reserve Bank of India, in its directives, provides for offering higher rates by cooperative banks as well as Regional Rural Banks to enable them to attract deposits and thus compete with bigger banks. These rates of interest are subject to revision by Reserve Bank of India frequently (at present maximum higher ceiling is 10%. Members of staff, of course, enjoy benefit of 1% higher rate of interest). The stipulation as regards minimum and maximum amount to be accepted varies from bank to bank and deposit scheme also but invariably in multiples of hundreds only.

The interest on term deposits is payable quarterly or half yearly, and in case of monthly deposit schemes it is payable on a monthly basis. Banks are, as such, required to provide for interest amount so payable during the period. This is generally done on a half yearly or yearly basis. Procedure for provision of interest varies from bank to bank. As per directives of Reserve Bank of India, interest on all types of deposits is payable at quarterly or longer rests. interest on fixed deposits for 12 months and above is paid on a quarterly basis. However, in receipt of deposits such as recurring deposits and re-investment plan schemes, interest is compounded quarterly. The current rates are effective from 03.07.1991.

Term deposits may be opened in different styles such as payable to either or survivor, any one or survivor, former or survivor and latter or survivor. Nomination facility is also available.

3.5.2 Term Deposit Account Ledger

Accounts are opened in the consecutive order of TDR numbers in the Term Deposit Ledger, which may be maintained segment wise. There are no rate wise sections in the ledger. The account number is on year wise running serial number e.g. 88/1, 88/2 etc. When segment wise ledgers are maintained, different series of account numbers suitably prefixed may be used.

The full particulars of the depositor, account number, repayment instructions, position regarding nomination, date on which minor attains majority, date of issue, TDR number, TD Register Section number, period , rate of interest, date of maturity and amount is entered in the ledger. There is also a provision for entering periodicity of interest payment desired, amount of the periodical interest, date on which the interest is payable, account to which interest is to be credited and total interest payable, with provision for entering 36 interest payments. The ledger has provision for entering two TDRs on one folio. In case the TDR is for more than 36 months' and a monthly interest payment is required, next block is to be left blank so that payment of interest may be entered in this block too.

As regards the 'Total Interest' column, care should be taken to fill in only the total discounted value of interest payable, if monthly interest is desired.

3.5.3 Term Deposit Register

All vouchers on term deposits/term deposit interest account are entered in the Term Deposit Register, wherein separate openings period/ interes twise are made. The vouchers are entered in the appropriate opening and allotted a section number. This number is also indicated in the ledger account. The TD Register is maintained in a loose leaf binder. At the end of the binder a summary sheet is provided, wherein a summary of the daily transactions is entered. The figures are carried over from the Summary to the Clean Cash Book. The filled in sheets of the register are removed at periodical intervals and kept in a transfer binder. At year end balances are carried over to fresh sheets, the old sheets removed, and all the sheets pertaining to the year are bound and retained as records.

Checking

The entries in TD Register are checked every day with the vouchers by an officer other than the desk official (where there is another officer). The entries are also compared with the entries in the ledger. While doing this all interest payments over Rs100/- are rechecked. The date cards are checked to ensure that all accounts are carried out, reminders due are sent and there is noting in respect of cancelled paid TDRs. The balance in the summary is tallied with the general ledger.

Payment/ Renewals

A term deposit becomes due for payment on the working day following expiry of the specified period of deposit. If the date falls on a Sunday, holiday or non-business working day, banks are permitted by Reserve Bank of India to pay interest at originally contracted rates on deposit amount for such holiday if so demanded by depositor. However, interest can be so paid only if deposit receipt is presented for encashment only. (In case of renewal it will be deemed to be renewed from the date on which it becomes due for payment).

When the TDR is presented on due date the date of payment is entered in the TDR ledger and authenticated. Date of payment is entered in the column. The amount of interest paid is entered in the ledger. The passing official has to ensure that the total interest paid tallies with the interest recorded at the time of issue. TDR is used as a debit voucher for TDR A/c/ TDR Interest A/c. For renewals, a fresh account opening form is not necessary.

Receipt not Presented on the Due Date

On the due date, term deposit account for principal, and term deposit interest account for interest/ balance of interest, are debited and the total amount credited to over-due term deposits account in the current account by using plain debit/credit vouchers. The details are entered in a special register called Overdue Term Deposits Register. The depositor is reminded on a standard form. When the receipt is subsequently presented, payment is made by debit to Overdue Term Deposit Account after noting the contra date in the register also. However, practice again differs from bank to bank.

Payment Before Maturity

A depositor may request for payment before maturity. Such request will be considered at the banker's option. The depositors discharge as received payment of principal and interest/ balance of interest due by partial forfeiture of interest' over a revenue stamp will be obtained on the receipt together with a written request from the depositor. The rate of interest on such deposit paid before maturity will be 1% less than the rate applicable for the period for which the deposit has remained with the bank. In case of deposits payable to the depositors jointly, the discharge of all parties is required. In the case of E or S, and F or S, the discharge of any one is sufficient. The difference in interest provision made and interest actually paid will be noted and consolidated and adjustment is made during interest provisions at the month end. The entry in the date card will be marked off.

3.5.4 Balancing

As per practice prevailing in various banks, outstanding term deposit receipts are jotted down in a register, categorywise, separately. It is then totalled and tallied with the respective category in bank's General Ledger. This is done preferably on the last Friday of the month or quarter or half year, as per the practice prevailing in the bank. Balancing is done both register wise and ledgerwise.

3.5.5 Addition, Deletion of Names

Banks sometimes receive request for addition or deletion of name (s) in deposit receipts. Such requests should be studied carefully. Deposit receipt is issued in the name of one person and if he requests for addition of name, bank should have no objection. However, if deposit receipt is in joint names and payable to two or more persons, and if request is from only one of the depositors, bank should not accept this unless a consent from all the depositors is obtained. In case of deletion of a name of one of the depositors also, bank should accept only if all the existing depositors agree. In short, bank may allow addition or deletion of name or names of joint account holder at the request of all the joint account holders usually it is allowed once only.

3.5.6 Deposit in the Name of Illiterate persons

Term deposits may be issued in the names of illiterate persons, the thumb impression being taken in place of signatures. In addition, a passport size photograph of the depositor is taken at the banks cost and affixed to account opening form. The thumb impression is attested by a supervising official.

3.5.7 Extension

Extension is as if the TDR is paid before maturity without invoking the penalty provided.

- After extension the TDR remains for a period longer than the unexpired portion of the original contract.
- Interest for the period between the date of acceptance of the TDR and date of request for extension will be paid at the rate for the period run, without penalty.
- If arrears are due from the customer (on account of periodical interest paid) the same are to be recovered and credited to the TDR interest account.
- If the interest rate structure has changed, enhanced interest rate will be applicable from the due date of extension and not from the date of change in interest etc.
- Fresh application is taken with a note that if the extended TDR is prematurely paid before the due date of the old TDR, penalty provision will apply from the date of the original TDR. This is also noted in the TD Ledger.
- Fresh TDR should bear the legend 'extension of'.

3.5.8 In Lieu of Earnest Money (Deposit Receipt Issued for Earnest Money)

The TDRs are issued in the following style:

Government. Official / Department / Public Body A/c...... (name of the depositor). The fact that the deposit stands at the absolute disposal of the government official, is to be brought out in the application or by means of a separate letter.

Discharge of the government department is required for repaying / premature payment / grant of loans. In addition, a letter permitting the above is also required. If this is not acceptable, at least a letter stating that the goverment department does not have interest in the deposit should be obtained.

3.5.9 Transfer of Term Deposits

Transfer of term deposits from one branch to another is done free of cost. A written application alongwith the TDR is obtained. The signature is verified. Particulars of periodical interest paid are recorded in the pages. The remark that the deposit has been transferred to ……. branch is made in the TDR Register. The principal and the interest accrued but not paid are remitted to the transfer branch by means of a draft. The TDR is marked with the legend 'Transferred to ..... Branch' in red ink and the TDR and drafts sent to the transferee branch along with account opening form and other connected papers. Suitable entry will be made in Term Deposit Ledger and Date card etc.

3.6 Special Term Deposits / Re-Investment Plan Deposits

The Scheme

The special term deposit, also known as Reinvestment Plan, envisages acceptance of term deposit with a provision for automatic reinvestment of interest earned thereon at quarterly intervals till the maturity of the deposits. As such, no payment of interest is made to the depositors before the expiry of the term. This is, therefore, a scheme for those who do not require interest in the interim. The principal plus interest compounded at quarterly intervals is paid in one lump-sum at the expiry of the period for which the deposit is kept.

3.6.2 Application

The application form, as in the case of term deposits, will be utilised with an indication that the deposit is to be accepted under the reinvestment plan. The relative receipt issued to the depositor will indicate the rate as applicable to an ordinary term deposit but will incorporate a clause regarding the benefit of reinvestment of interest at quarterly intervals that will occur to the depositor.

3.6.3 Accounting Procedure

Deposits accepted under the scheme will be credited to 'Special Term Deposit Account' in the general ledger or to Re-investment Plan Account as per the nomenclature.

The record of deposits will be maintained in the special term deposit register, different folios being allocated for different maturities. Where different rates are applicable on deposits of the same maturity, for instance, special rates being applied to staff deposits or in the event of deposit rates undergoing a change in future, separate openings will need to be maintained for different interest rates. In other words, all deposits entered in any folio would have the same maturity and bear the same interest rate.

3.6.4 Monthly Interest Provision

Monthly interest provision will be calculated at the rates indicated in a ready reckoner table for every Rs1000- on the month end balance under each category (as appearing in the relative opening). Having so calculated the provision amount for each category separately, entries will then be passed for the aggregate of the provision amount, by debit to interest account and credit to special term deposit interest account.

3.5.5 Premature Payment

Premature payment will be allowed at the banks discretion at 1% (differential prescribed by the Reserve Bank) less than the interest rate applicable for the period for which the deposit has already run, for e.g., in the case of deposit accepted under the scheme for 36 months, if premature repayment is asked for on the expiry of 26 months, the relevant rate of interest for term deposit being 9% p.a. compound interest with quarterly rates will be paid to the depositor at 8% p.a. for the period the deposit has remained with the bank. The difference between the aggregate provisions made and the actual interest payable will be reaccredited to interest account.

3.6.6 Conversion into Ordinary Term Deposit

If requests are received from depositors for conversion of special term deposit receipts into ordinary term deposit receipts, such request can be acceded to, provided the period of the receipts remains unchanged. Principal amount is then transferred from special term deposit account to ordinary term deposit account. Necessary adjustments will be made in term deposit interest account and special term deposit interest account. However, it is desirable to accede to such requests on maturity of deposit.

3.6.7 Transfer to Another Branch

The instructions regarding the transfer of term deposit accounts from one branch to another and the accounting procedure there of will apply *mutatis mutandis,* to the special term deposit account as well. However, the question of periodical payment of interest to the depositor would not arise in the case of reinvestment plan.

3.6.8 Tax Liability on Interest

According to the existing provisions of the Income Tax Law, interest earned upto Rs 10,000/- on bank deposits is exempted from Income Tax.

3.6.9 Balancing

Balancing is done on half yearly basis.

3.7 Recurring Deposit Scheme

3.7.1 Scheme

The Recurring Deposit Scheme has been so designed as to make it operationally simple. The scheme is aimed at providing a person with an opportunity to build up his savings through regular monthly deposits of fixed sums over a period of time. It is most useful for the salaried class. It is one of those time deposit schemes in which the customer has to deposit the agreed amount every month.

The advantages of the scheme over other schemes are

- It contains an element of compulsion in savings which is welcome to a certain class of depositors.
- Effective rate of interest works out to be higher than the rate as applicable to term deposits of corresponding maturities.

3.7.2 Who can open Recurring Deposit Account

A recurring deposit account may be opened in the name(s) of

- One person, in his/her name
- Two persons jointly, repayable jointly or to either or survivor, or former or survivor, or latter or survivor
- More than two persons jointly and repayable to all of them, or any one or more of the survivors of them, or to the last survivor of them
- A minor who has not completed 12 years of age to be operated upon by his/her guardian, or a minor alone if he has completed the age of 12 years in which case the monthly installments should be so adjusted that at the end of the stipulated term, the total amount repayable in such an account does not exceed Rs 50,000/-
- Deposits under the recurring deposit scheme can be accepted freely from any category of customers.
- All accounts can be opened once depositor(s) fill in the banks prescribed form of account opening and specimen signature form.

3.7.3 Accounting Procedure

- All deposits into a recurring deposit account should be by way of cash or by mail transfer at par from any other office of the bank or by a locally payable cheque, money order, postal order etc. Standing instructions from depositors for transfer of monthly installment from their savings banks or current account may also be accepted and such transfers are effected free of charge. Should the balance in an account prove to be insufficient to effect the transfer, the standing instruction shall not be acted upon; and advice should, however, be sent to the depositor concerned, of non-compliance, for want of adequate balance in the account.
- Deposits should made by way of pay-in-slips ,credit should beafforded to the ledger account, and balances checked and initialed by an authorised supervising official in the usual manner. Recurring deposit ledgers should be checked daily with day books like any other depot ledgers.

3.7.4 Pass book

A passbook is supplied to each depositor. While the passbook need not be produced at the time of paying the installments, no repayment of a recurring deposit account should ordinarily be made without production of the passbook. When the passbook is presented with the deposit of an installment, the corresponding entry, which should be made therein promptly, needs to be authenticated by an authorised official and the passbook handed back to the depositor. Ordinarily, passbooks should not be retained overnight and when this is done, an acknowledgement must be given to the depositor. If the passbook is spoilt, mutilated or lost, a charge of Rs.2/- is levied for issue of a fresh passbook.

3.7.5 Payment of Installment

A fraction of a month will be treated as full month for the purpose of calculating such interest. The total interest so chargeable is rounded off to the nearest rupee and recovered from the total amount of interest payable at the time of maturity or at the time of deposit of arrear installments. Where a depositor fails to pay an installment for any calendar months on or before the last working day of that month, no reminder will be sent by the bank. The penalty interest charged is radiated to Recurring Deposit Interest Accounts.

3.7.6 Monthly Provision of Interest

Amounts received for recurring deposit account are credited to ‘Recurring Deposit Account’ in general ledger. Monthly provision in respect of interest payable on recurring deposit is made every month by debit to interest account and credited to recurring deposit interest account. Such provision is made at a fixed rate for every Rs.100/- for the month end balance in the recurring deposit account in the general ledger.

3.7.7 Balancing

The recurring deposit ledger accounts should be balanced once a quarter and checked by a supervising official. A set of balance books are be maintained for the purpose as is done in the case of saving bank account.

3.7.8 Date of Maturity

The maturity value of a recurring deposit is paid 30 days / one month after the last installment has been paid or on the expiry of the period for which the deposit was accepted, whichever is later. A suitable legend to this effect may be incorporated in the space provided for date of payment in the passbook by means of a rubber stamp. Since the date of maturity cannot be determined with precision at the time of opening of an account, the precise maturity date should be determined and desired only after receipt of the last installment.

3.7.9 Pay Maturity

On the date of maturity, the interest in respect of the concerned account should be applied and the account closed and transferred to Deposit at Call Account. While making payment of the proceeds to the depositor subsequently (where the request for closure of the recurring deposit account is received through a letter) the letter should say that no interest will be payable for the period beyond the stipulated period, during which total amount payable remains outstanding in the account. However, the renewal of an overdue recurring deposit account as a term deposit with retrospective effect from the original date of maturity may be permitted in accordance with the directives.

3.7.10 Transfer of Accounts

A recurring deposit account can be transferred from one office of the bank to another. Should a depositor wish to transfer his account, he must present his passbook and make a written application for the transfer. While transferring an account the transferring branch should calculate the interest provision in respect of the account at the appropriate rate and transfer the interest provision so arrived at to the transferee branch by debiting to its recurring deposit account and the amount of interest provision should be clearly and separately indicated in the relative mail transfer advice. The transferee branch must credit the amount of provision so received to the Recurring Deposit Interest Account. The transferring branch need not make any entries or the relative passbook, Instead it needs to merely note against the last entry in the passbook the fact of the account having been transferred to a particular branch, under authentication. Similarly, it will not be necessary to show the opening entries in the passbook at the receiving office. The passbook should be returned to the depositor after recording therein the new account number, etc.

3.7.11 Repayment

In the usual course, when all the stipulated installments are paid, the balance in the account together with accrued interest is payable one month after the last installment has become payable and has been paid. The passbook is cancelled and returned to the depositor when the account is closed.

3.7.12 Repayment Before Maturity

If a sole depositor, or in the case of a joint account with E or S facility any one of them, all depositors in case the deposit is payable jointly, wish to close the account prematurely, all the stipulated installments already paid become repayable together with compound interest on monthly products at the rate of one per cent less than the rate of interest applicable for the period for which the deposit has remained with the bank. However, if an account is closed within three months of its opening, interest will be paid at the applicable rate less one per cent penalty. A service charge of upto Rs 10/- may be levied by the bank, at the discretion of the branch manager/ manager of the division.

3.7.13 Closure of Account

An account is normally closed when all the stipulated number of installments have been paid, or for some other reason, and the depositor has signed the account closing form which need not be stamped. Accounts can also be closed on receipt of a letter from the depositor to that effect (the letter being in any form) provided the passbook has been returned to the bank. When the depositor does not turn up on the due date the principal amount and interest are held in the Deposit at Call Account. When maturity amounts are held in Deposit at Call Account, if the depositors so desire, the amount may be transferred to fixed deposit / special term deposit account, bearing interest rate prevailing at the time of maturity of the recurring deposit account or at the time when the depositor wants to convert it into a term deposit / special term deposit, whichever is lower.

3.7.14 Loss of Term Deposit Receipt and Issue of Duplicate Receipt

When the bank receives the request from the depositor for the issue of duplicate receipt, the following procedure should be followed

- A letter signed by depositor / depositors informing the bank about loss of deposit receipt and requesting for issue of duplicate should be obtained.
- A duly stamped letter of indemnity duly signed by all the depositors should be obtained to safeguard banks interest in case the original is also presented for payment.
- An appropriate remark in relevant time deposit ledger should be made.

3.7.15 Certificate of Deposit

- It is issued by scheduled commercial banks other than RRB's
- It is issuable at discount rate decided by issuing bank
- The denomination of certificate of deposit should be in multiples of Rs 10 lakh subject to minimum size of an issue to single investor being Rs 50 lakh
- Maturity period should not be less than 3 months and more than 1 year
- It is payable at par, transferable by endorsement, and delivery is only after 45 days
- It is exempted from stamp duty
- CDs are part of bank deposits.

3.8 Electronic Banking

Modern Internet and e-business services have reduced the world to a 'digital global village'.The world wide web has been dramatically changing our every day life; Internet banking, also known as electronic banking, is the latest advicement in information technology. In simple words, it is banking using the electronic media.

e-banking is a service which connects the user, with a PC and a browser, to the website of the bank and allows him to avail of the services provided by the bank. There is of course no human operator to respond to the needs of the customer.

Modern banks have a centralised database, that is web-enabled. All the services, which the bank has permitted on the Internet, are displayed on the menu. Any service can be selected and further interaction is directed by the nature of the service.

Services provided by banks through e-banking lower transaction costs, add value to the relationship with banks and provides convenience to customers. e-banking provides facilities to customers for managing savings, checking accounts, applying for loans and paying bills over the Internet using personal computer, mobile phone or hand held computer (Personal Digital Assistant).

These days, web-enable banks have been providing the following new services to their customers.

1. **Electronic Funds Transfer system (EFTs) –** This is a cost saving scheme for the convenience of customers. Under this scheme banks transfer the salaries from companys account to employees' accounts as per the instruction of the employer. This system is not used only for depositing and withdrawing salaries but is also used to provide many services to the customers such as transfer cash from one account to another account of the same branch from one account to another account of differant, branches within or overseas, and providing services for making and receiving payment's on line. This system removes the risk time and inconvenience of handling cash.

2. **Automated Teller Machine (ATMs) –** This is a free standing self-service terminal performing 60 per cent of the tellers job quickly and at lesser cost. While using the ATM, a plastic card is inserted into the terminal. Upon request, the user has to type-in the identification code also. The machine then responds by delivering the required cash, cashing cheques, taking deposits and performs other simple banking transactions.

3. **Debit Card –** The card issued to bank account holders against their bank balance to facilitate and simplify the payment, withdrawal and transfer of money any time, any where through the computer

is known as Debit Card. There is no overdraft facility to debit card holders. There is also no fee, interest and charge against issue of these cards. Such cards are being issued in India by ICICI, HDFC, HSBC, Citibank, SBI, PNB etc.

4. **Credit Card –** The card issued to selected customers to enable them to make payment of credit bills upto specified limit any time, anywhere through the computer is known as credit card. It is also used for withdrawing cash from ATMs. The amount overdrawn has to be repaid with in the specified date. Interest is charged if payment is not made upto specified date. The credit card system has faciliated, simplified and encouraged credit transactions.

   Credit card is a substitute for cash that can be used by selected customers. It is the key to the opening of bank account for daily payments. It provides overdraft facilities also. These are plastic cards having a photo identity and embossed signature of the customer. It also contains issuing bank's name and validity period of the card.

3.9 Bank Reconciliation Statement

When a businessman opens an account with a bank, he is issued a passbook by the bank. A passbook, as you know, is nothing but a copy of the customers account maintained by the bank in its ledger. Entries in the passbook are recorded by the bank whever the customer presents the passbook to the bank for the same. At the same time, in the case of a business enterprise, the business maintains many books of account. One of the passbooks, as you learnt in Chapter - 2, is the cash book. When the business maintains a cash book with a bank, in the bank column all withdrawing transaction are recorded like deposit and withdrawal of cash, issue of cheques for making payment, deposit of cheques received into bank etc. Now, if all the transactions in the passbook and in the bank column of the cash book are recorded then the bank balance as shown by the cash book must be the same as the bank balance shown by the passbook. But this does not happen everytime; at time's there is a difference between the bank balance as shown by the cash book and the bank balance as shown by the passbook. Following are the important reasons for the non agreement of the cash book balance with the passbook balance.

(i) **Cheques issued but not yet presented for payment.** The entry in the cash book is made immediately on issue of the cheque but entry in the passbook will be made by the bank only when the cheque is presented for payment. There will thus be a gap of some days between the entry in the cash book and in the passbook.

(ii) **Cheques paid into the bank but not yet cleared.** As soon as cheques are sent to the bank, entries are made in the bank column on the debit side of the cash book. But usually banks credit the customer's account only when they have received the payment from the bank concerned; i.e. when the cheques have been cleared. Again there will be some gap between the depositing of the cheques and the credit given by the bank.

(iii) **Interest allowed by the bank.** If the bank has allowed interest to the customer, the entry will normally be made in the customers account and later shown in the passbook. The customer usually comes to know of the amount of interest by perusing the passbook and only then he makes the relevant entry in the cash book.

(iv) **Interest and expenses charged by the bank.** Like (iii) above, the interest charged by the bank and the amount of the bank charges are entered in the customers account and later in the passbook. The customer makes the required entries only after he sees the passbook.

(v) **Interest and dividends collected by the bank.** Sometimes investments are left with the bank in safe custody; the bank itself sees to it that the interest or the dividend is collected on the due dates. Etnries are made as indicated in (iv) above.

(vi) **Direct payments by the bank.** The bank may be given standing instructions for certain payments such as against insurance premium. In this case also the customer may come to know of the payment only on seeing the passbook. The entries in the passbook and in the cash book may thus be on different dates.

(vii) **Direct payment into the bank by a customer.** If such a payment is received by the bank, it will be entered in the customers account and also in the passbook; the account holder may come to know of the amount only when he sees the passbook.

(viii) **Dishonour of a bill discounted with the bank.** If the bank is not able to receive payment on promissory notes discounted by it, it will debit the customer's account together with any charges that it may have incurred. The customer will naturally make the entry only when he sees the passbook.

(ix) **Bills collected by the bank on behalf of the customer :** If goods are sold, the discount may be sent through the bank. If the bank is able to collect the amount, it will credit the customers account. The customer may make the entry only on receiving the passbook.

(x) **An error committed by the bank :** A bank rarely commits an error but, if it does, the balance shown in the passbook will naturally differ from that shown in the cash book.

3.9.1 Reconciliation : If none of the circumstances mentioned above exist, the balance shown by the passbook and that shown by the cash book will agree. If they disagree, it will be because of some of the reasons mentioned above. At the end of the month, the two balances should be compared and, if there is disagreement, exact reasons for it should be established. In other words, the two balances must be fully reconciled. The chief advantages of such a reconciliation are

- The reconciliation will take care of any errors that my have been committed either in the cash book or in the passbook
- Any undue delay in the clearance of cheques will be shown up by the reconciliation
- A regular reconciliation discourages the staff of the customer or even that of the bank from embezzlement. There have been many cases when cashiers merely made entries in the cash book but never deposited the cash in the bank; they were able to get away with it only because of lack of reconciliation.

This reconciliation is made in a statement to reconcile the balances of cashbook and passbook on a particular date and is called the 'bank reconciliation statement'.

3.9.2 Need and Importance of Bank Reconciliation Statement

It is essential to prepare a bank reconciliation statement due to the following reasons.

- A bank reconciliation statement locates the errors or omissions that may have been committed either on the part of the customer or the bank. The errors so detected can be rectified accordingly.
- By preparing a bank reconciliation statement, the customer becomes sure of the correctness of the bank balance shown by the cash book. It helps him in making further transactions with the bank. For example, suppose the cash book shows a bank balance of Rs 20,000, whereas the balance shown by the pass book is Rs. 15,000. By reconciling the two, it is disclosed that cheques for Rs 5,000 were deposited into the bank but have not been collected so far (or some of these have been dishonoured). In such a case, further cheques will be issued by assuming the bank balance of Rs 15,000 only.
- A reconciliation statement facilitates the preparation of a revised cash book. For example, the entries relating to bank charges, interest allowed or charged by the bank, direct payment by the bank on our behalf etc. will be recorded in the passbook but for which there is no entry in the cash book. Such entries will now be recorded in the cash book as well.
- Periodic preparation of this statement reduces the chances of embezzlement by the staff of the firm or even that of the bank. For example, if a cashier merely makes an entry in the cash book but does not deposit the cash and cheques into the bank, it will be disclosed by preparing a bank reconciliation statement.
- A reconciliation statement helps in revealing the unnecessary delay in the collection of cheques by the bank.
- It also helps in keeping a track of cheques which have been sent to the bank for collection.

3.9.3 Procedure for preparation of Bank Reconciliation Statement

Procedure for preparation of bank reconciliation statement is as follows.

(i) Tick off all the items in the passbook with the entries in the bank column of the cash book and make a list of the entries as are found not ticked either in the cash book or the passbook. The unticked items are responsible for the difference in the balance shown by the cash book and the passbook.

(ii) Take balance as per cash book or passbook as the starting point.

(iii) Adjust the starting point with the other balance by adding or subtracting the unticked items as located in (i). If balance as per cash book has been taken as the starting point, then balance as per cash book is to be adjusted according to entries passed in the passbook or vice versa.

Illustration 1. From the following particulars, prepare Bank Reconciliation Statement showing the balance as per bank pass book on 31 March, 2007. The following cheques were paid into the firm's current account in March 2007, but were credited by the bank in April 2006 :

Shri Morarji Dalal Rs 2,500, Shri Dinkar Tapase Rs 3,000, and Shri Baliram Gidwani Rs 2,400.

The following cheques were issued by the firm in March, 2007 and were cashed in April, 2007

Shri M. Kher Rs 3,000, Shri Natverlal Mehta Rs 5,000, and Shri Dayabhai Desai Rs 3,000.

A cheque for Rs 1,000, which was received from a customer, was entered in the bank column of the cash book in March 2007 but the same was paid into bank in April 2007.

The passbook shows a credit of Rs 2,500 for interest and a debit of Rs 500 for bank charges. The balance as cash was Rs 1,80,000 on 31 March 2007.

Solution

BANK RECONCILIATION STATEMENT as on 31 March, 2007

		Rs
Balance as per cash book		1,80,000
Less cheques paid into bank not yet cleared :	Rs	
Morarji Dalal	2,500	
Dinkar Tapase	3,000	
Baliram Gidwani	2,400	7,900
		1,72,100
Less cheque debited in cash book but not yet banked		1,000
		1,71,100
Less bank charges entered in passbook but not entered in cash book		500
		1,70,600
Add cheque issued but not yet cashed		
M. Kher	3,000	
Natverlal Mehta	5,000	
Dayabhai Desai	3,000	11,000
		1,81,600
Add Interest credited in passbook but not yet entered in cash book		2,500
Balance as per bank passbook		1,84,100

Illustration 2. From the following particulars ascertain the balance that would appear in the bank pass book of A on 31 December 2006.

(i) The bank overdraft as per cash book on 31 December, 2006 – Rs. 6,340.

(ii) Interest on overdraft for 6 months ending 31 December, 2006 – Rs 160 is enterest in the passbook.

(iii) Bank charges of Rs 30 for the above period are debited in the passbook.

(iv) Cheques issued but not cashed prior to 31 December, 2006, amounted to Rs 1,168.

(v) Interest on investments collected by the bank and credited in the passbook, Rs 1,200.

Solution

BANK RECONCILIATION STATEMENT as on 31 December, 2006

The above illustration can also be presented with two columns for 'Plus' and 'Minus'.

Particulars	Plus Amount Rs	Minus Amount Rs
Overdraft as per cash		6,340
Interest debited in passbook but not yet in cash book		160
Cheques issued but not yet presented	1,168	
Cheques paid in but not yet credited by the bank		2,170
Bank Charges		30
Interest collected by the bank in the passbook but not yet entered in cash book	1,200	
	2,368	8,700
Overdraft as per passbook (Rs. 8,700 - Rs. 2,368)	6,332	
Total	8,700	8,700

Illustration 3. From the following particulars, prepare a a bank reconciliation statement showing the balance as per cash book.

The following cheques were paid into the bank in December 2005 but were credited by bank in January 2006

Seema – Rs 3,500, Sangita – Rs 2,500, Sonia – Rs 2,000

The following cheques were issued by the firm in December, 2005 but were presented in January, 2006

Arti – Rs 4,000, Bharti – Rs 4,500

A cheque for Rs. 1,000, which was received from a customer, was entered in the bank column of cash book in December 2005 but was omitted to be banked in December 2005.

The passbook shows a debit of Rs 1,000 for bank charges and a credit of Rs 2,000 for interest.

Interest on investments, Rs 2,500, collected by bank appeared in the passbook.

The bank balance as per passbook was Rs 20,000 on 31 December, 2005.

Solution. **BANK RECONCILIATION STATEMENT**

As at 31st December, 2005

Particulars	Plus Amount Rs	Minus Amount Rs
Balance as per passbook Rs. 20,000	20,000	
Add : Cheques paid into bank but not credited		
Seema Rs 3,500		
Sangita Rs 2,500		
Sonia Rs 2,000	8,000	
Less : Cheques issued but not yet presented for payment		
Arti Rs 4,000		
Bharti Rs 4,500		8,500
Add : Chques entered in the bank column of the Cash book but omitted to be banked	1,000	
Add : Bank charges	1,000	
Less : Interest allowed by the bank		2,000
Less : Interest on investment		2,500
Balance as per cash book		17,000
	30,000	**30,000**

Illustration 4. The bank passbook of Mr Zia-ur-Rehman showed an overdraft of Rs 33,575 on 31 March, 2005. On going through the passbook, the accountant found the following

i) A cheque of Rs. 1,080 credited in the passbook on 28 March, is dishonoured and debited in the passbook on1 April, 2005. There was no entry in cash book about the dishonour of the cheque until 15th April.

ii) Bank had credited his account with Rs 2,800 for interest collected by them on his behalf but the same had not been entered in his cash book.

iii) Out of Rs 20,500 paid in by Mr X in cash and by cheques on 31 March, cheques amounting to Rs. 7,500 were collected on 25th April.

iv) Out of cheques amounting to Rs 7,800 drawn by him on 27 March, a cheque for Rs 2,500 was encashed on 3 April.

Prepare bank reconciliation statement on 31 March, 2005.

Solution. **BANK RECONCILIATION STATEMENT**

As at 31 March, 2005

Particulars	Plus Amount Rs	Minus Amount Rs
Overdraft as per passbook		35,575
Less : Interest collected and credited by the bank		2,800
Add : Cheques paid into bank but not yet collected	7,500	
Less : Cheques issued but not yet encashed		2,500
Overdraft as per cash book	31,375	
	38,875	**38,875**

Note : Item No. 1 of the question will not be shown in the statement because it has appeared in both the cash book and passbook before 31 March, 2005.

Illustration 5. My bank passbook for Account No. 1 shows an overdraft of Rs 6,500 on 31 March, 2006. This does not agree with the cash book balance. From the following particulars ascertain the cash balance:

Cheques amounting to Rs 15,000 were paid into the bank in March out of which, it appears, only cheques amounting to Rs 4,500 were credited by the bank. Cheques issued during March amounted in all to Rs 11,000. Out of these, cheques for Rs 3,000 were unpaid on 31 March, 2006. The bank has wrongly debited Account No. 1 with Rs 500 in respect of a cheque drawn on Account No. 2. The account stands debited with Rs 150 for interest and with Rs 30 for bank charges. The bank has paid the annual subscription of Rs 100 to my club according to my instructions. The entries for interest charges and subscription have not yet been made in the cash book.

Solution.

BANK RECONCILIATION STATEMENT (ACCOUNT NO. 1)

As on 31st March, 2006

Particulars	Plus Amount Rs	Minus Amount Rs
Overdraft as per Passbook		6,500
Cheques paid into bank but not entered in book	10,500	
(Rs 15,000 - 4,500)		
Cheques issued but not yet presented		3,000
Wrong debit to Account No. 1 instead of		
Account No. 2	500	
Payment for charges made and entered in passbook		
but not yet in cash book : Rs		
Interest 150		
Bank Charges 30		
Subscription 100	280	
(positive, i.e., debit) Balance as per cash book		9,500
		1,780
Total	**11,280**	**11,280**

Key Terms Introduced in the Chapter

- Investment
- Securities
- Envisage of plan
- Drunkards
- Settlement of an account
- Maturity
- Withdrawal
- Term deposits
- Lunatics
- Insolvent
- Trust account
- Earnest money

Summary with Reference to Learning Objectives

1. Banking Regulation act, 1949.
2. Functions of bank – primary and secondary.
3. R.B.I. act, 1934.
4. Functions of RBI.
   - Monetary authority
   - Regulating the financial system
   - Manager of foreign exchange
   - Issue of currency
   - Developing role in support of national objectives
5. Types of Accounts
   - Savings bank account
   - Current deposit account
   - Recurring deposit account
6. Bank Reconciliation Statement is a statement which is prepared on a particular date to reconcile the balances of cash book and passbook.
7. Causes of differences between cash book and passbook balance
   - Cheques issued but not yet presented for payment
   - Cheques paid into the bank but not yet cleared
   - Interest allowed by the bank
   - Interest and expenses charged by the bank
   - Interest and dividends collection by the bank
   - Direct payments by the bank

- Direct payment into the bank by a customer
- Dishonour of a bill discounted with the bank
- Bills collection by the bank on behalf of the customer
- An error committed by the cash book.

Questions for Practice

Short Answer Questions

1. Define 'bank' as per banking regulation act, 1949.
2. Discuss the meaning of savings bank account.
3. Explain the meaning of recurring deposit account.
4. What is RBI ? List its functons.
5. Mention the steps of opening a bank account.
6. What is the procedure of closing a bank account?
7. Who can open a current account.?
8. What is the process of transferring an account from one branch to another?
9. Mention the advantages of a recurring deposit scheme.
10. Discuss the process of balancing of a current account.
11. What is a bank reconciliation statement?

Long Answer Questions

1. What are the forms of business transactions in which a banking company is engaged?
2. What are types of deposit accounts?
3. Elaborate the functions of RBI.
4. What do you mean by a savings bank account? Who can open such an account?
5. Can a saving bank account be opened in the name of lunatics, drunkards, insolvent persons and blind persons? Give reasons for your answer.
6. If a passbook of a savings account is lost or damaged, what is the process to get a new pass book issued?
7. Explain the process of settlement of an account on the death of account holder.
8. What formalities need to be fulfilled while opening a current account?
9. What is the accounting procedure of special term deposits? Can premature payment be made? Explain.
10. Explain the provisions of providing interest on a recurring deposit account.
11. Explain the causes of differences in the cash book and passbook while preparing a bank reconciliation statement.

Practical Questions

1. From the following particulars, prepare a bank reconciliation statement showing the balance as per cash book on 31 March, 2003.

   The following chques were paid into firms current account in March, 2003 but were credited by the bank in April, 2003.

   'A' – Rs 2,500, 'B' – Rs 3,500 and 'C' – Rs 1,900

   The following cheques were issued by the firm in March, 2003 and were cashed in April, 2003 : 'P' Rs 2,500, 'Q' – Rs 4,500 and 'R' – Rs 4,000.

   A cheque of Rs 1,000 which was received from a customer was entered in the bank column of the cash book in March, 2003 but the same was paid into the bank in April, 2003.

   The pass book shows a credit of Rs 2,5,000 for interest and a debit of Rs 1,000 for bank charges. The balance as per cash book was Rs 1,80,000 on 31 March, 2003. [Ans. Balance as per pass book = Rs 1,83,6000]

2. Prepare a bank reconciliation statement from the following particulars.

   M/s Sunder Lal & Sons find that the bank balance shown by their cash book on 31 December, 2004 is Rs. 10,500 (credit) but the passbook shows a different balance due to the following reasons:

   (a) Cheque No. 51 for Rs 540 favouring A, B and Co. has not yet been presented.

   (b) A post-dated cheque for Rs 300 has been debited in the bank column of the cash book but could not have been presented in any case.

   (c) Four cheques totaling Rs 1,200 sent to the bank have not yet been collected, while a fifth cheque for Rs 400 deposited in the account has been dishonoured.

   (d) Fire insurance premium amounting to Rs 50 paid by the bank under a standing order has not been entered in the cash book.

   (e) A bill for Rs 1,000 was retired by the bank under a rebate of Rs 15 but the full amount of the bill was credited in the bank column of the cash book.

   [Ans. Overdraft as per passbook = Rs 11,895]

3. From the following particulars ascertain the balance that would appear in the bank passbook of Sh. Bhola Nath on 31 December, 2004.

   (a) The bank overdraft as per cash book on 31 December, 2004 is Rs 12,680.

   (b) Interest on overdraft for 6 months ending 31 December, 2004, Rs 320, is entered into the passbook.

   (c) Bank charges of Rs 60 for the above period are debited in the passbook.

   (d) Cheques issued but not presented prior to December 2004, amounted to Rs 2,336.

   (e) Cheques paid into the bank but not cleared before December 31, 2004 were for Rs 4,340.

   (f) Interest on investments collected by the bank and credited in the passbook, Rs 2,400.

   [Ans. Overdraft as per passbook = Rs 12,664]

4. From the following particulars ascertain the bank balance as per the passbook of Mrs Ranga Rao as at 28 February, 2005.

   (a) Credit balance as per cash book on 28 February, 2005 was Rs 15,000.

   (b) Interest charged by the bank upto 28 February, Rs 50, is recorded in the passbook only.

   (c) Two cheques of Rs 900 and Rs. 1,500 were issued but out of them one cheque of Rs 900 was presented for payment upto 28 February.

   (d) Bank charges made by the bank of Rs 12.50 were recorded in the passbook.

   (e) Dividend on shares Rs 650 was collected by the bankers directly for which Ranga Rao did not have any information.

   (f) Cheques paid into bank of Rs 2,500 but only cheque of Rs 1,900 was cleared and credited by the bankers. [Ans. Overdraft balance as per passbook = Rs. 13,512.50]

5. Prepare a bank reconciliation statement from the information given below :

   (a) Bank overdraft as per cash book on 30th April, 2004, Rs 2,000.

   (b) Cheques issued but not presented for payment, Rs 1,250

   (c) Rs 25 charged by the bank on account of bank charges not yet entered in the cash book.

   (d) Interest charged by the bank on Rs 75 but not entered in the cash book.

   (e) Interest on investment collected by the bank and credited in the passbook.

6. Prepare a bank reconciliation statement from the following particulars :

		Rs
(a)	Overdraft as per cash book on 31 December 2004	8,000
(b)	Cheques paid into the bank but not cleared before 31 December, 2004	2,000
(c)	Cheques issued but not cashed by the customer prior to 31 December, 2004	1,200
(d)	Bank charges for the period charged by the bank	100
(e)	Interest on overdraft charged by the bank	200
(f)	Interest on debentures collected by the bank not shown in the cash book	500

[Ans. Overdraft balance as per pass book = Rs 8,600]

7. On 31 December, 2003 the bank passbook of Naresh & Co. showed an overdraft of Rs 10,700. From the following particulars, prepare a bank reconciliation statement.

   (a) Cheques issued before 31-12-2003 but presented for payment after that date amounted to Rs 900.

   (b) Cheques paid into the bank but not collected and credited until 31.12.2003 amounted to Rs 2,200.

(c) Interest on overdraft amounting to Rs 1,200 did not appear in the cash book.

(d) Rs 5,000 being interest on investment collected by the bank and credited in the pass book was not shown in the cash book.

(e) Bank charges of Rs 50 were not entered in the cash book.

(f) Rs 800 in respect of a dishonoured cheque were entered in the passbook but not in the cash book.

8. On 31 December. 2004, my Passbook No. 1 showed an overdraft of Rs 9,500. Out of cheques of Rs 4,500 paid on 28 December, Rs 2,000 appear to have been credited on 3 January, 2005. Out of cheques amounting to Rs 8,000 issued during the month of December, cheques worth Rs 4,500 appear to have been presented before 31 December, 2004. Inadvertently, the bank has credited a sum of Rs 1,000 to my account which belonged to some other account. Interest on overdraft from bank was Rs 500. This was subsequently entered by me in the book. My bank account showed a credit of Rs 600 for interest on securities collected by it.

Prepare a bank reconciliation statement as on 31 December, 2004.

[Ans. Overdraft as per cash book = Rs 12.100]

CHAPTER 4

Vouchers and their Preparation

Learning Objectives

After studying this chapter you will be able to

- understand the meaning of vouchers
- appreciate the importance of vouchers
- classify vouchers into supporting vouchers and accounting vouchers
- classify accounting vouchers into cash vouchers, debit vouchers, credit vouchers, transfer vouchers and adjustment vouchers
- understand the purpose of preparing different types of accounting vouchers
- prepare the different types of accounting vouchers.

As discussed in Chapter 2, the transactions in the books of accounts are recorded on the basis of some documentary evidence which prove beyond doubt that the transaction actually took place. These documents are called vouchers. After recording the transactions on the basis of the information provided by them, vouchers are kept in chronological order in files for future reference. In this chapter we will discuss the different types of vouchers, their importance, and preparation.

When a business enterprise makes purchases it receives, from suppliers, a cash memo, or bill, or invoice, and similarly, when the business sells goods to its customers it issues similar types of cash memos, credit memos, invoices or bills to them while retaining the duplicate copies of these documents with it. These documents are proof's of transactions having taken place. On the basis of these documents the accountant records the transactions in the books of accounts. Therefore, we can say that a document which supports a transaction is called a voucher.

4.1 Types of Vouchers: Vouchers are of two types

i) Supporting vouchers

ii) Accounting vouchers

Vouchers which support business transactions are called supporting vouchers, for e.g., cash receipts, invoices, bills, counterfoils of pay-in-slips confirming the deposit of cash or cheques in the bank etc. Supporting vouchers are the primary evidence of business transactions having taken place.

A supporting voucher is a written document having details of the business transaction and signed by the maker. It can be used as legal evidence of a business transaction having taken place.

Supporting vouchers, for the purpose of recording the transactions in the journal proper or subsidiary books, are handed over to the accountant. These supporting vouchers may be in different forms, shapes and sizes. No doubt that supporting vouchers support business transactions but before the transactions are recorded in the books of accounts they should be properly analysed. The analysis of business transactions for the purpose of recording is done by preparing another set of vouchers called 'accounting vouchers'. An accounting voucher, therefore, refers to a written document containing the analysis of business transaction for accounting and recording purposes, prepared by the accountant on the basis of supporting vouchers. The accounting voucher is countersigned by some authorised and responsible person of the business organisation. We shall discuss accounting vouchers in detail here.

The different types of vouchers have been shown with the help of the following diagram.

- VOUCHERS
  - CASH VOUCHER
    - CREDIT VOUCHER
    - DEBIT VOUCHER
  - NON - CASH VOUCHER
    - TRANSFER VOUCHER

4.2 Types of Accounting Vouchers:

Accounting vouchers may be divided into two categories.

i) Cash vouchers

ii) Non-cash vouchers

4.2.1 Cash Vouchers: Cash vouchers are prepared for cash transactions i.e. cash receipts and cash payments. They can be further subdivided into two

i) Credit vouchers and

ii) Debit Vouchers

Credit Vouchers: Credit vouchers are prepared for recording transactions related to receipt of cash only. The business may receive cash because of the following reasons.

- Cash sales of goods
- Cash sales of assets
- Income received in cash, for e.g., rent received, interest received, dividend received on investments etc.
- Cash received from debtors
- Loan obtained
- Cash withdrawn from bank for use in business
- Cash brought as capital by the owner(s)
- Cash received in advance from the customers or for providing certain other services.

In all transactions pertaining to the receipt of cash, one aspect of the transaction is cash account and the other aspect is the account on account of which cash has been received, for e.g., the individual, or firm, or entity from whom cash has been received, or the revenue heads of accounts, or the fixed asset on the sale of which cash has been received. While recording a transaction on the basis of a credit voucher, cash account is debited with the amount given in the voucher and the account on account of which cash has been received is credited. The name of the account which is to be credited is mentioned in the credit voucher. The format of a credit voucher is given below.

CREDIT VOUCHER

Name of the Business	
Voucher No.________________________	Date ________________
Credit Name of the individual/firm/company/asset/Revenue A/c on account of which cash is received (vide Bill No. ....)	Amount Rs
Sd/- Manager	Sd/- Accountant

Illustration 1 : The cash memo booklet of M/s Gee Computers shows the sale of a computer for Rs. 25000. Prepare a credit voucher of the same.

CREDIT VOUCHER

GEE COMPUTERS 24, NEHRU PALANCE NEW DELHI		
Cash Memo NO.269		Date : 14.4.2007
Credit	Sales Account	Amount in Rs 25,000/-
	Total	25,000/-
Signature (S.N.Singh) Manager		Signature (Ashok Kumar) Accountant

Debit Vouchers: Debit vouchers are prepared for recording transactions pertaining to payment of cash only. The cash payments in a business may be because of the following reasons.

- Cash purchases
- Cash purchase of assets
- Cash payment for expenses
- Cash payments to creditors
- Cash withdrawn by the owners for personal use
- Repayment of loans and advances
- Cash deposited into bank.

In all cash payments, one account affected by the transaction is cash account and the other is the party to whom the payment is made, or the expense or the item of property for which payment is made. Revenue stamp is needed on the voucher if the amount is more than Rs. 5000/-. The format of a debit voucher is given below.

DEBIT VOUCHER

Receuved
Rs______.
The part of the debit voucher marked with words as a supporting voucher in case of transactions where the supporting voucher is not available e.g. payment for hiring taxi, autorikshaw etc.

FIRM'S NAME

Voucher No.______________ Date ________

Debit	Name of the account on account of which payment is made (vide cash memo No. ....)	Amount Rs.

Sd/ Sd/
Manager Accountant

Illustration 2. A cash memo issued by M/s Sunil Kumar in favour of M/s Anil Kumar, 73A Ram Nagar, Hyderabad, shows a sale of goods of Rs. 10,000. Prepare a debit voucher for M/s Anil Kumar on the basis of this cash memo.

Receuved
Rs______.

REVENUE STAMP

M/S ANIL KUMAR
73 RAM NAGAR
HYDERABAD

No. 1324 Date: 15.4.2007

		Amount (Rs)
Debit	PURCHASES	10,000
	(vide Cash Memo No. ....) Total	10,000

Sd/
Manager Accountant

4.2.2 Transfer Voucher: These days every business enterprise undertakes large number of credit transactions. For recording such transactions another type of voucher is prepared which is called a transfer voucher. A transfer voucher, thus, is a voucher prepared for recording credit and other non-cash transactions. Some examples of non-cash transactions are

- Credit Purchases
- Credit Sales
- Returns Outwards
- Returns Inwards
- Depreciation on Fixed Assets
- Bad Debts etc.

Since transfer vouchers are prepared for non-cash transactions, therefore, the transactions do not involve any cash receipt or cash payment. Since every transaction has two aspects, and here none of the aspects involves cash, therefore, these vouchers are simultaneously prepared both in debit and credit forms. The transfer voucher has a column for the account to be debited and another column for the account to be credited. The format of such a voucher is as follows.

TRANSFER VOUCHER

FIRM'S NAME		
Voucher No.________________		Date __________
		Amount (Rs)
Debit	Name of the account to be debited	
Credit	Name of the account to be credited	
Sd/-		Sd/-
Manager		Accountant

Illustration 3: On 1.4.2007, Shyam Electrical Co. purchased 100 CFL tubelights @ Rs 30 each and 10 table fans @ Rs 500 each on credit from Sultan Traders. Prepare a transfer voucher for recording the transaction in the books of Shyam Electricals.

TRANSFER VOUCHER

M/S SHYAM ELECTRICALS 12/4 BHAGIRATH PALACE, DELHI		
Voucher No. 417		Date: 1.4.2007 Amount (Rs)
Debit	Purchase Account	
	100 CFL Tube lights @ Rs 30 each 10 Table Fans @ Rs 500 each	3,000 5,000
	Bill No. 395 Total	8,000
Credit	M/s Sultan Trader	8,000
	Total	8,000
Sd/- Manager		Sd/- Accountant

4.3 Process of Preparation of Accounting Vouchers:

Transactions in the books of accounts of a business enterprise are recorded with the help of accounting vouchers. These accounting vouchers are prepared on the basis of supporting vouchers. The process of preparation of accounting vouchers involves the following steps

i) Analysis of supporting vouchers

ii) Identification of the accounts

iii) Preparation of accounting vouchers

We will discuss each of these steps separately

4.3.1 Analysis of Supporting Vouchers:

This is done with the objective to ascertain the nature of the transaction - whether it is a cash transaction or non-cash transaction. Cash transaction can be (a) cash receipts or (b) cash payments. Supporting vouchers for cash receipts may be the following.

- Duplicate copies of cash memos issued by the firm
- Duplicate copies of the cash receipts issued on account of rent received, commission received, and interest received etc.

Vouchers for cash payments may include the following.

- Cash memos received from the sellers
- Original copies of receipts received on account of rent, commission, interest paid in cash.
- Receipts of bills such as electricity bill, telephone bill, water bill etc.
- Counterfoils of pay-in-slips.

Non-cash transactions may include

- Credit purchases
- Credit sales
- Return outwards
- Returns inwards
- Depreciation of fixed assets
- Bad debts etc.

Supporting vouchers for credit purchases may be the original copies of the invoice received from the supplier of goods, for credit sales they may include duplicate copy of invoice or bill, for return outwards and return inwards they may be debit notes and credit notes.

4.3.2 Identification of Accounts: After the analysis of supporting vouchers as just discussed, in the second step the accounts that are affected by the transaction are identified. This can be illustrated with the help of the following examples.

Example 1: A cash memo for goods sold for cash. This is a supporting voucher for cash receipt. The two accounts affected in this support voucher are cash account and sales account.

Example 2: Payroll. A payroll gives details of the salary paid to the employees. This is a supporting voucher for a cash payment. Two accounts involved are salary account and cash account.

Example 3: An invoice for goods sold on credit to M/s Ram Kumar. This is a supporting voucher for a non-cash transaction. The two accounts affected by the transaction are sales account and M/s Ram Kumar Account.

4.3.3 Preparation of Accounting Vouchers: After analysing the supporting vouchers and identification of the accounts that are affected by the supporting voucher, the last step in the process is the preparation of the accounting voucher itself. At the time of preparation of the accounting voucher we must understand its structure. An accounting voucher has three parts

(i) Uppermost part: In this part the name of the firm, date of preparing the voucher and voucher number are written.

(ii) Middle part: In this part the description of the transaction is written.

(iii) Lower part: This part is meant for the signatures of the accountant and countersignatures of some authorised responsible person.

The uppermost part and the lower part in all the vouchers are the same. The only difference is in the middle part. This part may be different taking into account the type of the voucher that is being made. Usually the vouchers are in printed forms in which the Firm's Name, Voucher Number, Date, Debit/Credit, Amount etc. are already printed and the accountant may have to fill in the details only.

Illustration 4. The following transactions took place in the book of M/s Prem Medicales Store, SCF-89, Sector-46C, Chandigarh. Prepare debit, credit and transfer vouchers.

Date 2006		Particulars	Amt.
i	Mar. 1	Purchased furniture for cash vide Cash Memo No.161	15,000
ii	Mar 4	Salary & wages paid for the month of Feb'2006 vide Salary & Wages Sheet No.13	3,600
iii	Mar.10	Sold goods for cash vide Bill No 2175.	12,000
iv	Mar. 13	Bought goods from M/s Chawla & Sons vide Bill No.1171	4,000
v	Mar. 16	Withdrawn cash from Bank for office use vide Cheque No.13126	3,000
vi	Mar. 19	Depreciation charged on furniture @ 15% on Rs 20,000	

(v) **Solution :**

M/s Prem Medical Store Voucher No. iv	Date:16-03-06 Amt. (Rs)
Credit : Bank A/C	3,000
(being cash withdrawn from bank vide Cheque No.13126)	3,000
Authorised By:	Prepared By:

Transfer Vouchers

(iv)

M/s Prem Medical Store Voucher No.(v)	Date:13-03-06 Amt. (Rs)
Debit:- Purchase A/c	4,000
	4,000
Credit: M/s Chawla & Sons (being goods bought from Chawla & Sons vide bill No.1171)	4,000 4,000
Authorised By:	Prepared By:

(vi)

M/s Prem Medical Store Voucher No.(vi)	Date:19-03-06 Amt. (Rs)
Debit: Depreciation A/c	3,000
	3,000
Credit : Furniture A/c	3,000
(being depreciation charged @ 15% on Rs.20,000)	3,000
Authorised By:	Prepared By:

(i) Debit vouchers

Received Rs______. REVENUE STAMP	M/s Prem Medical Store	
	Voucher No.(i)	Date : 01-03-06
		Amt. (Rs)
	Debit: Furniture A/c	15,000
	(being furniture purchased for cash vide Cash Memo No.161)	15,000
	Authorised By:	Prepared By:

(ii)

Receuved Rs______. REVENUE STAMP	M/s Prem Medical Store	
	Voucher No.(ii)	Date : 04-03-06
		Amt. (Rs)
	Debit: Salary & Wages A/c	3,600
	(being salary & wages paid for the month of Feb '2006 vide Salary & Wages Sheet No.13)	3,600
	Authorised By:	Prepared By:

(iii) **Credit Vouchers**

Received Rs______. REVENUE STAMP	M/s Prem Medical Store	
	Voucher No.(iii)	Date : 10-03-06
		Amt. (Rs)
	Credit: Sales A/c	12,000
	(Being goods sold for cash vide Cash Memo No.2175)	12,000
	Authorised By:	Prepared By:

Key Terms Introduced in the Chapter

- Source documents
- Cash Memo
- Vouchers
- Transactions
- Revenue Stamp
- Voucher no.
- Accounting Vouchers
- Non-cash Vouchers
- Debit
- Credit
- Debit note
- Credit note
- Pay-in-slip
- Invoices & Bills
- Cheques
- Bill No.
- Invoice No.

Summary with Reference to Learning Objectives

A voucher may be defined as a written document to be used in support of entry made in the book of accounts.

Special features of vouchers

- Vouchers are documentary evidence
- They are written documents
- They Support the entries appearing in the books
- They Present full description of the transactions
- They Substantiate the accuracy of the entries in the book of account.

Examples of Vouchers

- Cash Receipts
- Cash Payments
- Purchases
- Sales
- Purchased Return

Contents of Accounting Vouchers

- Name and address of the firm
- Voucher number
- Date
- Details of party to be debited
- Details of party to be credited
- Proof of receiving the amount
- Revenue stamp (if the amount is Rs 5,000 or exceeds Rs 5,000)
- Signature of the accountant and officer of the firm

Classification/Types of Vouchers

Supporting Vouchers

- Internal supporting vouchers
- External vouchers

B. Accounting Vouchers

- Cash vouchers which are of two kinds (i) Debit (payment) vouchers (ii) Credit (receipt) voucher
- Non-cash vouchers or transfer vouchers.

Practical Questions

1. Prepare debit vouchers in the books of Bright Computers, a firm dealing in computers.

2006	Particulars	Rs
Jan.1	Purchased computer for cash vide Memo No.731	25,000
Jan.7	Salary paid for the month of Dec,2006 vide Salary Sheet No.99	15,000
Jan.11	Paid for rickshaw hire	25
Jan.16	Paid cash of Ram & Sons A/c, vide Memo No.101	2,500

2. Prepare credit voucher in the book of M/s Ayan Traders.

2006	Particulars	Rs
Mar.1	Starting business with cash	1,50,000
Mar.4	Sold raw material to Ashu on cash vide Bill No.15	75,000
Mar.8	Sold raw material for cash vide Cash Memo No.116	31,000
Mar.15	Withdrawn from bank for office use by Cheque No.10121	12,000
Mar.28	Received cash from Gian and Co. vide Cash Memo No.14	5,500

3. Prepare transfer vouchers from source voucher:

2006	Particulars	Rs
Jan.1	Bought of goods from Ram on credit vide Bill No.515	5,200
Jan.8	Sold goods to M/s Aman vide Bill No.17125	6,000
Jan.31	Depreciation charged on machinery @ 10% on Rs.100,000	10,000

4. Prepare accounting vouchers.

2006	Particulars	Rs
Apr.1	Commission received vide Cash Receipt No.4443	15,000
Apr.9	Discount received vide Cash Receipt No.5521	5,007
Apr.16	Paid for conveyance vide Cash Memo No.80	2,001
Apr.19	Paid for wages vide Cash Memo No. 156	7,002
Apr.25	Purchased cloths on credit vide Bill No. 2251	50,000

5. Prepare debit voucher on the books of HCL Computer Ltd, New Delhi, a firm dealing in computers.

Date 2006	Particulars	Amt. Rs
Jan.1	Purchased computer for cash vide Memo No.1021	27,000
Jan.6	Salary paid to Rajeev Sharma for the month of Dec. 2006 vide Salary Sheet No.13	7,500
Jan.9	Paid for octroi charges	110
Jan.10	Paid wages to labour	600
Jan.15	Paid cash of Singla & Associate A/c, vide Memo. No.17	10,000
Jan.16	Purchased computer for cash vide memo. No.29	20,000

6. Prepare debit vouchers in the books of Mohindra Book Depot, Sector-31, Chandigarh, a form dealing in books.

Date 2006	Particulars	Amt. Rs
July 1	Purchased books from Arya Book Depot, New Delhi for cash vide Memo No.21	11,000
July 3	Paid cash to Aman Verma A/c	3,000
July 6	Paid commission	70
July 8	Paid salary to employee for the month of June	2,000

7. Prepare credit vouchers in the books of M/s Singla Provision Store, Sector-47D, Chandigarh.

Date 2006	Particulars	Amt. Rs
April 1	Business started with cash	350,000
April4	Received cash from Karan Singh vide Cash Memo No. 271	6,000
April 6	Sold goods to Mr Anil Puri on cash vide Bill No.176	10,000
April 9	Withdrawn from bank for office use by Cheque No.16342	7,300
April 15	Sold goods to Miss Nikita Naithani for cash vide Memo No.117	10,200
April 20	Cash received from Surjit Paul Tirkey vide Cash Memo No.716	12,000

8. Prepare transfer vouchers from source voucher.

Date 2006	Particulars	Amt. Rs
March 2	Bought goods from Rajeev Sharma on credit vide Bill No.132	76,000
March 6	Sold goods to Mrs Kavita Singh vide Bill No.17126	3,000
March 10	Depreciation charged on furniture @ 2½% on Rs 6,700	

9. Prepare accounting vouchers with the following information.

Date 2006	Particulars	Amt. Rs
June 2	Rent received vide Cash Receipt No.101	3,000
June 9	Discount received vide Cash Receipt No.117	1,200
June 11	Paid for conveyance vide Cash Memo No.119	125
June 15	Paid wages vide Cash Memo No. 123	560
June 20	Purchased clothes on credit vide Bill No.242	15,000

Q10. Prepare debit voucher in the books of Surjeet Book Depot Mansa, a firm which sells books.

Date 2006	**Particulars**	**Amt.Rs.**
Jan. 1	Purchased furniture for cash vide Memo No.131	3,000
Jan. 6	Paid for freight for car hire	50
Jan. 9	Paid cash to Manghat Ram Jain A/c vide Memo No.112	3,100
Jan. 12	Paid salary to Manoj kumar for the month of Dec.	1,200

Q11. Prepare transfer vouchers from the following information of M/s Jain Cloth Store, Chandni Chowk, Delhi.

Date 2006	**Particulars**	**Amt.Rs.**
March 1	Purchased goods from Pardeep Emporium, Rewari, vide Bill No.236	20,000
March 6	Depreciation charged on office equipment @ 2% on Rs 37,000	

Q12. Prepare accounting vouchers with the following information.

Date 2006	**Particulars**	**Amt.Rs.**
July 1	Purchased goods on credit from Universal Trader vide Bill No.137	17,000
July 6	Received cash from Jagat Ram & Sons vide Cash Receipt No.62	6,000
July 7	Paid salary to Rajan vide Cash Memo No.89	14,000
July 8	Sold goods to Bansal Provision Store vide Cash Memo No.77	8,300
July 10	Depreciation on furniture @3.5% on Rs 1,50,000	

Q13. Prepare credit vouchers in the books of M/s Mukesh Cosmetics Traders.

Date 2006	Particulars	Amt.Rs.
March 1	Business started with cash	1,50,000
March 2	Sold goods to Swati Traders on Cash Bill No.163	20,000
March 4	Sold goods to Khanna & Co. on Cash Bill No.173	16,000
March 6	Withdrawn from bank for office use by Cheque no.13261	11,000
March10	Received cash from Ajay Singh Rajput vide Cash Memo No.181	3,000

Q14. Prepare accounting vouchers with the following information.

Date 2006	Particulars	Amt. Rs
Sept 1	Commission received from Amar Cash Receipt No.136	1,000
Sept 16	Paid for rickshaw charge vide Cash Memo No.84	35
Sept 17	Paid for wages vide Cash Memo No.81	2,000
Sept 20	Purchased goods on Credit vide Bill No.2241	3,000
Sept 21	Discount Received vide Cash Receipt No.1173	200

Q15. Prepare credit vouchers in the books of CMC Medical Store.

Date 2006	Particulars	Amt.Rs.
Mar. 1	Business started with cash	7,00,000
Mar. 5	Goods sold for cash vide Bill No.11	30,000
Mar. 10	Goods sold to Rajeev on cash vide Bill No.17	60,000
Mar. 15	Received from Ram Singh vide Cash Memo No.117	30,000

CHAPTER 5

Trial Balance and their Errors

Learning Objectives

After studying this chapter you will be able to

- know the meaning of trial balance
- understand the objectives of preparing trial balance
- learn the process of preparing trial balance
- explain different types of accounting errors
- understand the process of locating errors
- state the meaning of suspense account
- enumerate the importance of preparing suspense account
- rectify the errors without preparing suspense account
- rectify the errors with suspense account.

5.1 Introduction

The accounting process which you have learnt so far is regarding the recording of transactions on the basis of accounting principles in the journal proper and other subsidiary books, posting them from the journal to the ledger, and balancing the ledger accounts. You have also learnt that when a simple transaction is journalised some accounts are debited and some other accounts are credited and the totals of debits and credits are equal. It means that when the transactions are posted in the ledger the totals of debts and credits should also be equal. A balance is the tool to check the arithmetical accuracy of the fact that the transactions have been correctly recorded in the journal posted in the ledger, and the ledger balances have also been correctly calculated. In this chapter you will learn the meaning and preparation of trial balance. You will also learn about the different types of accounting errors and the method of their rectification.

5.2 Meaning of Trial Balance

A balance is a statement which shows the balances, or the totals, of debits and credits of all ledger accounts prepared for the purpose of verifying the arithmetical accuracy of the posting of ledger accounts. When all the accounts of an organisation are balanced off and such balances are put in a columnar statement having debit balances on one side and credit balances on the other side, such a statement is called 'a trial balance'. The trial balance is prepared, generally, at the end of the accounting period. However, it can be prepared at the end of any period of time say monthly, quarterly or half-yearly. It must be kept in mind that the agreement, or equality, of the two sides of a trial balance is not conclusive proof of the correctness of the accounts.

The trial balance is an important step in the accounting process and forms the basis of preparation of the final statements. The balances given in the trial balance are used for the preparation of profit and loss account and balance sheet of an organisation. Following is the format of a trial balance.

TRIAL BALANCE OF (NAME OF ORGANISATION)
AS ON (DATE ON WHICH IT PREPARED)

Name of Accounts	L.F.	Debit Amount Rs.	Credit Amount Rs.
Total			

5.2.1 Objectives of Preparing a Trial Balance

A trial balance is prepared to meet for the following objectives

(i) To have the balances of all the ledger accounts at one place so that the necessity of going through the pages of the ledger is avoided for finding out those balances whenever required

(ii) To verify the fact that every transaction has been recorded as per the rules of debit and credit in the journal and the ledger through its agreement

(iii) To help in locating the errors

(iv) To help in the preparation of financial statements.

5.3 Preparation of Trial Balance

A trial balance can be prepared by using any one of the following two methods.

(i) Totals Method

(ii) Balances Method

5.3.1 Totals Method

In this method the totals of debit side and credit side of the ledger accounts are shown in the two columns of the trial balance and the balances of the different ledger accounts are not used. The sum totals of the debit and credit columns of the trial balance are arrived at. If these totals are equal then it is the check of the arithmetical accuracy of the accounts. Preparing a trial balance by totals method is not very popular.

Illustration 1. Suresh started his business with a capital of Rs 5,00,000 on 1.1.2007. His other transactions for the month were as follows.

2007		Rs.
Jan 2	Deposited into bank	3,00,000
Jan 3	Purchased furniture for cash	50,000
Jan 4	Cash purchase of goods	30,000
Jan 5	Purchased goods from Mohan on credit	10,000
Jan 6	Purchased stationery	1,000
Jan 7	Purchsed goods from Ravi on credit	8,000
Jan 8	Sold goods on credit to Ashok	3,000
Jan 9	Cash sales	8,000
Jan 10	Paid to Ravi on account	4,000
Jan 11	Purchased computer for office use and paid by cheques	30,000
Jan 12	Paid insurance premium	1,500
Jan 13	Sold goods for cash	5,000
Jan 14	Withdrew cash from bank	70,000
Jan 15	Withdrew cash for personal use	10,000

Jan 16	Purchased goods from Alka	17,000
Jan 17	Purchased goods from Ravi	18,000
Jan 18	Paid to Ravi on account	12,000
Jan 19	Cash sales	17,000
Jan 20	Sold goods to Ashok	9,000
Jan 21	Received from Ashok on account	8,000
Jan 22	Paid to Alka on account	9,000
Jan 23	Received from Ashok on account	2,000
Jan 24	Amount obtained loan from ICICI Bank	50,000
Jan 25	Cash sales	13,500
Jan 31	Paid salary	7,500
Jan 31	Rent	5,000

Record the above transactions in the journal of Suresh, post them in the ledger and prepare a trial balance of Suresh as on 31.1.2007 on 'Total Method' basis.

SOLUTION

SURESH

JOURNAL

Date	Particulars	LF	Debit Amount Rs.	Debit Amount Rs.
2007 Jan 1	Cash Account....................................Dr To Capital Account (Started business with cash)		5,00,000	5,00,000
Jan 2	Bank Account....................................Dr To Cash A/c (Deposited cash into bank)		3,00,000	3,50,000
Jan 3	Furniture Account...............................Dr To Cash A/c (Purchased furniture)		50,000	50,000
Jan 4	Purchases Account.............................Dr To Cash (Cash Purchase of goods)		30,000	30,000
Jan 5	Purchases Account..............................Dr To Mohans Account (purchased goods on credit from Mohan)		10,000	10,000
Jan 6	Stationery Account................................Dr To Cash (Purchased stationery)		1,000	1,000
Jan 7	Purchases Account..............................Dr To Ravis Account (Purchased goods on credit from Ravi)		8,000	8,000

Jan 8	Ashoks Account..................................Dr To Sales Account (sold goods to Ashok on credit)		3,000	3,000
Jan 9	Cash Account....................................Dr To Sales Account (sold goods for cash)		8,000	8,000
Jan 10	Ravis Account...................................Dr To Bank Account (paid to Ravi on account)		4,000	4,000
Jan 11	Computer Account...............................Dr To Bank A/c (purchased computers)		30,000	30,000
Jan 12	Insurance Account...............................Dr To Cash A/c (paid insurance)		1,500	1,500
Jan 13	Cash Account.....................................Dr To Sales Account (cash sales)		5,000	5,000
Jan 14	Cash Account ....Dr To Bank Account (withdrawn cash from bank for office use)		70,000	70,000
Jan 15	Drawing Account................................Dr To Bank Account (withdraw cash for personal use)		10,000	10,000
Jan 16	Purchases Account..............................Dr To Alkas Account (purchased from Alka)		17,000	17,000
Jan 17	Purchases Account..............................Dr To Ravis Account (purchased goods from Ravi)		18,000	18,000
Jan 18	Ravis Account...................................Dr To Cash Account (paid to Ravi)		12,000	12,000
Jan 19	Cash Account....................................Dr To Sales Account (sold goods for cash)		17,000	17,000
Jan 20	Ashoks Account.................................Dr To Sales Account (sold goods to Ashok)		9,000	9,000

Jan 21	Cash Account......................................Dr To Ashok's Account (received from Ashok on account)		8,000	 8,000
Jan 22	Alka's Account....................................Dr To Cash Account (paid to Alka on account)		9,000	 9,000
Jan 23	Cash Account......................................Dr To Ashok's Account (received from Ashok on account)		2,000	 2,000
Jan 24	Bank Account......................................Dr To Bank Loan Account (received loan from ICICI bank)		50,000	 50,000
Jan 25	Cash Account......................................Dr To Sales Account (cash sales)		13,500	 13,500
Jan 31	Salary Account Dr Rent Account Dr To Cash Account (paid salary & rent)		7,500 5,000	 12,500

LEDGER
CASH ACCOUNT

Dr Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 1	To Capital		5,00,000	2007 Jan 2	By Bank		3,00,000
Jan 9	To Sales		8,000	Jan 3	By Furniture		50,000
Jan 13	To Sales		5,000	Jan 4	By Purchases		30,000
Jan 14	To Bank		70,000	Jan 6	By Stationery		1,000
Jan 19	To Sales		17,000	Jan 12	By Insurance		1500
Jan 20	To Ashok		8,000	Jan 18	By Ravi		12,000
Jan 23	To Ashok		2000	Jan 21	By Alka		9,000
Jan 25	To Sales		13,500	Jan 31	By Salary		7,500
					By Rent		5,000
	Total		**6,23,500**		**Total**		**4,16,000**

CAPITAL ACCOUNT

Dr Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
				2007 Jan 1	By cash		5,00,000

BANK ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 2	To cash		3,00,000	2007 Jan 10	By Ravi		4,000
Jan 24	To bank loan		50,000	Jan 11	By Computer		30,000
				Jan 14	By Cash		70,000
				Jan 15	By Drawings		10,000
	Total		**3,50,000**		Total		**1,14,000**

FURNITURE ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 3	To cash		50,000				

PURCHASES ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 4	To cash		30,000				
Jan 5	To Mohan		10,000				
Jan 7	To Ravi's Account		8,000				
Jan 16	To Alka		17,000				
Jan 17	To Ravi		18,000				
	Total		83,000				

MOHAN'S ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
				2007 Jan 5	By purchases		10,000

STATIONERY ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 6	To cash		1,000				

RAVI'S ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
Jan 10	To bank		4,000	Jan 7	By purchases		8,000
Jan 18	To cash		12,000	Jan 17	By purchases		18,000
	Total		16,000		Total		26,000

SALES ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
				2007			
				Jan 8	By Ashok		3,000
				Jan 9	By Cash		8,000
				Jan 13	By Cash		5,000
				Jan 19	By Cash		17,000
				Jan 20	By Ashok		9,000
				Jan 25	By Cash		13,500
					Total		55,500

ASHOK'S ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
Jan 8	To Sales		3,000	Jan 21	By Cash		8,000
Jan 20	To Sales		9,000	Jan 23	By Cash		2000
	Total		12,000		Total		10,000

COMPUTER ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007							
Jan 11	To Bank		30,000				

INSURANCE ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 12	To Cash		1,500				

DRAWINGS ACCOUNT

Dr Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 15	To bank		10,000				

ALKA'S ACCOUNT

Dr Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 22	To cash		9,000	2007 Jan 17	By purchases		17,000

BANK LOAN ACCOUNT

Dr Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
Jan 24				2007	By bank		50,000

SALARY ACCOUNT

Dr Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 31	To cash		7,500				

RENT ACCOUNT

Dr Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007 Jan 31	To cash		5,000				

TRIAL BALANCE OF SURESH
AS ON 31.1.2007

NAME OF ACCOUNT	DEBIT BALANCES	CREDIT BALANCES
Cash	6,23,500	4,16,000
Bank	3,50,000	1,14,000
Capital	-	5,00,000
Furniture	50,000	-
Purchases	83,000	-
Mohan	-	10,000
Stationery	1,000	-
Ravi	16,000	26,000
Sales	-	55,500
Ashok	12,000	10,000
Computer	30,000	-
Insurance	1,500	-
Drawings	10,000	-
Alka	9,000	17,000
Bank Loan	-	50,000
Salary	7,500	-
Rent	5,000	
	-	
Total	**11,98,500**	**11,98,500**

5.3.2 Balance Method:

In this method, the trial balance is prepared by showing the balances of the ledger accounts in the trial balance. The debit balances are shown in the debit column and the credit balances are shown in the credit column. The total of the balances of the two columns are metched. If the total of the debit column is equal to the total of the credit column then only the trial balance is said to agree and it proves the arithmetic accuracy of the recording of the transactions in the journal and ledger and the balancing of the ledger accounts. The balances of the ledger accounts are used in preparing the trial balances because the balance of a ledger account summarises the net effect of all transactions relating to an account and helps in preparing the 'Trading and Profit and Loss Account' and the 'Balance Sheet' of the business. Preparation of trial balance using the balance method is the most widely used and popular method.

Illustration 2: Enter the following transactions in the books of Kamal, post them in ledger and prepare a trial balance as on 30.04.2007

		Rs.
2007		
April 1	Started business with Cash	1,00,000
April 2	Deposited Cash into Bank	30,000
April 5	Purchased goods for Cash	10,000
April 6	Purchased goods from Naveen	20,000
April 10	Paid to Naveen on account	8,000
April 15	Purchased goods from Kavi	40,000
April 16	Paid to Kavi on account by Cheque	18,000
April 20	Sold goods for Cash	35,000
April 25	Sold goods to Vimal	30,000
April 28	Received from Vimal on account	21,000
April 30	Paid Salary	14,000

KAMAL'S JOURNAL

Date	Particulars	LF	Debit Amount Rs.	Debit Amount Rs.
2007 April 1	Cash Account....................................Dr To Capital Account (Started business)		1,00,000	1,00,000
April 2	Bank Account....................................Dr To Cash Account (Deposited Capital)		30,000	30,000
April 5	Purchases Account...........................Dr To Cash (Purchased goods for Cash)		10,000	10,000
April 6	Purchases Account...........................Dr To Naveen's Account (Purchased goods from Naveen)		20,000	20,000
April 10	Naveen's Account.............................Dr To Cash Account (Paid to Naveen on Account)		8,000	8,000
April 15	Purchases Account...........................Dr To Kavi's Account (Purchased goods from Kavi)		40,000	40,000
April 18	Kavi's Account..................................Dr To Bank (Paid to Kavi on Account)		18,000	18,000
April 20	Cash Account....................................Dr To Sales Accounts (Cash Sales)		35,000	35,000
April 25	Vimal's Account.................................Dr To Sales Account (Sold goods to Vimal)		30,000	30,000
April 28	Cash Account.................................Dr To Vimal's Account (Received from Vimal on Account)		21,000	21,000
April 30	Salary Account.................................Dr To Cash (Paid Salary)		14,000	14,000

LEDGER

CASH ACCOUNT

Dr | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 1	To Capital		1,00,000	April 2	By Bank		30,000
April 20	To Sales		35,000	April 5	By Purchases		10,000
April 25	To Vimal		21,000	April 10	By Naveen		8,000
				April 30	By Salary		14,000
				April 30	By balance c/d		94,000
			1,56,000				1,56,000
May 1	To Balance b/d		94,000				

CAPITAL ACCOUNT

Dr | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 30	To Balance c/d		1,00,000	April 1	By Cash		1,00,000
			1,00,000				1,00,000
				May 1	By Balance b/d		1,00,000

PURCHASE ACCOUNT

Dr | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 5	To Cash		10,000	April 30	By Balance b/d		70,000
April 6	To Naveen		20,000		(Trading A/c)		
April 15	To Kavi		40,000				
			70,000				70,000
May 1	To balance b/d		70,000				

SALES ACCOUNT

Dr | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 30	To Balance b/d		65,000	April 20	By Cash		35,000
	(Trading A/c)			April 25	By Vimal		30,000
			65,000				65,000
				May 1	By Balance b/d		65,000

NAVEENS ACCOUNT

Dr **Cr**

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 10	To Cash		8,000	April 5	By Purchase		20,000
" 30	To balance b/d		12,000				
			20,000				20,000
				May 1	By balance b/d		12,000

BANK ACCOUNT

Dr **Cr**

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 2	To Cash		30,000	April 8	By Kavi		18,000
				" 30	By balance b/d		12,000
			30,000				30,000
" 30	To balance b/d		12,000				

KAVI'S ACCOUNT

Dr **Cr**

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 1	To Bank		18,000	April 15	By Purchases		40,000
" 30	To balance b/d		22,000				
			40,000				40,000
				May 1	By balance b/d		22,000

VIMALS ACCOUNT

Dr **Cr**

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 25	To Sales		30,000	April 28	By Cash		21,000
				" 30	By balance b/d		9,000
			30,000				30,000
May 1	To balance b/d		9,000				

SALARY ACCOUNT

Dr | | | | | | | Cr

Date	Particulars	J F	Amount Rs.	Date	Particulars	J F	Amount Rs.
2007				2007			
April 30	To Cash		14,000	April 30	By balance b/d		14,000
			14,000		(P/L A/c)		14,000
May 1	To balance b/d		14,000				

TRIAL BALANCE OF SURESH
AS ON 31.1.2007

NAME OF ACCOUNT	DEBIT BALANCES Rs.	CREDIT BALANCES Rs.
Cash	94,000	
Capital		1,00,000
Purchases	70,000	
Sales		65,000
Naveen		12,000
Bank	12,000	
Kavi		22,000
Vimal	9,000	
Salary	14,000	
	1,99,000	1,99,000

5.4 Errors not Affecting Trial Balance

As discussed above, trial balance is a statement of the balances of the ledger account of an enterprise put in a columnar form, the debit balances in the debit column and the credit balances in the credit column. It is prepared to test the arithmetical accuracy of recording the transactions in the journal proper and subsidiary book and also the ledger posting of these transactions. The agreement of the trial balance indicates that both the aspects of each transaction, i.e. debit aspect and credit aspect, have been recorded and that the books of accounts are arithmetically accurate. If the trial balance agrees, it does not mean that there are absolutely no errors in the books; there may yet be some errors which are not disclosed by the trial balance. Some such errors are discused below.

(i) **Omission of a transaction in the original book :** If a transaction is not at all recorded in the book of original entry, i.e. the subsidiary book, it means that both the aspects of the transaction are being omitted. This, however, will not affect the agreement of the trial balances. For example, purchase of goods from X has not been recorded in the purchases book, which means that neither purchases account has been debited nor X's account has been credited in the ledger. This omission will not result in the disagreement of the trial balance.

(ii) **Posting an item on the correct side but in a wrong account :** If a ledger posting is done in a wrong account but on the same side in which it would have been done in the correct account, this error will not be disclosed by the trial balance. For example, a payment to Mr A has been debited to the account of Mr B.

(iii) **Recording of wrong amount in the subsidiary book :** Subsidiary books are books of original entries. If a wrong amount is recorded in a subsidiary book, the same will not affect the trial balance, for e.g. a sale of Rs.5,000 if recorded in the subsidiary book as Rs.500 will neither affect the total of the sales account nor the account of the customer. The total debits and the total credits will also remain the same.

(iv) **Compensating errors :** If the wrong impact of an error is notarised by the wrong impact of some other error or errors the same will not affect the trial balance, for e.g., if a wrong credit of Rs.2,000 in an account is offset by a wrong debit in some other account, these will not affect the trial balances.

(v) **Errors of principle :** Transactions in the books of accounts are recorded on the basis of some accounting principles, concepts, conventions, assumptions etc. If an accounting principle is violated at the time of recording a transaction, the same will not affect the trial balance, for e.g., say wagas paid for the installtion of machinery are debited in the wages account. This error will not affect the trial balance even though it is a capital expenditure and should have been debited to the machinery account. By debiting it to wages account, it has been considered as revenue expenditure which is an error of principle.

The disagreement of the trial balance indicates that some errors have been committed in the accounting process adopted up to the preparation of the trial balance. If the difference in the totals of the debit column and the totals of the credit columns is very large then all possible steps should be undertaken to identify and rectify the errors. It is not desirable to prepare the final accounts in such a situation as they will not present the true picture of the state of affairs of the business enterprise. But if, because of the requirement of law under some special circumstances, the preparation of final accounts cannot be delayed, then the difference in the trial balance may be put on the shorter side in a 'Suspense Account'. In such a situation the account will be shown in the balance sheet. The debit balance will be shown on the asset side and the credit balance on the liability side.

5.5 Types of Errors

Accounting errors can be divided into the following categories

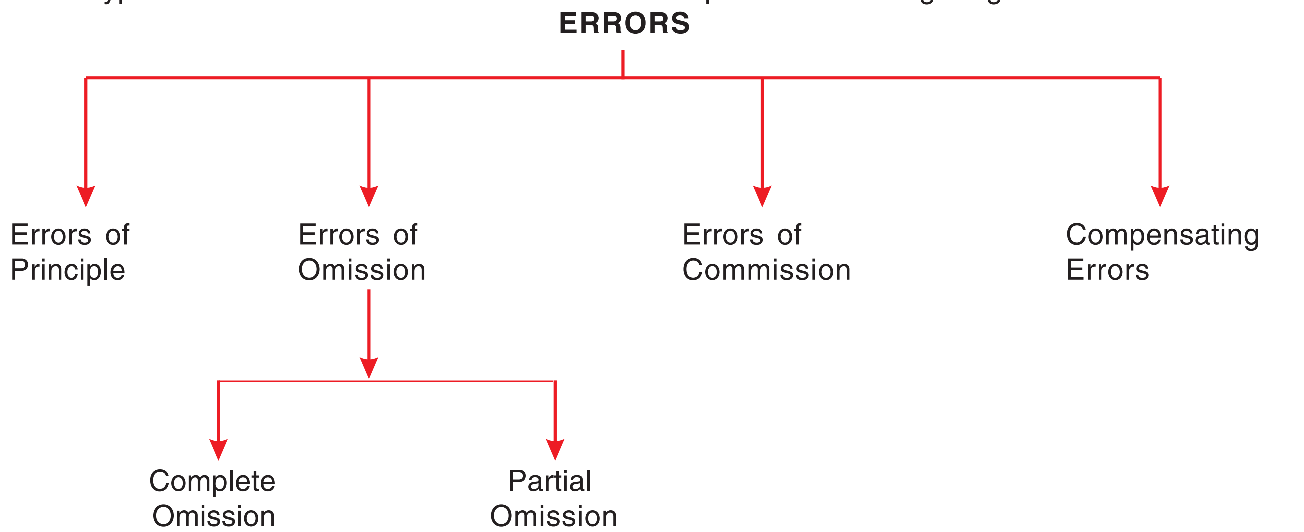
(i) Errors of Principle.

(ii) Errors of Omission

(iii) Errors of Commission

(iv) Compensating Errors

The different types of errors have been shown with the help of the following diagram



Errors of Principle: When an accounting transaction is recorded in the books of accounts violating an accounting principle, such an error is called error of principle. Such errors take place when amount received or spent is not properly distinguished as Capital and Revenue. The distinction is of paramount importance because any incorrect allocation between revenue and capital will not indicate the correct position of profit earned or loss suffered by the enterprise and the position of its assets and liabilities shown as by its final accounts. In other words, wrongly considering a revenue item, as a capital item or vice versa results in errors of principle. For examples furniture purchased by a firm dealing in the financial securities for use in its office if considered as an ordinary purchase will be an error of principle. Similarly, when furniture is purchased for the purpose of resale by a furniture dealer it is treated as goods purchase and will be included in the purchase account not furniture account. If it is included in assets account, it will be an error of principle. etc. Amount spent on the ordinary repair of building or machinery wrongly debited to Building/Machine account will be an error of principle.

Errors of Omission: When a transaction is totally or partly omitted from being recorded in the books of accounts then such an error is called error of omission. They can be of two types.

i. **Complete omission** : When a transaction is completely omitted from being recorded in the books of accounts then the resultant error is called error of complete omission. For example not recording a transaction in a subsidiary book. This will neither affect the debit balance nor the credit balance and hence will not affect the agreement of trial balance. Such errors are not disclosed by the trial balance.

ii. **Partial omission:** When a transaction is entered in the subsidiary book but while doing ledger posting one aspect of the transaction, either debit or credit, is not posted in the ledger such an error is called error of partial omission. For e.g., total of purchases book, sales book, purchase return book, sales return, book not posted in the respective purchases account or sales account or posting of a transaction from the cash book is not done in the concerned account or posting is not done from the purchases book, sales book, purchases return book, sales return, Book or posting of only one aspect of the transaction either debit or credit in the ledger. Errors of partial omission affect the agreement of the trial balance because due to such errors there will be either short debit or short credit.

Errors of Commission: These errors are the result of some commission. They are committed by doing something which was not supposed to be done. They take place during the course of recording of transactions in the books of accounts because of the carelessness, ignorance, lack of knowledge etc. of the people entrusted with the job of recording the transactions in the books of accounts. Examples of such errors are wrong casting of subsidiary book, posting a wrong amount in an account, posting an amount on the wrong side of an account, posting an amount in wrong account but on the same side, posting an amount in the wrong side of wrong account, recording of a transaction in a subsidiary book, carrying forward of wrong amount etc.

Compensating errors: These errors cancel each other. In other words, when an error offsets the wrong effect of an already committed error, it is called a compensating error. The amount involved in such errors is the same, for example, overcasting or undercasting of the purchases book may be compensated with the overcasting or undercasting of the sales book respectively with a similar amount, or omission of posting of an amount in an account may be compensated by posting wrongly similar amount on the same side of another account. Compensating errors do not affect the agreement of the trial balance and may exist in spite of the agreement of the trial balance.

5.6 Effect of Errors on Trial Balance

From the point of view of the effect of errors on trial balance, accounting errors can be divided into the following two categories.

(i) Errors affecting trial balance.

(ii) Errors not affecting trial balance

Error affecting trial balance: Errors which affect only one side of an account affect the agreement of the trial balance. Such types of errors are disclosed by the trial balance. Following are some examples of such types of errors.

- Wrong casting of a subsidiary book
- Wrong casting of the totals of pages of the subsidiary books
- Wrong carry forward of totals from one page to another page

- Wrong posting of amount from the subsidiary book to the ledger account
- Wrong balancing of a ledger account
- Omission of posting of a ledger balance to the trial balance
- Wrong posting of a ledger balance in the trial balance
- Posting of a ledger balance in the wrong column of the trial balance
- Wrong totaling of the trial balance
- Errors in preparation of various schedules like debtors schedule and creditors schedule.

Errors not affecting trial balance : There are certain types of accounting errors which do not affect the agreement of the trial balance and hence are not disclosed by it. Some examples of such errors are given below.

- Errors of Complete Omission do not affect the agreement of the trial balance, for example, not recording the transactions in books of original entry, omission of posting of the transaction from the subsidiary books to the ledger etc.
- Posting a correct amount in a wrong account but on the correct side, for e.g., Rs 1,000 paid to Ram wrongly debited to Shyam's account.
- Errors of Principle do not affect the agreement of the trial balance because such errors do not affect the debit balances and the credit balances, for example, payment of wages for the manufacture of furniture is an error of principle but will not affect the trial balance.
- Errors of Compensation naturalise the wrong effect of an already committed error and hence such errors do not affect the trial balance, for example, a sale of Rs 4,000 was recorded in the purchases book. However, the customers account was correctly debited and the sales account was correctly credited while posting the purchases book. The second error in this case has cancelled the effect of the first error and hence will not affect the trial balance.

5.7 Location of Errors

You have already learnt that agreement of the trial balance is not a conclusive proof of the accuracy of the accounts, and if it does not agree, than it is a clear indication that some error(s) have been committed during the course of accounting process adopted till the prepration of the trial balance. Before taking up work of preparation of final accounts, we should try to locate the errors committed so far and rectify them. For locating the errors with minimum effort, we should reverse the steps which were followed in the accounting process till the stage of preparation of trial balance. These steps have been detailed as follows.

(i) Recast the totals of the debit and credit columns of the trial balance.

(ii) Re-check to ensure that the ledger balances of all the accounts have correctly been transferred in the respective debit and credit columns of the trial balance.

(iii) Re-check the balances of the individual accounts in the ledger.

(iv) Re-check the corrections of the balances of all accounts individually in the ledger.

(v) Re-check that all the entries from the subsidiary books have been correctly posted in the respective ledger accounts.

(vi) Find out the difference in the totals of the debit column and the credit column and see whether it is divisible by 2. If it is so than there is a possibility that an amount equal to one half of the difference may have been posted to the wrong side of another ledger account, for e.g., if there is a difference of Rs. 2,000 between the two totals of the trial balance than it is quite possible that a credited item of Rs 1000 has been posted wrongly in the ledger as a debit item. For locating side errors, the accountant must scrutinise all the debit entries of Rs. 1,000.

(vii) If the difference between the totals of the debit and credit columns of the trial balance is divisible by 9 than there is a possibility of the transposition of the digits of the amount figure, for e.g. if a debit amount of Rs. 575 is posted as Rs. 755, the debit trial in the trial balance will exceed by Rs.180. This difference is divisible by 9.

5.8 Rectification of Errors

You have learned the process adopted for the location of errors. Once the errors have been located than we have to rectify the same. Now we shall learn the method of rectification of errors. It is important to note that for rectification erasing or striking of figures should be avoided. Erasing or striking of figures tend to discredit the records and increase the chances for fraud. It also reduces the legal value of the books of accounts, apart from giving a dirty look. Thus erasing or striking off the figures in the books of accounts are strictly avoided. For the purpose of rectification the errors can be divided into the following two types.

1. Errors not affecting trial balance
2. Errors affecting trial balance.

5.8.1 Rectification of Errors not Affecting Trial Balance

You have already learnt that errors not affecting trial balance are mostly errors of complete omission, errors of principle and compensating errors. Such errors are rectified by passing an adjustment entry. In case of a rectification, we may first see 'what was actually done?' that is, what errors have been made. Secondly, we may see 'what should have been done?' that is finding the correct entry which should have been made. Thirdly, make the entry for the correction of error. Consider the following illustrations.

ILLUSTRATION 1

Rectify the following errors

1. The purchase of machinery for Rs. 5,00,000 has been entered in Purchase Day Book.
2. Received Rs. 10,000 from Mukesh but credited to Mohan's Account.
3. A sale of old machinery for Rs. 70,000 has been entered in Sales Account.
4. Rs. 5,000 paid as wages for erection of a machine has been charged to Repairs Account.
5. Rs. 5,100 received from Govind, previously written off as bad debt, has been credited to his Account.

Solution :

What is actually done? wrong entry has been made.
What should have been done? correct entry should have been made.
What should be done now to rectify the error? Rectification entry should be made.

Journal

Date	Particular		Rs.	J.F	Dr. Amount Rs.	Cr. Amount Rs.
1.	Wrong entry made :	Purchase A/c	Dr.		5,00,000	
		To Creditors A/c				5,00,000
	Correct entry :	Machinery A/c	Dr.		5,00,000	
		To Creditors A/c				5,00,000
	Rectification entry :	Machinery A/c	Dr.		5,00,000	
		To Purchase A/c				5,00,000

There is no mistake in the Creditors Account as it has been credited correctly. Purchase Account was wrongly debited instead of Machinery Account. To rectify the error, the debit entry in the Purchase Account has to be transferred to Machinery Account. That is, the wrong debit in the Purchase Account is cancelled by giving a credit entry.

Date	Particular		Rs.	J.F	Dr. Amount Rs.	Cr. Amount Rs.
2.	Wrong entry made :	Cash Account	Dr.		10,000	
		To Mohan's A/c				10,000
	Correct entry :	Cash A/c	Dr.		10,000	
		To Mukesh's A/c				10,000
	Rectification entry :	Mohan's A/c	Dr.		10,000	
		To Mukesh Account				10,000

Cash Account is correct. The mistake is that Mohan's account is wrongly credited and Mukesh' Account has been omitted to be entered. To rectify the error, we have to cancel the wrong credit by giving an equal debit and credit in Mukesh Acount.

Date	Particular		Rs.	J.F	Dr. Amount Rs.	Cr. Amount Rs.
3.	Wrong entry made :	Customer's A/c	Dr.		70,000	
		To Sales A/c				70,000
	Correct entry :	Customer's A/c	Dr.		70,000	
		To Machinery A/c				70,000
	Rectification entry :	Sales A/c	Dr.		70,000	
		To Machinery Account.				70,000

Customer Account is debited correctly. But Sales Account has been credited instead of crediting Machinery Account. To rectify the error one has to cancel the wrong credit by giving an equal amount of debit in Sales Account and credit Machinery Account.

Date	Particular		Rs.	J.F	Dr. Amount Rs.	Cr. Amount Rs.
4.	Wrong entry made :	Repairs A/c	Dr.		5,000	
		To Cash A/c				5,000
	Correct entry :	Machinery A/c	Dr.		5,000	
		To Cash A/c				5,000
	Rectification entry :	Machinery A/c	Dr.		5,000	
		To Repair A/c				5,000

Cash account is correctly credited. But debit entry has been wrongly made to Repairs Account instead of Machinery Account. To rectify the error, debit the Machinery Account and credit the Repairs Account.

Date	Particular		Rs.	J.F	Dr. Amount Rs.	Cr. Amount Rs.
5.	Wrong entry made :	Cash A/c	Dr.		5,100	
		To Govind A/c				5,100
	Correct entry :	Cash A/c	Dr.		5,100	
		To Bad Debts Recovered A/c				5,100
	Rectification entry :	Govind A/c	Dr.		5,100	
		To Bad Debts Recovered A/c				5,100

Cash Account is correctly debited. Bad Debts Recovered Account must be credited. But by mistake, Govind Account has been credited. Now the wrong credit given to Govind Account has to cancel and a for that credit entry is to be made to Bad Debts Recovered Account.

The time of detection of errors decides the mode of rectification. To be more detailed, the errors can be rectified in three stages as follows (a practical approach).

ILLUSTRATION 2

Rectify the following errors in the books of Roshan Lal :

1. A sale to Babu for Rs.261 has been entered in Sales Book as Rs.216.
2. A typewriter purchase for Rs.3,000 has been entered in the Purchase Book.
3. An old machine sold for Rs.800 was entered in the Sales Book.
4. Goods worth Rs.1,500 sold to Ramlal has been entered in the Purchase Book.

SOLUTION

			Rs.	Rs.
1.	Babu Account	Dr.	45	
	To Sales Account			45

(Being sales of Rs.261 to Babu were entered in the Sales Book as Rs 216. The error is now rectified Rs. 261-216=Rs. 45 which is less than the actual sales amount).

			Rs.	Rs.
2.	Typewriter Account	Dr.	3,000	
	To Purchase Account			3,000

(Being purchase of typewriter which was wrongly entered in the Purchase Account, is now rectified.) What is done is that wrong debit is given to Purchase Account. There is no entry in the Typewriter Account. Now the debit in the Purchase Account has to be cancelled and Typewriter Account has to be entered.

			Rs.	Rs.
3.	Sales Account	Dr.		800
	To Machinery Account			800

(The wrong entry made to Sales Account is now rectified. The sale of machine should not have been entered in the Sales Account. Therefore, debit the Sales Account to cancel the wrong entry and credit the Machinery Account, which has not been entered.)

			Rs.	Rs.
4.	Ramlal Account	Dr.	3,000	
	To Purchase Account			1,500
	To Sales Account			1,500

(Being sales made to Ramlal, wrongly entered in the purchase book, are now corrected)

What is done is that instead of giving a debit to Ramlal Account, he has been credited with Rs1,500. Therefore, his account is debited with Rs.1,500 to cancel the credit entry and again debit with Rs.1,500 for the sales made to him. Thus total of Rs.(1,500+1,500) is debited to his account. Then Purchase Account is credited with Rs.1,500 to cancel the wrong debit entry. Sales Account is also credited with Rs. 1,500 which has not been credited earlier.

ILLUSTRATION 3

Show how you will rectify the following errors

1. A credit sale of Rs.450 to Babu was debited to Bhola.
2. An office Almirah purchased for Rs. 750 was debited to Repairs Account.
3. Purchase of goods for the consumption of the proprietor were debited to Purchase Account worth Rs. 1,000.

SOLUTION :

			Dr.	Cr.
			Rs.	Rs.
1.	Babu Account	Dr.	450	
	To Bhola Account			450
	(Being sales made to Babu wrongly debited to Bhola now rectified)			

			Rs.	Rs.
2.	Office Furniture Account	Dr.	750	
	To Repairs Account			750
	(Being the purchase of office furniture wrongly debited to Repairs Account, now rectified)			

			Dr.	Cr.
			Rs.	Rs.
3.	Drawing Account	Dr.	1,000	
	To Purchase Account			1,000
	(Being sales purchase of goods for personal consumption wrongly debited to Purchase Account, now rectified)			

5.8.2 Rectification of Errors Affecting Trial Balance Suspense Account

When the Trial Balance disagrees, efforts are made to locate the errors and to rectify them. When the errors cannot be located, and the preparation of the Final Accounts is urgent, the difference in the Trial Balance is made good by writing it temporarily in the smaller side of the Trial Balance, under the name of 'Suspense' account'. The Suspense Account is only a temporary device which should not be allowed to remain in the books for long. In the next Accounting period, attempts must be made to discover the errors which caused the difference in the Trial Balance. Again if the credit side of the Trial Balance is shorter, the Suspense Account is credited and if the debit side of the Trial Balance is shorter, the Suspense Account is debited. Thus, the Trial Balance is artificially tallied and the Final Accounts are prepared. The Suspense Account also is shown in the Balance Sheet. If it shows a debit balance, it appears on the asset side, and if it shows a credit balance, it appears on the liability side. Errors affecting trial balance are single sided errors. These errors are also rectified with the help of suspense account by passing a journal entry.

ILLUSTRATION 4

The Trial Balance of Mr. Gujral did not agree and the difference was temporarily put to Suspense Account. Later on the following errors were located. Pass the entries to rectify them.

(i) The total of debit side of an Expense Account has been cast in excess by Rs.1,500.
(ii) The Sales Account has been totaled short by Rs.2,100.
(iii) One item of purchase of Rs 25 has been posted from the Day Book to ledger as Rs250.
(iv) The Sale Return of Rs 4,100 from a party has not been posted to that Account, though the party's Account has been credited.
(v) A Cheque of Rs. 6,500 issued to the Supplier's Account (shown under Sundry Creditors) towards his dues has been wrongly debited to the Purchase Account.
(vi) A credit sale of Rs. 750 has been credited to the Sales and also credited to Sundry Debtors Account.

SOLUTION

In this problem, the difference has been placed in the Suspense Account. But only one-sided errors require the use of Suspense Account. Two-sided errors are rectified by just passing usual entries in the journal proper.

			Dr.	Cr.
(i)	Suspense Account	Dr.	Rs.	Rs.
	To Expense Account		1,500	
	(Being the error in totaling of an Expense Account, now rectified)			1,500

(ii)	Suspense Account	Dr.	2,100	
	To Sales Account			2,100
	(Being undercast of sales book now rectified)			
(iii)	Supplier Account	Dr.	225	
	To Suspense Account			225
	(Being the wrong excess debited to Supplier Account Rs. 250 – 25 = Rs. 255, now rectified. There is no error in the Purchase Account as the Purchase Account is debited with the total Purchase Book.			
(iv)	Sales Returns Account	Dr.	4,100	
	To Suspense Account			4,100
	(Being the entry to the Sales Returns Account, which has not been entered)			
(v)	Sundry Creditor Account	Dr.	6,500	
	To Suspense Account			6,500
	(Being the wrong debit given to Purchase Account, is now rectified)			
(vi)	Sundry Debtors Account	Dr.	1,500	
	To Suspense Account			
	(Being the sales wrongly credited to Debtor's Account,			1,500
	is now rectified)			

ILLUSTRATION 5

The following errors were located in the books of a concern after its books were closed and a Suspense Account was created in order to get the Trial Balance agreed. Rectify the errors.

(i) Sales Day Book was overcast by Rs. 200.

(ii) A sale of Rs.500 to Xavier was wrongly debited to the Account of John Xavier.

(iii) Repair Expenses of Rs. 180 was posted as Rs. 810.

(iv) A bill Receivable received from Poppy for Rs. 300 was passed through Bills Payable Books.

(v) Legal expenses of Rs. 900 paid to advocate Mr Mohan was debited to his personal account.

(vi) Cash received from Das was debited to Dasan Account for Rs. 150.

(vii) While carrying forward the total of one page of the Purchase Book to the next, the amount of Rs. 2,345 was written as Rs. 3,245.

SOLUTION

			Dr. Rs.	Cr. Rs.
(i)	Sales Account	Dr.	200	
	To Suspense Account			200
	(Being overcast in Sales Day Book, now rectified)			
(ii)	Xavier Account	Dr.	500	
	To John Xavier Account			500
	(Being sales made to Xavier wrongly debited to John Xavier Account, Now rectified)			
(iii)	Suspense Account	Dr.	630	
	To Repairs Account			630
	(Being Repairs Account debit of Rs.8.10 in place of Rs.180, is now rectified)			

(iv)	Bills payable Account	Dr.	300	
	Bills Receivable Account	Dr.	300	
	To Poppy Account.			600
	(Being Bills Receivable passed through Bills Payable Book, now rectified)			
(v)	Legal Expenses Account	Dr.	900	
	To Mohan Account			900
	(Being legal expenses paid, wrongly debited to Mohan Account, now rectified)			
(vi)	Suspense Account	Dr.	300	
	To Dasan Account			150
	To Das Account			150
	(Being the sales wrongly credited to Debtors Account, is now rectified)			
(vii)	Suspense Account	Dr.	900	
	To purchase Account			900
	(Being excess amount of Rs.900 (Rs.3245 - Rs. 2345) debited in Purchase Account, now rectified)			

Dr. **Suspense Account** Cr.

	Rs.		Rs.
To Repairs Account	630	By Difference in Trial Balance	1,630
To Dasan Account	150	(Balance figure)	
To Das Account	150	By Sales Account	200
To Purchase Account	900		
	1,830		**1,830**

ILLUSTRATION 6

How do you rectify the following errors through a Suspense Account?

1. Furniture purchased for Rs.700 was taken to the Purchase Account.
2. Goods sold on credit to A for Rs 6,000 were debited to Bs Account.
3. Goods worth Rs.1,000 returned by C were not passed through the Sales Returns Book.
4. An amount of Rs.2,600 incurred for repairs to Machinery was debited to the Machinery Account.
5. Goods worth Rs.2,700 purchased from E were posted to the debit side of the Personal Account.
6. An amount of Rs.500 received in cash from F towards Rent was not posted to Rent Account.
7. An amount of Rs.600 received from G for cash sales was debited to Hs Account.

Solution			**Dr.**	**Cr.**
1.	Furniture Account	Dr.	Rs.	Rs.
	To Purchase Account		700	
	(Being the furniture purchased wrongly debited to Purchase Account, now rectified)			700
2.	As Account	Dr.	6,000	
	To Bs Account			6,000
	(Being the wrong debit to Bs Account, now rectified)			

3.	Sales Returns Account	Dr.	1,000	
	To Cs Account			1,000
	(Being the wrong entry made in the Purchase Book is rectified)			
4.	Repairs Account			
	To Machinery Account	Dr.	2,600	
	(Being the rectification of wrong entry made in Machinery Account)			2,600
5.	Suspense Account	Dr.	5,400	
	To Es Account			5,400
	(Being the wrong debit in Es Account, now rectified)			
6.	Suspense Account	Dr.	500	
	To Rent Account			500
	(Being the Rent Account, which is not credited, is now rectified)			
7.	Suspense Account	Dr	600	
	To H's Account			600
	(Being the wrong debit made to H's account, now rectified)			

ILLUSTRATION 7

A Bookkeeper, having failed to agree the Trial Balance, opened a Suspense Account and transferred the difference of Rs1709 to the credit of Suspense Account. The following errors were later discovered. Give journal entries and show the Suspense Account.

1. Sales Book was undercast by Rs. 2000..
2. Purchase of Machinery for Rs 3,000 was passed through the Purchase Book.
3. Goods sold to Raj for Rs. 45 was posted to his account as Rs. 54.
4. Purchase of Returns Book was overcast by Rs. 200.
5. The total of the Sales Book page 10 was carried forward as Rs 1,222 instead of Rs 1,122.

Solution

In the case of those errors which affect only one account, introduce Suspense Account to make a journal entry.

			Dr. Rs.	**Cr.** Rs.
1.	Suspense Account	Dr.	2,000	
	To Sales Account			2,000
	(Being undercast of sales rectified)			
2.	Machinery Account	Dr	3,000	
	To Purchase Account			3,000
	(Being the debit given to Purchase Account instead of Machinery Account, now rectified)			
3.	Suspense Account	Dr	9	
	To Raj Account			9
	(Being the excess debit given to Raj, now rectified)			
4.	Purchase Returns Account	Dr	200	
	To Suspense Account			200
	(Being the overcast of Purchase Return Book, rectified)			

5.	Sales Account To Suspense Account (Being excess carry forward of the total of Sales Book, now rectified)	Dr	100	100

Dr. **Suspense Account** Cr.

	Rs.		Rs.
To Sales Account	2,000	By Difference in Books	1,709
To Raj Account	9	By Purchase Returns A/c	200
		By Sales Account	100
	2,009		**2,009**

ILLUSTRATION 8

The Trial Balance of Balan on 31 December 1992 showed a difference of Rs 580 (excess debit). It was put to a Suspense Account and the books were closed. On going through the books in January 1993, the following errors were discovered. You are required to pass rectifying journal entries and prepare the Suspense Account.

1. Rs.540 received from Mehta was posted to the debit of his account.
2. Rs. 100 being Purchase Returns was posted to the debit of Purchase Account.
3. Discount Rs 200 received, entered in the Cash Book was not posted to the ledger.
4. Rs 574 paid for repairs to motor car was debited to the motor car account as Rs. 174.
5. A sale of Rs 350 to Sethi was entered in the Sales Book as Rs. 530.
6. While carrying forward total of one page in Kamal Account, the amount of Rs 250 was written on the credit side instead of debit side.
7. The purchase of machinery on 1 January 1992 for Rs 6,000 was entered in the Purchase Account.

SOLUTION

			Dr. Rs.	Cr. Rs.
1.	Suspense Account To Mehta Account (Being Rs. 540 received from Mehta wrongly debited to him, now rectified)	Dr	1,080	1,080
2.	Suspense Account To Purchase Account To Purchase Returns (Being purchase returns of Rs. 100 wrongly debited to Purchase account and omission in Purchase Returns, now rectified)	Dr.	200	100 100
3.	Suspense Account To Discount Account (Being omission in Discount Account, now rectified)	Dr.	200	200
4.	Repairs Account To Motor Car Account To Suspense Account (Being repairs to motor car Rs. 574, wrongly debited to Motor Car as Rs 174, now rectified)	Dr.	574	174 400

5	Sales Account	Dr.	180	
	To Sethi Account			180
	(Being sales of Rs 350, wrongly entered in Sales Book as Rs 530, now rectified)			
6.	Kamal Account	Dr.	500	
	To Suspense Account			500
	(Being Kamal Account credited with Rs. 250 instead of being debited Rs 250, now rectified)			
7.	Machinery Account	Dr.	6,000	
	To Purchase Account			6,000
	(Being purchase of Machinery wrongly debited to Purchase Account, now rectified)			

ILLUSTRATION 9

The following errors were located in the books of a concern after its books were closed and a Suspense Account was opened with a credit balance of Rs. 352. Rectify the errors and prepare Suspense Account.

1. Sales Day Book was overcast by Rs.100.
2. A sale of Rs 50 to X was wrongly debited to the Y Account.
3. General expense Rs 18 was posted in the General Ledger as Rs 80.
4. A Bill Receivable for Rs 155 was passed through Bills Payable Book. The bill was given by P.
5. Legal expenses Rs 119 paid to Duftry was debited to his Personal A/c.
6. Cash received from C. Das was debited to G. Das, Rs150.
7. While carrying forward the total of one page of the Purchase Book to the next, the amount of Rs 1,235 was written as Rs. 1,325.

Find out the nature and amount of the Suspense Account and pass entries for the rectification of the above errors in the subsequent year's books.

SOLUTION			**Dr.**	**Cr.**
			Rs.	Rs.
1.	Sales Account	Dr.	100	
	To Suspense Account			100
	(Being Sales Book overcast, now rectified))			
2.	X Account	Dr	50	
	To Y Account			50
	(Being sales to X, wrongly debited to Y A/c, now rectified)			
3.	Suspense Account	Dr	62	
	To General Expenses Account			62
	(Being general expenses of Rs 18, debited as Rs. 80, now rectified)			
4.	Bills Payable Account	Dr.	155	
	Bills Receivable Account	Dr.	155	
	To P Account			310
	(Being Bills receivable from P wrongly entered in Bills Payable Book, now rectified)			
5.	Legal Expenses Account	Dr.	119	
	To Daftry Account			119
	Being legal expenses paid to Daftry wrongly debited to G. Das, now rectified)			

6.	Suspense Account To G. Das To C. Das (Being cash received from C. Das, wrongly debited to G. Das, now rectified)	Dr.	300	
				150 150

6. Suspense Account Dr. 300
   To G. Das 150
   To C. Das 150
   (Being cash received from C. Das, wrongly debited to G. Das, now rectified)

7. Suspense Account Dr. 90
   To Purchase 90
   (Being carry forward Rs 1,325, instead of Rs. 1,235, now corrected)

Dr. **Suspense Account** Cr.

	Rs.		Rs.
To General Expenses Account	62	By Difference in Books on the Basis of Trial Bal. (Balancing fig)	352
To C. Das Account	150	By Sales Account	100
To G. Das Account	150		
To Purchases	90		
	452		**452**

ILLUSTRATION 10

The trial balance of a trader did not agree. The credit side was more by Rs. 310, so the difference was put in the Suspense Account. Afterwards the following errors were found. Rectify the errors and prepare Suspense Account.

1. A sale of goods to X for Rs. 350 has been credited to his account.
2. Goods purchased from Y amounting to Rs.750 were entered in the Purchase Day Book but were omitted from Y's account in the Creditors Ledger.
3. An office typewriter purchased for Rs. 500 has been passed through the Purchase Account.
4. Goods returned to S. Sen valued Rs 75 were debited to P. Sen's Account.
5. Repairs to office car worth Rs 750 were debited to the Car Account.
6. Goods sold to Banerji valuedity Rs 730 have been posted into his account as Rs. 370.

SOLUTION

	Particulars		Dr. Rs.	Cr. Rs.
1.	X Account (Rs 350×2)	Dr.	700	
	To Suspense Account			700
	(Being sales to X for Rs 350, wrongly credited to his account, now rectified)			
2.	Suspense Account	Dr	750	
	To Y Account			750
	(Being sales to X, omitted to be posted, now rectified)			
3.	Office Equipment Account	Dr.	500	
	To Purchase A/c			500
	(Being purchase of typewriter, wrongly entered to Purchase Book, now rectified)			

4. S. Sen Account	Dr.	75	
To P. Sen Account			75
(Being goods returned to S. Sen wrongly debited to P.Sen, now rectified)			
5. Repair A/c	Dr.	750	
To Car Account			750
(Being repairs to car wrongly debited to Car, now rectified)			
6. Banerji Account (Rs. 730 - Rs. 370 = Rs. 360)	Dr.	360	
To Suspense Account			360
(Being sales to Banerji of Rs 730, wrongly posted to his account as Rs. 370, now rectified)			

Dr. **Suspense Account** Cr.

	Rs.		Rs.
To Difference in T.B. (Balance figure)	310	By X Account	700
		By Banerji Account	360
To Y Account	750		
	1,060		**1,060**

ILLUSTRATION 11

The following errors were discovered in the books of Slack on 31 December, 2006. The difference in the Trial Balance had been entered in a Suspense Account and, on correction of the errors, the Suspense Account was eliminated.

1. The total of the Purchase Day Book had been undercast by Rs 100.
2. The Discount column on the debit side of the Cash Book had been posted to the credit of Discount Received Account Rs. 20.
3. Sales Book is undercast by Rs. 76.
4. A cheque received from Quick for Rs 39 had been debited in the Cash Book, but the double entry had not been completed.
5. The Returns Outward Book had been overcast by Rs. 50.

Show by means of Journal entries how these errors would be corrected.

Prepare the Suspense Account bringing out the original difference.

SOLUTION

		Dr. Rs.	**Cr.** Rs.
1. Purchase A/c	Dr.	100	
To Suspense Account			100
(Being the undercasting of Purchase Day Book, now rectified)			
2. Discount A/c	Dr.	40	
To Suspense Account			
(Being Discount allowed wrongly credited to Discount Received Account, now rectified)			
3. Suspense A/c	Dr.	76	
To Sales A/c			76
(Being Sales A/c rectified)			

4.	Suspense Account	Dr.	39	
	Quick Account			39
	(Being cheque received from Quick not posted from Cash Book, now rectified)			
5.	Returns outward A/c	Dr.	50	
	To Suspense Account			50
	(Being error caused by overcasting in Returns Outward Book, now rectified)			

Dr. **Suspense Account** Cr.

	Rs.		Rs.
To Difference in T.B. (Balance figure)	75	By Purchase A/c	100
To Sales A/c	76	By Discount A/c	40
To Quick Account	39	By Returns Outward A/c	50
	190		190

ILLUSTRATION 12

The books of Mr Anandi for the year ending 31 March 2007 were closed with a difference in trial balance. The following errors were detected subsequently. You are required to pass the necessary rectification entries in the books.

(a) Returns Outward Book was cast Rs. 10 short.

(b) The total of the Discount column on the debit side of the Cash Book for March 1992, amounting to Rs. 150, was not posted to the General Ledge.

(c) Purchase book was undercast by Rs. 600.

(d) A credit sale of Rs.76 was wrongly posted to the Sales Ledger as Rs. 67.

(e) The Sales Account was understated by Rs. 1,000 because of wrong carry over in the Sales Day Book.

SOLUTION

			Dr. Rs.	Cr. Rs.
a)	Suspense Account	Dr.	10	
	To Returns Outward A/c			10
	(Being the undercasting of the Purchase Day Book rectified)			
b)	Discount A/c	Dr.	150	
	To Suspense Account			150
	(Being total of Discount column not debited, now rectified)			
c)	Purchase A/c	Dr.	600	
	To Suspense A/c			600
	(Being Purchase A/c rectified)			
d)	Customer's Account (76-67)	Dr.	9	
	To Suspense Account			9
	(Being credit sales of Rs. 76, wrongly debited to Customer Account as Rs. 67, now rectified)			

e)	Suspense Account	Dr.	1,000	
	To Sales A/c			1,000
	(Being Sales Account wrongly understated, now rectified)			

5.9 Disposal of Suspense Account

Suspense Account is an imaginary account used as temporary measure only for the purpose of reconciling a Trial Balance. Later, as and when the errors affecting the suspense account are located, rectification entries are passed with the help of suspense account. Thus, when all the errors are located and rectified, the suspense account will automatically stand closed, i.e., it will not show any balance. But if Suspense Account still shows a balance, it will indicate that certain errors are still to be discovered and rectified. In such cases, if the suspense account shows a debit balance, it is taken to the balance sheet on the assets side and, on the contrary, if it shows a credit balance it is taken to the balance sheet on the liabilities side.

Key Terms used in the Chapter

- Trial Balance
- Profit & Loss Account
- Suspense Account
- Rectification
- Compensation
- Trading Account
- Balance sheet
- Errors
- Omission
- Partial

Summary with Reference to Learning Objectives

1. Trial balance is a statement verifying the arithmetical accuracy of posting of ledger accounts.
2. Methods of Preparation of Trial Balances
   - Total Method
   - Balance Method
3. Error is a numerical mistake that may have occurred in posting or preparation of ledger accounts.
4. Categories of Errors
   - Errors which are disclosed by Trial Balance.
   - Errors which are not disclosed by trial balance.

5 Types of Errors
   - Error of Principle
   - Error of omission
   - Complete omission
   - Partial ommission
   - Error of Commission
   - Compensating errors

Questions for Practice

Short Answer Type Questions

1. Where will you transfer the total of Purchases Book?
2. Name the subsidiary books whose balance is always debit.
3. Give two examples of errors of Principle.
4. Name four errors which cannot be disclosed by preparing Trial Balance.
5. What do you mean by one sided error? Give three examples.
6. What do you mean by double sided error? Give three examples.
7. Why do we need a Suspense A/c?
8. Differentiate between capital and revenue expenditure.
9. What is the purpose of preparing suspense account?

Long Answer Type Questions

1. What do you mean by account errors? What are its different types? Explain.
2. What are the different types of errors of commission? Explain in detail.
3. How will you rectify errors of undercosting and overcosting in the
   (i) Purchase book
   (ii) Sales Book
   (iii) Returns inward book
   (iv) Returns outward book
4. How will you rectify the following errors
   (i) If posting is made at the debit side of the suppliers account through purchases book.
   (ii) If posting is made in sales book, instead of purchase book.
   (iii) If posting is made in returns inward book, instead of return outward book.
5. Explain errors which are not detected by trial balance.
6. What is a one sided error? Give two examples.
7. What is a suspense account? When is it opened and how is it closed?

Practical Questions

1. Rectify the following errors
   (i) Goods worth Rs. 302 sold to Mohan was posted to his account as Rs. 32.
   (ii) Repairs made were debited to buildings account worth Rs. 400.
   (iii) Furniture purchased for Rs. 2,000 was entered in the Purchases Book.
   (iv) Goods worth Rs. 130 sold to Prakash were posted to the debit of Naresh.

2. Rectify the following errors
   (i) The purchase of stationery worth Rs. 250 was debited to Trade Expenses Account.
   (ii) Rs. 120 paid for repairs wrongly debited to Buildings Account.
   (iii) Machinery sold for Rs. 15,000 has been posted as cash sales.
   (iv) A sum of Rs 175 paid by way of rent was debited to landlords personal account.

3. Pass journal entries to rectify the following errors
   (i) Construction of a new shed costing Rs 13,000 debited to Building Repairs Account.
   (ii) An amount of Rs 180 received on account of interest was credited to the Commission Account.
   (iii) The total of the purchases book was cost short by Rs 1,000.
   (iv) An item of Rs 150 representing returns inwards from kumar was omitted to be entered in his account.

4. How would you rectify the following errors
   (i) The credit side of Mohans account in the ledger has been overcost by Rs. 100.
   (ii) The purchases book was undercost by Rs. 300.
   (iii) Rs. 5,000 spent on extension of building have been debited to Building Repairs Account.
   (iv) The total of purchases book has been undercost by Rs. 100.

5. Rectify the following errors
   (i) A sum of Rs 250 written off as depreciation on machinery has been debited to Machinery A/c.
   (ii) A credit sale of goods of Rs. 120 to Ramesh has been wrongly passed through the Purchases Book.

(iii) Goods returned by customer worth Rs. 100 entered in Purchases Returns Book.
(iv) Sales to X worth Rs 400, posted to Ys account.

6. Rectify the following errors
   (i) Wages outstanding Rs 350 has not been taken into account.
   (ii) Unexpired insurance Rs 200 had not been taken into account, while preparing Profit and Loss Account.
   (iii) A sale of goods to Raja Ram for Rs 2,500 was passed through the Purchases Book.
   (iv) Goods returned by Mani Ram Rs 1,200 were entered in the Returns Outword Book.

7. Give rectifying journal entries for the following errors
   (i) A Purchase of goods from A amounting to Rs 2,500 has been wrongly passed through the Sales Book.
   (ii) Rs 1,500 paid for furniture purchased has been charged to Ordinary Purchases Account.
   (iii) A cheque for Rs. 150 received from Ram Swaroop was dishonoured and has been posted to the debit of Sales Returns A/c.
   (iv) An amount of Rs 400 due from Mahesh Chand which had been written off as a bad debt was unexpetedly recovered and has been posted to the Personal A/c of Mahesh Chand.

8. Rectify the following errors
   (i) Rent paid to Ram Lal worth Rs 500 was debited to his personal account.
   (ii) Goods valued at Rs 75 were purchased, received and taken into stock, but were not recorded in the books.
   (iii) Interest accured on investment Rs 37 not recorded in the books.
   (iv) The sales book for the month of March was undercast by Rs 3,000.

9. Rectify the following errors
   (i) Payment of rent of proprietors residence amounting to Rs 2,000 was debited to Rent Account.
   (ii) Returns outword book was overcost by Rs 100.
   (iii) Bills payable book was overcost by Rs 150.
   (iv) Sales book cost short by Rs 250.

10. Pass the journal entries to rectify the following errors
   (i) Rs 450 received from Renu & Co. was posted to the debit of their account.
   (ii) Discount Rs 100 received was posted to the debit of Discount A/c
   (iii) Sales book carried forward Rs. 32 instead of Rs 23.
   (iv) Wages paid Rs 2,550 were recorded in the cash book as Rs 2,505.

11. Rectify the following errors
   (i) Payment of Trade Expenses, Rs 55 not posted.
   (ii) Discount column on the receipt side of Cash Book totalling Rs 123 has been added up to show Rs 143.
   (iii) Rs. 50 received from Show and Co. have been credited to Sen & Co.
   (iv) A credit purchase of goods from Suraj of Rs 750 has been wrongly entered in Sales Book.

12. A book keeper failed to balance his trial balance, the credit side exceeding the debit side by Rs 175 . This amount was entered in a suspense A/c, later the following errors were discovered.
   (i) The total of the credit side of Rameshs account was overcost by Rs 100.
   (ii) The sales book was undercost by Rs 100.
   (iii) Goods worth Rs 100 purchased from Chandra were wrongly entered in the sales book. The A/c of Chandra was correctly credited.
   (iv) The total of returns outword book amounting to Rs 200 was not posted to the ledger.
   (v) A credit balance of Rs 755 of Rent Receivable A/c was shown as Rs. 570

(Ans. Total of Suspense A/c Rs. 660)

13. The accountant of Elixir Emporium could not agree the trial balance of his concern as at March 31, 2005. The credit excess of Rs 14,400 was placed to Suspense Account. By April 30, 2005, the following errors had been noticed and rectifying journal entries required.

(i) There was a totalling error in the credit side of bank column of Cash Book. The total disclosed was Rs 38,000 as against the correct total of Rs. 36,000.
(ii) On posting in the sales account from the sales day book of Rs. 13,000 had been entered as Rs 23,000.
(iii) On posting in the sales account from the sales day book of Rs. 13,000 had been entered as Rs. 23,000.
(iv) Rs. 1,300 being repair to buildings had been wrongly credited to Building A/c.
(v) Rs. 200 being miscellaneous income received was omitted to be posted in the ledger.

(Ans. Total of Suspense A/c – Rs. 14,600)

14. The trial balance of a book-keeper shows an excess of debits over credits by Rs. 261.00. This difference is placed in a Suspense a/c to facilitate closing of the books. Later on the following errors were discovered .

(i) A credit item of Rs 349 has been debited to a Personal A/c as Rs 439.
(ii) A sum of Rs 625 written off as fixtures depreciation has not been posted to Depreciation A/c.
(iii) Rs. 9,000 paid for furniture have been charged to the Purchases Account.
(iv) A discount allowed to a customer has been credited to him as Rs. 145 in place of Rs. 154.
(v) A sale of Rs 594 was posted as Rs. 495 in the Sales A/c.
(vi) The total of Returns Inword Book has been added Rs 10 short.

(Ans. : Total of Suspense A/c Rs. 896)

15. There was a difference of Rs 725 in a Trial Balance. It has been transferred to credit side of Suspense A/c later on following errors were found.

(i) An amount of Rs. 375 has been posted to the debit side of Commissionr Account instead of Rs. 275.
(ii) Goods of Rs 200 purchased from Krishan Kumar have been posted to his account as Rs. 250.
(iii) Total of Sales Returns Books was overcost by Rs. 475.
(iv) A credit amount of Rs 50 was posted as Rs 150 to the debit side of a personal account.
(v) Goods of Rs 300 were sold to Shyam, but it was recorded in Purchase Book.

(Ans. : Total of Suspense A/c Rs 775)

16. The books of Ram Kumar could not be tallied. The accountant transferred the difference of Rs. 1270 in the Suspense Account on the debit side. The following mistakes were found later on. Rectify these errors by Passing Journal entries and prepare suspense account.

(i) The Purchase of Rs 400 from Kiran was entered into Sales Book but Kirans Personal account was rightly credited.
(ii) The sales of old furniture of Rs. 540 was credited to sales account as Rs. 450
(iii) The sales of Rs. 430 to Ravinder was credited in his account as Rs 340.
(iv) Goods worth Rs. 100 were taken by the proprietor which was not recorded.
(v) The sales of Rs. 296 to Rakesh was entered in the Sales Book at Rs. 269.
(vi) Sales Return Book balance of Rs. 210 was not included in the A/c.

17. Give Journal entries to rectify the following errors.

(i) A B/R for Rs 1000 received from Nazish was dishnoured has been posted to the debit of sales return account.
(ii) A sum of Rs. 400 owned by Kamal has been included in the list of creditors.
(iii) An item of Rs. 100 written off as bad debts from Nazia has not been debited to bad debt account.
(iv) Wages paid for the construction of fixtures were debited to wages account Rs. 8,000.
(v) Rs. 5,000 paid to Shayasta & Co. for the purchase of furniture last month were debited to Furntiure A/c.
(vi) The purchase of Rs. 250 from Rehman was entered in the Sales Book.
(vii) A credit item of Rs. 698 has been debited to a personal account as Rs. 878.
(viii) A discount allowed to a customer has been credited to him as Rs. 136 instead of Rs. 154.

CHAPTER 6

End of Period Accounts Sole Trader

Learning Objectives

After studying this chapter you will be able to

- understand the meaning of End of Period Accounts i.e. Trading and Profit and Loss Account and Balance Sheet
- appreciate the objectives of preparing end of period accounts
- Explain the meaning of gross profit / gross loss, net profit / net loss, direct expenses etc.
- Prepare trading and profit and loss account and balance sheet without adjustments
- Understand the treatment of outstanding expenses, incomes accrued, depreciation, provision for bad and doubtful debts, closing stock etc. while preparing end of the period accounts
- Explain the advantages of end of period accounts
- Explain the limitations from which the end of period accounts suffer.

Money is invested in a business with the primary aim of earning profits. For knowing this, it is necessary that the accountant must measure and accumulate accounting data in such a manner that the amount of profit earned or loss suffered by the business may be determined and reported. The profit figure is needed for income tax requirements and for chalking out expansion plans. For the purpose of determining the profit or loss figure, a statement known as trading and profit and loss account (or income statement), is prepared at the end of the year which includes all items of expenses and losses, and all revenues and gains occurring during the accounting period. This account or income statement is divided into two parts - first part is called trading account. This part is prepared to find out gross profit or gross loss. Gross profit is the difference between the net sales and cost of goods sold. In other words, gross profit/gross loss is the result of buying and selling of goods during trading period. The second part is called profit and loss account and shows the final figure of net profit or net loss. Another statement, balance sheet (or position statement), is also prepared with an aim to know the exact financial position of the business on the last date of the accounting period. The balance sheet shows the financial position of the business in the form of its assets and liabilities. It is divided into two parts when prepared in a T form. On the left hand side liabilities are shown and on the right hand side assets are shown.

These two statements, Trading and profit and loss account and balance sheet, are known as Financial Statements. They are also called Final Account because they are end of the period statements, or the end product of the financial accounting process. Both these statements are prepared from the balances appearing in the trial balance.

6.1 Preparation of End of the Period Statements

End of the period statements, i.e. trading and profit and loss account and balance sheet, are prepared from the balances appearing in the trial balance at the end of an accounting period. It means that trial balance becomes the basis for the preparation of these statements.

In order to decide the place where the particular balance should be taken, from the trial balance to end of the period statements, the following rules may be allowed.

- **Items from the debit column of the trial balance :** Balances appearing in the debit column of the trial balance may be items of expenses, or losses, or assets. If the debit balance of an item represents an asset like land, building, plant and machinery, debtors, bills receivables, investments, cash at bank, cash in hand etc, then it is shown on the asset side of the balance sheet. As discussed in Chapter I, assets are the properties or possessions of the business which are acquired for use in the business and not for the purpose of resale. The benefits from assets are obtained for more than one year. If the balance of an account is an expense then it will be shown on the debit side of the trading account, or on the debit side of the profit and loss account as the case may be. You also learnt in Chapter I that expenses are the items of expenditure whose benefits are availed by the business immediately or during the same accounting year. The expenses are purchases, wages, carriage, cartage, commission, discount, salary, stationery, postage, advertisement etc.

- **Items from the credit column of the trial balance :** The balances that are shown in the credit column of the trial balance are the items of liabilities, or incomes and gains. If these are liabilities there they are shown on the liability side of the balance sheet. In Chapter I you have learnt that liabilities are the obligations of the business which it has to discharge, e.g., capital, loans, creditors, bills payable, outstanding expenses, bank overdraft etc. The credit balances in the trial balance may also be items of incomes or gains; such balances are shown in the trading and profit and loss account. Items of incomes and gains are sales, discount received, commission received, rent received etc.

- **Preparation of trading account :** As discussed earlier, profit and loss account is divided into two parts. The first part is called the trading account and the second part is called the profit and loss account. Trading account is prepared to find out the gross profit earned or gross loss incurred by the business enterprise during the accounting period. Gross profit is the difference between sales and cost of goods sold. The figures of sales made by the business during the accounting period are available in the sales account in the ledger. Cost of goods sold represents the cost price of that merchandise which was sold during the accounting period out of the total merchandise which was available for sale. This means that adjustments for opening and closing stock have to be made in the amount of cost of goods / merchandise available for sale to arrive at the figure of cost of goods sold. It can be understood easily with the help of the following formula.

  Cost of goods sold = Opening stock + Net purchase + Direct expenses - Closing stock.

  Opening stock is the cost price of the goods which were accounted for from the previous year. Net purchases are total purchases (cash purchases + credit purchases) less purchase returned which can be made available from the purchases account and purchases return account in the ledger. Direct expenses are all such expenses which may have to be incurred by the business for bringing the goods or services in a saleable position. Examples of direct expenses are carriage inwards, cartage, freight, wages, customs duties, dock charges, Collieage, fuel, power etc. Therefore, when from net sales, cost of goods sold is subtracted the balance is gross profit. It can be shown in the form of an equation as follows:

  Gross Profit = Net sales - Cost of goods sold

When the amount of cost of goods sold is more than the figure of net sales the balance will be gross loss.

ILLUSTRATION 1 : From the following information, calculate gross profit.

Gross Sales	Rs 80,000
Sales Return	Rs 10,000
Purchase	Rs 25,000
Wages	Rs 5,000
Fuel & Power	Rs 3,000
Opening Stock	Rs 7,000
Closing Stock	Rs 2,500

Solution :

(i)	Cost of goods sold	=	Opening stock + Net purchases + Direct expenses - Closing stock
		=	Rs 7,000 + Rs 25,000 + (Rs. 5,000 +3,000) - Rs 2,500
		=	Rs 37,500
(ii)	Net sales	=	Gross sales - Sales return
	Or	=	Cash Sales + Credit sales - Sales return
		=	Rs 80,000 - Rs. 10,000
		=	Rs 70,000
(iii)	Gross profit	=	Net sales - Cost of goods sold
		=	Rs 70,000 - Rs 37,500
		=	Rs 32,500

Illustration 2: From the following balance obtained from the trial balance of Ajay for the year ended 31.12.2006, calculate the amount of gross profit earned by him during the year ended 31.12.2006.

	Rs.
Opening stock	80,000
Cash purchases	10,00,000
Credit purchases	12,00,000
Purchases returns	10,000
Cartage	5,000
Closing stock	1,15,000
Cash sales	17,00,000
Credit sales	10,00,000
Sales returns	8,000

Solution: Calculation of Gross Profit

		Rs		Rs
Cash sales		17,00,000		
Add credit sales		10,00,000		
Total sales		27,00,000		
Less sales returns		8,000		
Net sales	(A)			26,92,000
Opening stock		80,000		
Cash purchases		10,00,000		
Credit purchases		12,00,000		
Total purchases		22,00,000		
Less purchase returns		10,000		
Net purchases			21,90,000	
Cartage			5,000	
Cost of goods available for sales			21,95,000	
Less closing stock			1,15,000	
Cost of goods sold	(B)			21,60,000
Gross profit	(A - B)			5,32,000

Alternatively,

Gross profit = Net sales - Cost of goods sold

Net sales= Total sales - Sales returns

Total sales = Cash sales + Credit sales

= Rs. 17,00,000 + Rs. 10,00,000 = Rs. 27,00,000

Net Sales = Rs. 27,00,000 - Rs. 8,000= Rs. 26,92,000

Cost of goods sold = Opening stock + Net purchases + Direct expenses - Closing stock

Net Purchases = Total purchases - Purchases returns

Total Purchases = Cash purchases + Credit purchases

= 10,00,000 + 12,00,000

= Rs. 22,00,000

Net Purchases = 22,00,000 - 10,000

= Rs. 21,90,000

Cost of goods sold = 80,000 + 21,90,000 + 5,000 - 1,15,000

= Rs. 21,60,000

Gross profit = 26,92,000 - 21,60,000

= Rs. 5,32,000

Illustration 3. Calculate the gross profit and its percentage on sales from the following details.

Opening stock	Rs 8,000	factory expenses	Rs 2,000
Purchases	Rs 2,000	Sales	Rs 84,000
Purchase return	Rs 4,000	Closing stock Rs 5,000	
Wages	Rs 7,000	Sales return	Rs 9,000

Solution

i) Net sales = Sales - Sales return

= Rs 84,000 - Rs 9,000

= Rs 75,000

ii) Cost of goods sold = Opening Stock + Net purchases + Direct exp. - Closing stock

= Rs 8,000 + (Rs 32,000 - Rs 4,000) + (Rs 7,000 + Rs 12,000) - Rs 5,000.

= Rs 8,000 + Rs 28,000 + Rs 19,000 - Rs 5,000

= Rs 50,000

iii) Gross profit = Net sales - Cost of goods sold

= Rs 75,000 - Rs. 50,000

= Rs 25,000

iv) Gross Profit on sales = $\frac{\text{Gross profit}}{\text{Net sale}} \times 100$

$= \frac{\text{Rs } 25{,}000}{\text{Rs } 75{,}000} \times 100 = \frac{100}{3}$

$= 33\frac{1}{3}\%$

Illustration 4: From the following balances extracted from the trial balance of Sohan Singh, calculate gross loss incurred by him for the year ended 31.3.3007.

Opening stock	Rs 87,000	Credit purchases	Rs 4,00,000
Cash sales	Rs 5,30,000	Purchases returns	Rs 5000
Credit sales	Rs 6,40,000	Wages	Rs 7,000
Sales returns	Rs 20,600	Cartage	Rs 8000
Cash purchases	Rs 7,00,000	Closing Stock	Rs 50,000

Solution

Total sales	=	Cash sales + Credit sales
	=	Rs 5,30,000 + Rs 6,40,000
	=	Rs 11,70,000
Net sales	=	Total sales - Sales returns
	=	Rs 11,70,000 - Rs 20,600
	=	Rs 11,49,400
Total purchases	=	Cash purchases + Credit purchases
	=	Rs 7,00,000 + Rs 4,00,000
	=	Rs 11,00,000
Net purchases	=	Total purchases - Purchases returns
	=	Rs 11,00,000 - Rs 5,000
	=	Rs 10,95,000
Direct expenses	=	Wages + Cartage
	=	Rs 8,000 + Rs 7,000
	=	Rs 15,000
Cost of goods sold	=	opening stock+ Net purchases + Direct expenses - Closing stock
	=	Rs 87,000 + Rs 10,95,000 + Rs 15,000 - Rs 10,000
	=	Rs 11,47,000
Gross loss	=	Cost of goods sold - Net sales
	=	Rs 11,57,000 - Rs 11,49,400
	=	Rs 7,600

Illustration 5. From the following information calculate the gross profit on cost and on sales.

Opening stock	Rs 6,000	wages	Rs 9,000
Cash purchases	Rs 28,000	Freight	Rs 6,000
Credit purchases	Rs 40,000	Fuel & power	Rs 4,000
Purchase return	Rs 5000	Closing stock	Rs 8000
Sales return	Rs 7,000		

Solution :

i)	Net purchases	=	Cash purchases + Credit purchases - Purchase return
		=	Rs 28,000 + Rs 40,000 - Rs 5,000
		=	Rs 68,000 - Rs 5,000
		=	Rs 63,000

ii)	Net sales	=	Cash sales + Credit sales - Sales return
		=	Rs 40,000 + Rs 67,000 - Rs 7,000
		=	Rs 1,07,000 - Rs 7,000
		=	Rs 1,00,000
iii)	Direct expenses	=	Wages + Freight + Fuel & Power
		=	Rs 9,000 + Rs 6,000 + Rs 4,000
		=	Rs 19,000
iv)	Cost of goods sold	=	Opening stock + Net purchases + Direct expenses - Closing stock
		=	Rs 6,000 + Rs 63,000 + Rs 19,000 - Rs 8,000
		=	Rs 80,000
v)	Gross profit	=	Net sales - Cost of goods sold.
		=	Rs 1,00,000 - Rs 80,000
		=	Rs 20,000
vi)	Gross profit on cost	=	$\frac{\text{Gross profit}}{\text{Cost of goods sold}} \times 100$
		=	$\frac{20,000}{80,000} \times 100$
		=	25%
vii)	Gross profit on sales	=	$\frac{\text{Gross profit}}{\text{Net sales}} \times 100$
		=	$\frac{20,000}{1,00,000} \times 100$
		=	20%

Illustration 6. Gross profit on sales is 20%. Net Sales is Rs. 80,000. Find gross profit & cost of goods sold.

Solution :

i)	Given, gross profit on Sales	=	20%
	Net Sales	=	Rs 80,000
	Gross profit	=	$\frac{\text{Net sales} \times \%\ \text{Profit}}{100}$
		=	$\frac{80,000 \times 20}{100}$ = Rs. 16,000
ii)	Cost of goods sold	=	Net sales - Gross profit
		=	Rs 80,000 - Rs.16,000
		=	Rs 64,000

Illustration 7. Calculate Gross Profit and Sales from the following data :

Cost of goods sold Rs 60,000. Gross profit on Sales = 25%.

Solution :

Given, cost of goods sold = Rs. 60,000, G.P. on sales = 25%.

Let Sales	=	Rs. 100
Gross profit on sales	=	25%
Cost of goods sold	=	Rs 100 - Rs 25 = Rs 75
If cost is Rs 75, the sales	=	Rs 100
If cost is Re 1, the sales	=	$\frac{100}{75}$
If cost is Rs 60,000, the sales	=	$\frac{100 \times 60,000}{75}$
	=	Rs 80,000
Gross profit	=	Net sales - Cost of goods sold
	=	Rs 80,000 - Rs 60,000
	=	Rs. 20,000

6.2 Advantages of Preparing a Trading Account

Following are the advantages of preparing a trading account.

(i) It helps in ascertaining the gross profit earned or gross loss suffered by the business as a result of its buying and selling activities.

(ii) Comparison of the figures of purchases, sales, direct expenses, opening stock, closing stock of the current year with that of the previous year helps in identifying the causes of such changes with a view to locate weak and strong areas of the trading activities of the business.

(iii) By calculating the ratio of gross profit to net sales, called the gross profit ratio, the extent to which the anticipated or planned results with respect to gross profit have been achieved can be ascertained.

(iv) It helps in exercising effective control over direct expenses and stock by comparing the figures of the current year with the figures of the previous year. If there are wide fluctuations in the figures of opening and closing stock then the same may be investigated and action taken.

(v) A close monitoring of the items of stock may also help in detecting the theft of goods in the enterprise.

The different items used for the calculation of gross profit can also be put in a 'T' shaped account and this account will be called trading account. The proforma of a trading account is given below.

Trading Account of ……………..(Business Name) for the year ended……….

Dr. Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening Stock	…………………	By sales	…………………
To Purchases……….	…………………	Less Returns………….	…………………
Less Returns………….	…………………	By Closing Stock	…………………
To Direct Expenses	…………………	By Gross Loss transferred to	…………………
To Gross Profit transferred to	…………………	Profit & Loss A/C	…………………
Profit and Loss A/c	…………………		
	…………………		…………………

As discussed earlier, direct expenses are those expenses which are incurred by the business in bringing the goods in a saleable condition. The examples of such expenses are wages and salaries, cartage, carriage or carriage inwards, freight, customs duty, dock charges, collieage etc. These items are shown on the debit side of the trading account individually as per their balances given in the trial balance. Gross profit is the balancing figure i.e. the difference between the totals of credit side and debit side. If the debit side is more than the credit side than the balancing amount will be gross loss. The amount of gross profit / gross loss is transferred to profit and loss account for ascertaining net profit / net loss.

Illustration 8: Prepare trading account of Sh. S. Dhawan for the year ending 31 March, 2007 from the following information:

	Rs
Purchases	13,00,000
Sales	15,00,000
Stock (April 1, 2006)	40,000
Wages	30,000
Carriage inwards	14,000
Returns outwards	3,000
Returns inwards	2,500
Freight	15,000
Additional information:	
Stock on 31 March, 2007 was	
	Rs. 1,70,000

Solution

Sh. S. Dhawan

TRADING ACCOUNT FOR THE YEAR ENDING MARCH 31,2007

Dr. Cr.

Particulars		Amount Rs.	Particulars		Amount Rs.
To Stock - opening		40,000	By Sales	15,00,000	
To Purchases	13,00,000		Less Sales Returns	2,500	
Less Returns	3,000	12,97,000			14,97,500
To Wages		30,000			
To Carriage Inwards		14,000	By Closing Stock		42,000
To Freight inwards		15,000			
To Gross Profit c/d (transferred to Profit and Loss A/c)		1,43,500			
		15,39,500			15,39,500

Profit and Loss Account

Profit and loss account is prepared to ascertain net profit earned or net loss incurred by the business during the accounting period. It is prepared in the same way in which trading account is prepared. After the gross profit / gross loss from the trading account, the remaining expenses and losses (other than the direct expenses) whose balances are shown in the trial balance are debited to the profit and loss account. Similarly the items of incomes and gains (other than sales) whose balances are shown in the trial balance are credited to the profit and loss account. The difference between the totals of the credit side and debit side is done to ascertain net profit or net loss. If the credit side is more than the debit side than the difference is net profit. On the other hand if the debit side is more than the credit side than the difference is net loss. The net profit or net loss is the result of all the activities of the business during the accounting period and is transferred to the capital account. Since it is the owners, share in the business, with net profit, the capital of the sole trader increases and with net loss the capital of the owner decreases. The proforma of the profit and loss account is as follow.

PROFIT AND LOSS ACCOUNT OF ....(NAME OF BUSINESS) for the year ending............

Dr Cr

Particulars	Amount Rs.	Particulars	Amount Rs.
To gross loss		By gross profit	
To salaries and wages		By cash discounts received	
To rent, rates & taxes		By bad debts recovered	
To lighting & insurance		By income from investments	
To printing & stationery		By commission received	
To postage, telegrams		By interest received	
To legal expenses		By gain on sale of fixed assets	
To trade expenses		By net loss (transferred to	
To audit fees		Capital Account)	
To car upkeep expenses			
To telephone expenses			
To general expenses			
To discounts allowed			
To Interest on loans			
To discount or rebate on bills of exchange			
To bad debts			
To selling & distribution expenses			
To packing of finished goods			
To store charges			
To carriage, freight, cartage outwards			
To cost of samples, catalogue expenses			
To commission			
To advertising expenses			
To depreciation on fixed assets			
To loss on sale of fixed assets			
To net profit (transferred to capital account)			

Illustration 9: Prepare Trading and Profit and Loss Account of Sh. Ram Prakash for the year ending 31 March, 2007 from the following figures taken from his trial balance.

	Rs
Stock as on April, 2006	1,50,000
Sales	12,89,600
Sales returns	9,600

Purchases	12,43,000
Purchases returns	3,000
Freight inwards	4,000
Carriage outwards	6,000
Salaries	30,000
Bank interest	2,000
Printing and stationery	7,000
Discount received	900
Discount allowed	1,600
Audit fees	3,000
Insurance premium	2,600
Trade expenses	2,500
Stock on 31 March, 2007 was	Rs 1,70,000

Solution

Sh. Ram Prakash

TRADING AND PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDING MARCH 31,2007

Dr Cr

Particulars		Amount Rs.	Particulars		Amount Rs.
To stock- opening		1,50,000	By sales	12,89,600	
To purchases	12,43,000		Less sales returns	9,600	
Less returns	3,000	12,40,000			12,80,000
To freight inwards		4,000	By stock- closing		1,70,000
To gross profit		56,000			
(transferred to P & L A/c)		14,50,000			14,50,000
To salaries		30,000	By gross profit b/d		56,00
To bank interest		2,000	By discount		900
To carriage outwards		6,000			
To printing and stationery		7,000			
To discount		1,600			
To audit fees		3,000			
To insurance premium		2,600			
To trade expenses		2,500			
To net profit		2,200			
(transferred to Capital A/c)		56,900			56,900

6.3 Balance Sheet

It is a statement showing the position of the assets and liabilities of the business on the last day of the accounting year or on the date on which it is prepared. A balance sheet depicts the financial position of the business. You have already learned about the preparation of Trading and Profit and Loss Account. It is once again recalled that from the trial balance the business of all the nominal accounts, i.e. accounts representing expenses and losses and incomes and gains, are transferred to the trading and profit and loss account to ascertain gross profit and net profit respectively. The remaining accounts in the trial balance are the accounts of assets and liabilities. The accounts having debit balances are the accounts of assets and the accounts having credit balances are the accounts of liabilities. These balances of assets and liabilities are shown in the balance sheet. These are balances of real and personal accounts and are grouped as assets and liabilities. They are arranged in a proper way in the form of a statement which is called a balance sheet or a position statement. When balance sheet is represented in a 'T' from, assets are shown on the right hand side and liabilities are shown on the left hand side.

6.4.1 Marshaling of Balance Sheet

The arrangement of the different items of assets and liabilities in a balance sheet is called marshaling of balance sheet. This can be done in two ways

(i) In order of liquidity
(ii) In order of permanence

In Order of Liquidity

Under this method, the assets in the balance sheet are arranged in order of liquidity which they can be, converted into cash. In other words, first current assets in order of liquidity are arranged followed by fixed assets, i.e assets which are most liquid are shown first followed by less liquid assets. Similarly, liabilities are also arranged in order of liquidity, i.e current liabilities are first followed by less liquid current liabilities followed by fixed liabilities. Following is the profoma of a Sole trader's balance sheet in order of liquidity.

BALANCE SHEET as on 31 March, 200___.

Liabilities	Rs	Assets	Rs.
Current Liabilities		**Current Assessts**	
Creditors		Cash in hand	
Bills payable		Cash at bank	
Bank overdraft		Stock-in-trade	
Outstanding expenses		Debtors	
Income received in advance		Bills receivable	
Fixed Liabilities		Prepaid expenses	
Loan		**Investments** (give details)	
Mortgage		**Fixed Assets**	
Capital		Furniture and Fixtures	
		Plant and machinery	
		Building	
		Land	
		Goodwill	

Order of permanence

When the assets and liabilities in the balance sheet are arranged in order of permanence in the fixed items, then the marshalling of the balance sheet is said to have been done in order of permanence. It means when the order is reversed as is followed for the presentation of assets and liabilities in order of liquidity then it will become marshalling of the items of balance sheet in order of permanence. Given below is the performa for the presentation of items in a balance sheet in order of permanence.

BALANCE SHEET as on 31 March, 200___.

Liabilities	Rs	Assets	Rs
Capital		**Fixed Assets**	
Fixed Liabilities		Goodwill	
Loan		Land	
Mortgage		Building	
Current Liabilities		Plant and machinery	
Income received in advance		Furniture and fixtures	
Outstanding expenses		Investments	
Bank overdraft		**Current Assets**	
Bills payable		Prepaid expenses	
Creditors		Bills receivable	
		Debtors	
		Stock-in-trade	
		Cash at bank	
		Cash in hand	

6.5 Closing Entries

While preparing trading and profit and loss account we discussed that all the nominal accounts are transferred to the trading and profit and loss account in order to calculate gross profit and net profit respectively. The recorded entries with the help of which the nominal accounts are closed for transferring their balances to the trading and profit and loss account are called closing entries. Thus, closing entries are entries recorded for the purpose of closing the nominal account's i.e. accounts of expenses and loss and incomes and gains for ascertaining gross profit and net profit. Simple rule for recording a closing entry is that the accounts of expenses and losses which have debit balances are closed by transferring their balance to the debit of Trading and Profit and Loss Accounts if incomes and given which have credit balances are closed by transferring their balances to the credit of Trading and Profit and Loss Account. Such entries have been given below.

(i) For Closing accounts of expenses and losses which always show debit balance

Trading & Profit & Loss A/c ………… Dr.
To Individual Direct Expenses A/c

(ii) For closing accounts of incomes and gains which have credit balances

Individual Income & Gains A/c .... Dr.
To Trading and Profit and Loss A/c

(iii) The opening stock, purchase account, wages accounts, carriage accounts and Sales Return A/c etc. will be closed by passing the following closing entry.

Trading Account ………….. Dr
To Opening Stock
To Purchase A/c
To wages A/c
To Carriage A/c
To Sales Returns A/c

(iv) Similarly the closing entries for Sales and Purchases Returns and closing stock will be as follows :-

Sales A/c …………….….... Dr
Purchases Returns A/c .... Dr
Closing Stock A/c ………….. Dr
To Trading A/c

(v) Also, the closing entries for the items of expenses and losses to be debited to Profit and Loss Account will be as follows

Profit and Loss A/c ………... Dr.
To Individual Indirect Expenses A/c

Closing entries for the item of incomes and gains related to Profit and Loss A/c will be as follows

Income and Gains A/c (individually) ……….. Dr
To Profit & Loss A/c

Illustration 10 : On the basis of balances obtained from the ledger of Sh. Pyare Lal for the year ended 31March 2007, pass the necessary closing entries for the preparation of end of the period accounts and prepare his Trading and Profit & Loss A/c and balance sheet as on above date.

	Rs.
Proprietor's Capital Account	1,19,400
Proprietor's Drawings Account	10,550
Bills Receivable	9,500
Plant and Machinery	28,800
Wages	40,970
Salaries	11,000
Sundry Debtors	62,000
Sundry Creditors	59,630
Loan (Credit)	20,000
Return Inward	2,780
Purchases	2,56,590
Sales	3,56,430
Commission Received	5,640
Discount Allowed	5,870
Rent & Taxes	5,620
Stock on 1st April, 2006	89,680
Travelling Expenses	1,880
Insurance	400
Cash	530
Bank	18,970
Repairs	3,370
Bad Debts	3,620
Fixture and Fittings	8,970

Additional Information :
Closing Stock Rs 1,28,960

Solution :

M/S PYARE LAL
CLOSING ENTRIES

	Particulars		**Dr Amount Rs**	**Cr Amount Rs**
1	Trading Account	Dr	3,87,240	
	To Stock (Opening)			89,680
	To Purchase			2,56,590
	To Wages			40,970
	(Being the transfer of debit balances to trading account)			
2	Sales less returns	Dr	5,53,650	
	Stock (end)	Dr	1,28,960	
	To Trading account			
	(Being the transfer of debit balances to trading account)			4,82,610
3.	Trading Account	Dr	95,370	
	To Profit and loss account			95,370
	(Being the transfer of gross profit to Profit and Loss account)			

4.	Profit and Loss Account Dr To Salaries To Discounts To Rent and Taxes To Travelling Expenses To Insurance To Repairs & Renewals To Bad Debts (Being the transfer of debit balances to Profit and Loss account)	31,769	 11,000 5,870 5,620 1,880 400 3,370 3,620
5.	Commission Dr To Profit and Loss Account (Being the transfer of credit balance of commission to Profit and loss account)	5,640	 5,640
6.	Profit and Loss Account Dr To Capital Account (Being the transfer of net profit to capital account of proprietor)	69,250	 69,250
7.	Capital Account Dr To Drawings (Being the transfer of proprietors drawings account to capital account)	10,550	 10,550

M/s Pyare Lal

Trial Balance for the year ending 31 March, 2007

Name of the Account	Debit Balances Rs	Credit Balances Rs
Proprietor's Capital Account		1,19,400
Proprietor's Drawings Account	10,550	
Bills Receivable	9,500	
Plant and Machinery	28,800	
Wages	40,970	
Salaries	11,000	
Sundry Debtors	62,000	
Sundry Creditors		59,630
Loan (Received)		20,000
Returns Inward	2,780	
Purchases	2,56,590	
Sales		3,56,430
Commission Received		5,640
Discount Allowed	5,870	
Rent and Taxes	5,620	
Stock, 1 April 1996	89,680	
Travelling Expenses	1,880	

Insurance	400	
Cash	530	
Bank	18,970	
Repairs and renewals	3,370	
Bad Debts	3,620	
Fixtures & Fittings	8,970	
	5,61,100	**5,61,100**

M/s Pyare Lal

Trading Account

for the year ending 31 March, 2007

Particulars	**Amount Rs.**	**Particulars**	**Amount Rs.**
To Stock-opening	89,680	By Sales 3,56,430	
To Purchases	2,56,590	Less : Returns-inward 2,780	3,53,650
To Wages	40,970	By Stock-Closing	1,28,960
To Gross Profit c/d	95,370		
(transferred to Profit and Loss A/c			
	4,82,610		4,82,610

M/s Pyare Lal

Profit & Loss A/c

for the year ending 31st March, 2007

Particulars	**Amount Rs.**	**Particulars**	**Amount Rs.**
To Salaries	11,000	By Gross Profit b/d	95,370
To Discount	5,870	By Commission	5,640
To Rent and Taxes	5,620		
To Travelling Expenses	1,880		
To Insurance	400		
To Repairs & Renewals	3,370		
To Bad Debts	3,620		
To Net Profit			
(transferred to Capital A/c)	69,250		
	1,01,010		1,01,010

M/s Pyare Lal

Balance Sheet

for the year ending 31 March, 2007

Liabilities		**Rs.**	**Assets**	**Rs.**
Currrent Liabilities :			Current Assets	
Sundry Creditors		59,630	Cash in Hand	530
Fixed Liabilities			Cash at Bank	18,970
Loan		20,000	Bills Receivable	9,500
Capital	1,19,400		Sundry Debtors	62,000
Add Net Profit	69,250		Stock	1,28,960
	1,88,650		Fixed Assets	
Less Drawings	10,550	1,78,100	Plant & Machinery	28,800
			Fixture & Fittings	8,970
		2,57,730		2,57,730

6.6 Adjustment Entries

The Trading and Profit and Loss Account is prepared on the basis of the matching principle, i.e incomes of the year must be mentioned with the expenses of the year. It means in the trading and profit and loss account all expenses only of the current year are debited and all incomes only of the current year are credited to arrive at the figures of gross profit and net profit. This means that if any item of expenses or income is not included in the amount of trial balance which is specific to the current year, i.e the year whose Trading and Profit & loss Account is being prepared, such figure is added to the related expenses or income. Similarly, any item of expense or income includes a figure which does not relate to the current year that figure is deducted from the related expenses or income so as to arrive at the actual amount of incomes or expenses pertaining to the current year. Thus, for making these changes in this figure given in the trial balance, some journal entries are passed which are called adjustment entries. In the absence of adjustment entries the profit or loss shown by the trading & profit and loss account will be misleading because in some cases expenses and incomes will be overstated and in other cases those will be understated. Therefore, adjustment entries are those entries that are passed at the end of the accounting period for the purpose of adjusting various nominal and other accounts so that the gross profit / gross loss, net profit / net loss is indicated in the Trading and Profit and loss Account and also the Balance sheet represents a true and fair view of the financial position of the business.

Following are the common adjustments that are made while preparing end of period accounts.

(i) Closing Stock
(ii) Expenses outstanding
(iii) Expenses paid in advance
(iv) Incomes accrued
(v) Income received in advance Depreciation
(vi) Depreciations
(vii) Bad Debts
(viii) Provision for bad debts

Each of these has been discussed below.

Closing Stock : Closing stock is shown below the trial balance as an adjustment. The following adjustment journal entry is made for closing stock.

Closing Stock A/c .... Dr
To Trading A/c

Closing stock is shown in the Balance sheet and is carried forward to the next year. At the end of the next year, it appears in the trial balance as opening stock and from there it is transferred to the debit of trading account by passing a closing entry. Therefore, stock account is opened always at the end of the accounting period and remains as such throughout the next year at the end of which it is closed.

Expenses outstanding : Some expenses may remain unpaid on the date of preparing the end of period accounts. Such expenses are called outstanding expenses and they include salaries, rent, interest etc. Such items are both expenses and liabilities. The adjustment regarding the outstanding expenses is made by passing the following journal entry.

Expenses A/c (individually) ……… Dr
To outstanding Expenses A/c

The amount of outstanding expenses is also shown in the balance sheet as a liability.

Expenses paid in advance : It is customary to make payment of some of the expenses like Insurance premium, rent of the shop etc. in advance. If the payments for services are not fully used on the date of preparation of the end of the period. Accounts these unused parts of the service in terms of money are recorded by passing the following journal entry.

a) When expense is paid in advance.

Prepaid Expenses (individually) A/c …… Dr.
To Cash A/c

b) When the services of the prepaid expenses is used.

Expense A/c ....Dr.
To Pre-paid Expense A/c

Prepaid expenses are assets and. Are shown on the asset side of the Balance sheet.

Incomes Accrued : At times it happens that certain incomes like interest on securities, dividend on shares commission etc. are earned but not received. Such incomes are called as accrued. Incomes i.e incomes earned interest not received. The following adjustment entry is passed for such items

Accrued Income A/c ………….. Dr
To Income Account

Accrued income are assets also and are shown on the asset side of the Balance Sheet.

Income Received in Advance

Sometimes, it happens that certain sum of money is recived in advance but not earned in that period in which it is received such income is called income received in advance or unaccured income which is a liability for the business. The following adjustment entry is passed for such items:

Income Account .... Dr
To Unaccured Income Account

Income received in advance are liabilities and are shown on the liability side of the balance sheet.

Depreciation : Depreciation decreases the value of an asset because of wear and tear, passage of time, or technology becoming obsolete. It is an expense and is adjusted by passing the following adjustment entry:

Depreciation A/c Dr
To Asset A/c

The amount of depreciation is deducted from the value of assets while preparing the Balance sheet and the asset is shown less of depreciation.

Bad Debts : Debts which are irrecoverable are called bad debts. The amount of bad debts which are not shown in the balance of bad debts in the trial balance are adjusted by passing the following forward entry.

Bad Debts A/c ……….. Dr
To Debtors A/c

Provision for bad debts : The purpose of making a provision for bad debts is to bring down the balance of debtors to its true position so that the balance sheet shows the debtors at their accrued reliable value. For example, suppose debts of Rs. 1,00,000 have been incurred. The debtors in this case should be shown at Rs. 95,000. i.e. (Rs. 1,00,000 less provision for bad depts. Rs. 5,000). The following adjustment entry is passed for the same.

P/L A/c .... Dr.
To Provision for Bad Debts

Illustration 11 : Pass necessary adjustment and closing entries for the following adjustment as at 31 March, 2007.

(i) Stock on 31 March, 2007 was Rs. 35,000.
(ii) Salaries at the rate of Rs. 2,000 p.m. were paid for 11 months only.
(iii) Insurance Premium paid Rs. 3,000 up to 30 June 2007
(iv) Interest accrued on securities worth Rs. 5,000.
(v) Depreciation at 5% on office furniture of Rs. 40,000 and at 10% on plant valued at Rs. 1,50,000.
(vi) Bad debts during the year amounted to Rs. 1,000.
(vii) Make provision for doubtful debts on debtors at 5%. As per trial balance, debtors were of Rs. 40,000 and make a provision for discount on Debtors @2%.

Solution :

Adjustment and Closing Entries

	Particulars		LF	Dr. Amount Rs.	Cr. Amount Rs.
(i)	Stock A/c	Dr		35,000	
	To Trading A/c				35,000
	(Being adjustment entry for closing stock)				
(ii)	(a) Salary A/c	Dr		2,000	
	To Salary outstanding A/c				2,000
	(Being adjustment entry for outstanding salary of one month brought into account)				
	(b) Profit and Loss A/c	Dr		2,000	
	To Salary A/c				2,000
	(Being closing entry for transfer of salary account of profit and loss account)				
(iii)	(a) Insurance prepaid A/c	Dr		750	
	To Insurance Premium A/c				750
	(Being adjustment entry for insurance paid in advance for 3 months at the rate of Rs. 3,000 p.a.)				
	(b) P/L A/c	Dr		2,250	
	To Insurance Premium A/c				2,250
	(Being the closing entry for transfer of insurance account)				
iv)	(a) Interest Accrued A/c	Dr		5,000	
	To Interest A/c				5,000
	(Being adjustment entry for accrued interest on securities brought into the account)				

	(b) Interest A/c Dr To Profit and Loss A/c (Being closing entry for transfer of Interest account)		5,000	 5,000
v)	(a) Depreciation A/c Dr To Office Furniture To Plant (Being adjusting entry for depreciation on office furniture and plant)		17,000	 2,000 15,000
	(b) Profit and Loss Account Dr To Depreciation A/c (Being closing entry for transfer of Depreciation A/c to Profit and Loss Account)		17,000	 17,000
vi)	(a) Bad debts A/c Dr To Debtors (Being adjusting entry for recognising bad debts as loss not recoverable from debtors)		1,000	 1,000
	(b) Profit and Loss A/c Dr To Bad debts A/c (Being closing entry for transfer of loss to Profit and Loss Account)		1,000	 1,000
vii)	(a) Profit and Loss Account Dr To Provision for Doubtful Debts A/c (Being adjusting and closing entry for creating provision at 5% on (Rs. 40,000 - Rs. 1,000) i.e., Rs. 39,000]		1,950	 1,950
	(b) Profit and Loss Account Dr To Provision for Discount on Debtors (Being adjusting and closing entry for provision for discount @ 2% on Total Debts Rs. 40,000 Less Bad Debts Rs. 1,000 Remaining Debts Rs. 39,000 Less Doubtful Debts @ 5% on Rs. 39,000 Rs. 1,950 ------------- Good Debts Rs. 37,050 ------------- Discount @ 2% on Rs. 37,050 = Rs. 741)		741	 741

Illustration 12 : From the following balances extracted from the books of Atma Ram on 31 Dec., 1997 prepare trading and profit and loss account after making closing entries.

	Rs.		Rs.
Stock	9,600	Repairs to plant	160
Wages and Salaries	3,200	Cash in hand and at bank	200

Commission on purchases	200	Debtors	4,000
Freight	300	Income tax	550
Purchase less returns	11,850	Drawings	650
Sales Less returns	24,900	Capital	5,000
Trade expenses	20	Bills payable	500
Bills receivable	600	Loan	900
Rent	200	Discount on purchase	400
Plant	2,000	Creditors	2,330
Bad debts	500		

Information : Stock at the end was Rs. 3,500.

Solution :

Closing Entries

	Particulars		LF	Dr. Amount Rs.	Cr. Amount Rs.
(i)	Trading Account	Dr.		25,150	
	To Stock				9,600
	To Wages and salaries				3,200
	To Commission on purchases				200
	To Freight				300
	To Purchases less returns				11,850
	(Being transfer of debit balances to trading account)				
(ii)	Sales	Dr.		24,900	
	Stock at the end	Dr.		3,500	
	To Trading Account				28,400
	(Being transfer of credit balances to trading account)				
(iii)	Trading Account	Dr.		3,250	
	To Profit and Loss A/c				3,250
	(Being transfer of credit balances to trading accout)				
(iv)	Profit and Loss Account.	Dr		880	
	To Trade expenses				20
	To Rent				200
	To Bad debts				500
	To Repairs to plant				160
	(Being transfer of debit balance to profit and loss account)				

(v)	Discount on purchases Dr.		400	
	To Profit and Loss A/c			400
	(Being transfer of debit balance to profit and loss account)			
(vi)	Profit and loss account Dr.		2,770	
	To Capital A/c			2,770
	(Being transfer of net profit to capital account)			
(vii)	Capital Dr.		1200	
	To Drawings			650
	To Income tax			550
	(Being transfer of drawings and income tax to capital account)			

M/s Atma Ram

Trading and Profit & Loss A/c

for the year ending 31 Dec. 1997

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening Stock	9,6000	By Sales	24,900
To Purchase less returns	11,850	By Closing Stock	3,500
To Wages and salaries	3,200		
To Commission on purchases	200		
To Freight	300		
To Gross Profit c/d	3,250		
	28,400		**28,400**
To Trade expenses	20	By Gross profit b/d	3,250
To Rent	200	By Discount on purchase	400
To Bad debts	500		
To Repairs to plant	160		
To Net profit transferred to capital account	2,770		
	3,650		**3,650**

M/s Atma Ram

Balance Sheet

for the year ending 31 December, 1997

Liabilities		**Amount Rs.**	**Assets**	**Amount Rs.**
Capital				
Opening balance	5,000		Plant	2,000
Add Net profit	2,770		Stock at the end	3,500
	7,770		Debtors	4,000
Less : Income tax	550		Bills receivable	600
Drawings	650		Cash in hand and at bank	200
	1200	6,570		
Loan		900		
Bills payable		500		
Creditors		2,330		
		10,300		10,300

Illustration 13. Prepare Trading and Profit and Loss Account and Balance sheet from the followng balance, relating to the year ending 31 March, 2007.

M/s Vijay

Trading Account

for the year ending 31st March, 2007

Particulars	**Amount Rs.**	**Particulars**	**Amount Rs.**
Capital	10,000	Wages	5,000
Creditors	1,200	Bank	1,000
Returns Outward	500	Repairs	50
Sales	16,400	Stock (1.4.2006)	2,000
Bills Payable	500	Rent	4,000
Plant and Machinery	4,000	Manufacturing Expenses	800
Sundry Debtors	2,400	Trade Expenses	700
Drawings	1,000	Bad Debts	200
Purchases	10.500	Carriage	150
Returns Inward	300	Fuel and Power	100

M/s Vijay

TRADING AND PROFIT AND LOSS ACCOUNT

for the year ending 31st December, 2007

Particulars		**Amount Rs.**	**Particulars**		**Amount Rs.**
To Stock Opening		2,000			
To Purchase	10,500		By Sales	16,400	
Less Returns outward	500	10,000	Less Returns Inwards	300	
To wages		5,000	By Stock-Closing		16,100
To Manufacturing Expenses		800	By Gross Loss c/d		1,450
To Carriage		150			500
To Fuel and Power		100			
		18,050			**18,050**
To Gross loss b/d		500	By Net Loss transferred to		
To Repairs	50		Capital A/c		2,790
Add Unpaid	40	90			
To Rent		400			
To Trade Expenses		700			
To Bad Debts		200			
To Interest on Capital		500			
To Dep. on Plant and Machinery		400			
		2,790			**2,790**

M/s Vijay

Balance Sheet

for the year ending 31st December, 2007

Particulars		**Amount Rs.**	**Particulars**		**Amount Rs.**
Current Liabilities :			Current Assets :		
Creditors	1,200		Bank	1,000	
Bills Payable	500		Sundry Debtors	2,400	
Outstanding Repairs	40	1,740	Stock-in-trade	1,450	4,850
			Fixed Assets :		
Capital :	10,000		Plant and		
Add Interest on			Machinery	4,000	
Capital	500		Less Depreciation	400	3,600
	10,500				
Less Net Loss	2,790				
	7,710				
Less Drawings	1,000	6,710			
		8,450			8,450

Illustration 8. Prepare Trading and Profit and Loss Account and Balance Sheet of Poonam from the followng balance and adjustments.

M/s Poonam
Trading Account
for the year ending 31 March, 2007

Particulars	Dr. (Rs.) Rs.	Cr. (Rs.) Rs.
Purchase / Sales A/c	1,30,295	1,80,500
Cash in hand	500	
Cash at bank	9,500	
Stock as on 01.01.2007	40,000	
Wages……	22,525	
Returns ………..	2,400	
Repairs ………..	1,675	
Debtors/Creditors	30,000	30,305
Bad Debts	2,310	
Loan (12% P.A.)		20,000
Discounts	800	530
Capital		37,500
Interest on loan ……….	600	
Salaries	8,000	
Sales Tax	800	
Octroi	500	
Insurance	1,000	
Charity	125	
Rent	2,000	
Machinery	16,000	
Total	**269,030**	**2,69,030**

Adjustments:

(i) Wages include Rs. 2,000 for erection of new machinery installed on 1.1.2007.

(ii) Provide for depreciation on Machinery @ 5% p.a.

(iii) Stock on 31.12.2007 is Rs. 40,925.

(iv) Salaries unpaid Rs. 800.

(v) Further bad debts Rs. 400.

(vi) Make a provision of 5% on Debtors.

(vii) Rent is paid up to 31 March, 2008.

(viii) Unexpired insurance Rs. 300.

Solution

M/s Poonam
TRADING AND PROFIT AND LOSS ACCOUNT
for the year ending 31 December, 2007

Particulars		Amount Rs.	Particulars		Amount Rs.
To Stock		40,000	By Sales	1,80,500	
To Purchases	1,30,295		Less Returns	2,400	
				1,78,100	
Less Returns	195	1,30,100	Less Sales Tax	800	1,77,300
To Wages	22,525	20,525	By closing Stock		40,925
Less : Tr. To Machinery	2,000				
To Octroi		500			
To Gross Profit c/d		27,100			
		2,18,225			2,18,225
To Repairs		1,675	By Gross Profit b/d		27,100
To Bad debts		2,310			
To interest on loan	600		By Discount		530
Add Outstanding	1,800	2,400			
To Salaries	8000				
Add outstanding	800	8,800			
To Depreciation on Machinery 5% on Rs. 18,000		900			
To Insurance	1,000				
Less : Prepaid	300	700			
To Discount Allowed		800			
To Charity		125			
To Rent	2,000				
Less : Prepaid	500	1,500			
To Bad Debts		400			
To Provision for bad debts		1,480			
To Net profit Tr. To Capital A/c		6,540			
		27,630			**27,630**

M/s Poonam
Balance Sheet
for the year ending 31st December, 2007

Liabilities		Amount Rs.	Assets		Amount Rs.
Loan		20,000	Cash in hand		500
Interest on loan due		1,800	Cash at bank		9,500
Creditors		30,305	Sundry debtors	30,000	
Salaries due		800	Less Bad debts	400	
				29,600	
Capital :			Less Provision	1,480	28,120
Balance	37,500		Stock		40,925
Add Net Profit	6,540	44,040	Rent prepaid		500
			Unexpired insurance		300
			Machinery	16,000	
			Add tr. From wages	2,000	
				18,000	
			Less Depreciation	900	17,100
		96,945			**96,945**

Key Terms Introduced in the Chapter

- Financial Statement
- Revenue Expenditure
- Trading Account
- Positional Statement
- Depreciation
- Prepaid Expense
- Unearned Income
- Appreciation
- Capital Expenditure
- Deferred Revenue Expenditure
- P & L Account
- Grouping and Marshalling for Assets and Liabilities
- Outstanding Expense
- Accrued Income
- Bad Debt

Summary with Reference to Learning Objectives

1. Financial Statement : Statement prepared at the end of the accounting period to ascertain the financial status of the unit is known as financial statement.
2. Capital Expenditure : Expenses incurred in acquiring and increasing the value of the fixed assets are termed as Capital expenditure.
3. Revenue Expenditure : Expenses which are incurred on a routine business are known as revenue expenditure.
4. Deferred Revenue Expenditure : Expenses which are capital in nature are sometimes spilit up to be returned over certain period this is known as defered revenue expenditure.
5. Trading Account : Statement prepared to ascertain the Gross Profit / Gross Loss of the Business enterprise is known of trading account.
6. Profit and Loss Account : The Income statement prepared to ascertain the amount of Net profit and Net Loss of a business undertaking is known as Profit & Loss Account.
7. Positional Statement or Balance Sheet : Statements prepared to ascertain the financial status of assets and liabilities of a busines concern on a particular day is known as positional statement or balance sheet.

8. Grouping and Marshalling of Assets and Liabilities : (a) In order of liquidity (b) In the order of Permanence
9. Depreciation : Decrease in the value of assets due to its constant use or wear and tear.
10. Appreciation : Increase in the value of assets due to an increase in prices in the market.
11. Outstanding Expense : Expenses due but not paid.
12. Prepaid Expense : Expenses paid in advance ors unexpired expenses.
13. Accrued Income : Income earned but not received.
14. Unaccured Income : Income not earned but received in advance.
15. Bad Debt : Amount which is not recored in a financial year.

Question for Practice

Short Answer Questions

1. What are the objectives of preparing a financial statement?
2. What is a Balance sheet?
3. What is Gross Profit?
4. Explain the concept of Cost of Goods sold.
5. What is deferred revenue expenditure?
6. Name any three current assets and current liabilties.
7. Distinguish between Gross Profit and Net Profit.
8. Explain the objective / purpose of Trading Account.
9. How will be show the following items?
   (a) Drawing
   (b) Return inward
   (c) Return outward
   (d) Salary and wages
10. Name the external users of the Financial Statement.

Long Answer Questions

1. What do you mean by adjustment entries? Why is it necessary to pass adjusting entries at the time of preparing final account?
2. Why is it necessary to create provision for bad and doubtful debts? How is it treated in Final accounts?
3. Explain the treatment of accidental loss of goods in the Financial Account, if (a) Goods are not insured. (b) Goods are insured and full claim is admitted by the insurance company.
4. Explain the meaning of grouping and marshalling of assets and liabilities with a suitable example.
5. Explain the rationale behind making adjustments at the time of preparing the final accounts? Mention any three important adjustments that are made for the preparation of the profit and Loss Account.

Practical Questions

1. From the following information, calculate gross profit.

   Sales Rs. 68,000, Purchases Rs. 36,000, Sales Return Rs. 8,000, Purchase Return Rs. 4,000, Opening Stock Rs. 9,000, wages Rs. 12,500 Closing Stock Rs. 3,500.

   [Ans. Gross Profit Rs. 10,000]

2. From the following data, find the amount of Gross profit or gross loss :

   Opening Stock Rs. 7,500, Wages Rs. 8,000 Factory Overhead Rs. 4,500, purchases Rs. 40,000, Sales Return Rs. 5000, Purchases Return Rs. 6,000, Sales Rs. 50,000, Closing Stock Rs. 2,500. [Ans. Gross Loss Rs. 6,500]

3. From the following details, Calculate the amount of gross profit or gross loss and its percentage on cost and on sales. Cash Purchases Rs. 8,000, Credit purchases Rs, 22,500, Opening Stock Rs. 4,500, Cash Sales Rs. 15,000, Credit Sales, Rs. 38,000, Purchase Return Rs. 3,000, Sales Return Rs. 5,000. Wages Rs. 10,500, Fuel & Power Rs. 5,000, Closing Stock-7,500

   [Ans. Gross Profit Rs. 8000, G.P. on Cost = 20%, G. P. on Sales = $16\frac{2}{3}$ %]

4. Find the amount of net sales and Gross profit.

   Gross Profit on Cost = 25%.

   Cost of Goods sold = Rs. 64,000

   [Ans. G.P. = Rs. 16,000, Net Sales = Rs. 80,000]

5. Find the amount of Cost of goods sold.

   Gross Loss on Sales = 20% Sales = Rs. 1,80,000

   [Ans. Cost of goods sold = Rs. 2,16,000]

6. Find the amount of cost and Gross Profit.

   Gross Profit on Cost = 25%

   Sales = Rs. 3,00,000

   [Ans. Cost Rs. 240,000, Gross Profit = Rs. 60,000]

7. Find the amount of sales and Gross Profit.

   G.P. on Sales = $16\frac{2}{3}$ %

   Cost of goods sold = Rs. 1,48,375

   [Ans. Gross Profit Rs. 29,675, Sales Rs. 1,78,050]

8. From the following Trial Balance of Kumar as on 31 December, 2006 prepare Trading and Profit and Loss Account and a Balance Sheet.

Cr Balances	**Rs.**	**Dr. Balances (Contd.)**	**Rs.**
Capital	36,000	Bad Debts	287
Creditors	8,720	Interest	1,295
Bills Payable	2,528	Insurance	417
Sales	78,182	Machinery	10,000
Loan	12,000	Stock (1.1.71)	9,945
Dr. Balances		Purchases	62,092
Debtors	3,885	Wages	4,300
Salaries	4,000	Building	23,780
Discount	1,000	Fixtures & Fittings	16,156
Postage	273		

Charges depreciation on Machinery 4% and on Building 5%. Allow 5% interest on Capital, Stock on 31-12-2006 Rs. 14,300.
[Ans. Gross Profit Rs. 16,145, Net Profit Rs. 5,484, and Total of Balance Sheet Rs. 66,532.]

9. From the Trial Balance of Mohan & Co, prepare Trading Account, Profit & Loss A/c and Balance Sheet as on 31st Dec., 2006.

Cr Balances	**Rs.**	**Dr. Balances (Contd.)**	**Rs.**
Capital	10,000	Wages	5,000
Creditors	1,200	Bank	1,000

Returns Outwards	5,000	Repairs	50
Sales	16,000	Stock (1.1.76)	2,000
Bills Payable	500	Rent	400
Dr. Balances		Manufacturing Exp.	800
Plant & Machinery	4,000	Trade Exp.	700
Sundry Debtors	2,400	Bad Debts	200
Drawings	1,000	Carriage	150
Purchases	10,500	Returns Inwards	400

The Closing Stock was valued at Rs. 1,450, Provide for depreciation on Plant & Machinery Rs. 400 and allow 5% interest on Capital, Rs. 40 is due for repairs.
[Ans. Gross Loss Rs. 500; Net Loss Rs. 2,690; and Total of Balance Sheet Rs. 8,450.]

10. From the following Trial Balance prepare Trading and Profit & Loss Account and the Balance Sheet as on 31 Dec., 2006.

	Rs.		**Rs.**
Capital	19,000	Cash at Bank	2,600
Drawings	700	Salaries	800
Plant and Machinery	12,000	Repairs	190
Horses and Carts	2,600	Stock	1,600
Sundry Debtors	3,600	Rent	400
Sundry Creditors	2,600	Manufacturing Exp.	150
Purchases	2,000	Bills Payable	2,350
Sales	4,200	Bad Debts	500
Wages	800	Carriage	160

The Closing Stock was Rs. 1,600, Depreciate Plant & Machinery by 10% and Horses & Carts by 15%. Unpaid rent amounted to Rs. 50.
[Ans. Gross Profit Rs. 290; Net Loss Rs. 2,490; and Total of Balance Sheet Rs. 20,810]

11. D. Jains books show the following balances. You are asked to prepare his Trading and Profit & Loss A/c and Balance Sheet.

Dr Balances	**Rs.**	**Dr. Balances (Contd.)**	**Rs.**
Stock (1.1.2007)	21,000	Office Exp.	650
Purchases	21,650	Interest Paid on Loan	200
Carriage Inwards	250	Bills Receivable	1,800
Carriage Outwards	600	Legal Charges	1,900
Wages	6,000	Plant & Machinery	25,000
Motive Power Heating & Lighting	1,600	Tools	5,000
		Credit Balances	
Printing & Stationary	2,660	Sales	48,590
Sundry Debtors	28,100	Reserve	500
Furniture & Fixtures	2,000	Loan	38,000
Investments	4,000	Discount Received	580
Free Hold Premises	10,000	Sundry Creditors	2,430
Travelling Exp.	400	Capital A/c	42,710

Depreciate Furniture and Fixtures by 5%, and Plant & Machinery by 10%. Tools were valued on 31 Dec.2007 at Rs. 4,500. Stock on 31st Dec. 2007 was Rs. 18,000.
[Ans. Gross Profit Rs. 16,090; Net Profit Rs. 7,160; and Total of Balance Sheet Rs. 90,800]

12. From the following Trial Balance prepare a Trading and Profit & Loss A/c for year ended 31st Dec. 2006 and also the balance sheet as on that Date.

	Rs.		Rs.
Stock (1.1.2006)	6,000	Sundry Debtors	900
Purchases	11,250	Carriage & Freight	250
Carriage Inwards	250	Bills Receivable	1,800
Sales	16,500	Rent & Taxes	300
Cash in hand	500	General Exp.	275
Cash at Bank	1,600	Discount (Credit)	275
Building	10,000	Insurance	150
Salaries	650	Capital	12,000
B/R	500	Sundry Creditors	5,000
B/P	600		

Value of Stock in hand on 31 Dec. 2006 was Rs. 4,000. Provide for depreciation on Building at 5% and interest on Capital at 5%.
[Ans. Gross Profit Rs. 3000; Net Profit Rs. 800; and Total of Balance Sheet Rs. 17,000]

13. The following Trial Balance has been extracted from the books of M/s Ram Prasad & Sons on 31st December, 2006.

Dr. Balances	**Rs.**	**Cr. Balances**	**Rs.**
Machinery	4,000	Capital	9,000
Cash at Bank	1,000	Capital	16,000
Cash in hand	500	Sundry Creditors	4,500
Wages	1,000	Interest Received	300
Purchases	8,000		
Stock on 1 Jan., 1970	6,000		
Sundry Debtors	4,400		
Bills Receivable	2,900		
Rent	450		
Commission	250		
General Expenses	800		
Salaries	500		
	29,800		**29,800**

Provide for interest on Capital at 5% p.a. Depreciate Machinery at 10%. Wages outstanding amount to Rs. 50. Rent prepaid amounts to Rs. 100. Stock on 31 Dec. 2006 amounts to Rs. 8,000.
Prepare Trading and Profit & Loss Account for the year ending 31 December, 2006 and Balance Sheet as on the last date of the year.
[Ans. Gross Profit Rs. 8,950; Net Profit Rs. 6,500; and Total of Balance Sheet Rs. 20,500]

14. The following are the balances extracted from the books of Nand Lal on 31st December, 2006:

	Rs.		Rs.
Narain Lals Capital	30,000	Sales	1,50,000
Narain Lals Drawings	5,000	Sales Returns	2,000
Furnitures & Fittings	2,600	Discount (Dr.)	1,600
Bank Overdraft	4,200	Discount (Cr.)	2,000
Creditors	13,800	Tax & Insurance	2,000
Balance Premises	20,000	General Exp.	4,000

Stock (1.1.1962)	22,000	Salaries	9,000
Debtors	18,000	Comission (Dr.)	2,200
Rent from Tenants	1,000	Carriage on purchases	1,800
Purchases	1,10,000	Bad Debts written off	8,000

Stock on hand on 31 December, 2006 was Rs. 20,060.
Write off depreciation : Busines Premises Rs. 300, Furniture and Fittings Rs. 250.
Make a reserve of 5% on Debtors for doubtful debts. Allow interest on Capital at 5% and carry forward Rs. 200 for unexpired insurance.
Prepare Trading and Profit and Loss Account for the year and a Balance Sheet as on that date.
[Ans. Gross Profit Rs. 34,260; Net Profit Rs. 14,910; and Total of Balance Sheet Rs. 59,410]

15. The following are the Ledger balances abstracted from the books of Mr. X, a businessman :

	Rs.		Rs.
Xs Capital	60,000	Sales Returns	4,000
Xs Drawings	10,000	Discount (Dr.)	3,200
Bank Overdraft	8,400	Discount (Cr.)	4,000
Furnitures & Fittings	5,200	Tax & Insurance	4,000
Business Premises	40,000	General Exp.	8,000
Creditors	26,600	Salaries	18,000
Stock (1.1.1964)	44,000	Comission (Dr.)	4,400
Debtors	36,000	Carriage on purchases	3,600
Rent from Tenants	2,000	Reserve for bad & doubtful debt	1,000
Purchases	2,20,000	Bad Debts written off	1,600
Sales	3,00,000		

Stock on hand on 31 December, 2006 was estimated at Rs. 40,120.
Write off depreciation : Busines Premises Rs. 600, Furniture and Fittings Rs. 520.
Making a reserve of 5% on Debtors for doubtful debts. Allow interest on Capital at 5% and carry forward Rs. 1,400 for unexpired insurance.
Prepare Trading and Profit and Loss Account and Balance Sheet on 31st December, 2006.
[Ans. Gross Profit Rs. 68,520; Net Profit Rs. 31,800; and Trial of Balance Sheet Rs. 1,19,800]

16. The trial balance given is extracted from the books of a merchant on 31st December, 2006.

Dr. Balances	**Rs.**	**Dr. Balances (Contd.)**	**Rs.**
Furniture and Fittings	640	Taxes and Insurance	1,250
Motor Vehicle	6,210	General Charges	782
Buildings	7,500	Salaries	3,200
Bad Debts	125	**Credit Balances :**	
Sundry Debtors	3,800	Capital	12,500
Stock, 1st January, 2006	3,460	Provision for Bad Debts	200
Purchases	5,575	Sundry Creditors	2,500
Returns Inward	200	Sales	15,450
Advertising	480	Bank Overdraft	2,850
Interest	118	Returns Outward	125
Cash in Hand	650	Commission	375

- Stock in hand on 21st December, 2006 was Rs. 3,250.
- Depreciate Buildings @ 5%. Furniture and Fittines at 7½% and Motor Vehicle @ 20%.
- Rs. 85 is due for interest on bank overdraft.
- Salaries Rs. 300 and Taxes Rs. 120 are outstanding.
- Insurance amounting to Rs. 100 is prepaid.
- The provision for Bad Debts is to be made equal to 5% on Debtors.

Prepare the Trading and Profit and Loss Account for 2006 and the Balance Sheet on 31 December, 2006.

[Ans. Gross Profit Rs. 9,590; Net Profit Rs. 1048; Balance Sheet Rs. 20,295

17. On 31 March, 2007 the following figures were extracted from the books of M/s. Ramarao. Prepare final accounts for the year after taking into account the following adjustments

- Depreciation 10% of Plant & Machinery and Fixtures and Fittings
- Provide for March rent unpaid Rs. 150
- Provide for Bad Debts 2½% on Sundry Debtors
- Outstanding Wages Rs. 80 and Salaries Rs. 350; and
- Stock on 31 March, 1971, Rs. 16,580.

	Rs.		Rs.
Plant and Machinery	55,000	Cash at Bank	2,245
Fixtures and Fittings	1,720	Cash in Hand	118
Capital	93,230	Sundry Debtors	48,000
Factory Fuel and Power	542	Sundry Creditors	22,880
Office Slaries	3,745	Purchases	83,290
Lighting of Factory	392	Wages	9,915
Sales	1,26,117	Rent & Taxes	1,705
Travelling Exp.	925	Office Exp.	2,778
Carriage on Sales	960	Carriage on Purchases	897
Discount	422	Purchases Returns	3,172
Drawings	6,820	Bills Payable	6,412
Stock	21,725	Commission	260
Manufacturing Exp.	2,940	Sales Returns	7,422
Insurance	470	Insurance Prepaid	100

[Ans. Gross Profit Rs. 17,946 ; Net Loss Rs. 111; and Total of Balance Sheet Rs. 1,16,891]

18. From the following balance, and the undermentioned particulars, you are required to make out a Trading and Profit and Loss Account for the year ended 31 March, 2006 and a Balance Sheet on that date.

	Rs.		Rs.
Trade Creditors	35,780	Discount Received	5,800
Bills Payable	18,700	Bills Receivable	5,360
Law Charges	420	Purchases	1,17,200
General Expenses	7,580	Stock 2006	63,900
Cash at Bank	18,980	Trade Debtors	63,220
Capital Account	1,69,200	Carriage Inwards	3,580
Premises	40,000	Returns Inwards	28,600
Loan from Bank	40,000	Salaries	35,700
Returns Outwards	16,200	Sales	1,98,400
Bad Debts Provision	2,200	Bad Debts	2,600
Cash in hand	400	Rent, Rates and Taxes	11,200
Discount Allowed	8,600	Plant and Machinery	59,000
Wages (Manufacturing)	39,940		

The following adjustments are necessary.

- Bad Debts estimated at Rs. 2,910
- Provision for 3% discount on debtors and 2% on creditors.

- One years interest due to bank of Rs. 1,600.
- Depriciation of machinery in 2007 at 10%
- Stock in hand at 31 March of Rs. 93,840

[Ans. Gross Profit Rs. 55,220 ; Net Profit 5,166.30; and Total of Balance Sheet Rs. 2,70,180.70]

19. From the balance given below and the adjustments that follow, prepare Trading and Profit & Loss Account for the year ending 31 March, 1969 and a Balance Sheet as on the last date.

	Rs.		Rs.
Trade Creditors	35,780	Discount Received	5,800
Bills Payable	18,700	Bills Receivable	5,360
Legal Charges	420	Purchases	1,17,200
General Expenses	7,580	Stock , April 1, 1968	63,900
Cash at Bank	18,980	Trade Debtors	63,220
Capital	1,69,200	Carriage Inwards	3,580
Building	40,000	Sales Returns	28,600
Bank Loan @ 10% p.a.	40,000	Salaries	35,700
Returns outward	16,200	Sales	1,98,400
Reserve for Doubtful Debts	2,200	Bad Debts	2,600
Cash in Hand	400	Rent, Rates & Taxes	11,200
Discount Allowed	8,600	Plant and Machinery	59,000
Wages (Manufacturing)	39,940		

The following adjustments are necessary.

- Bad Debts estimated at Rs. 3,220. create reserve for the amount.
- Interest on Bank Loan is outstanding for full year.
- Depreciate Plant and Machinery at the rate of 10% and Building at 2½%
- Stock on 31 March, 1969 is Rs. 93,840.

[Ans. Gross Profit Rs. 55,220 ; Net Profit Rs. 3,000; and Total of Balance Sheet Rs. 2,70,680]

20. From the following Trial Balance of C.D. Lal as at 31 March, 2006, you are required to prepare the Trading and Profit & Loss Account for the year ended 31 March, 2006 and Balance Sheet as at that date.

Dr. Balances	**Rs.**	**Cr. Balances**	**Rs.**
Stock	45,000	Capital	75,000
Purchases	2,25,000	Sales	4,20,750
Plant and Machinery	75,000	Sundry Creditors	15,000
Trade Charges	10,000	Bad Debts Provision	200
Carriage Inward	1,500	Bills Payable	2,000
Factory Rent	1,500		
Discount	350		
Insurance	700		
Sundry Debtors	60,000		
Office Rent	3,000		
Printing & Stationery	600		
General Expenses	2,800		
Advertising	15,000		
Bills Receivable	3,000		
Drawings	6,000		
Salaries	18,000		
Manufacturing wages	20,000		
Furniture & Fixtures	7,500		

Coal, Gas & Water	1,000	
Cash in hand	2,000	
Cash at Bank	12,500	
	5,12,950	**5,12,950**

The following adjustments are to be taken into consideration

- The closing stock amounted to Rs. 35,000.
- Plant & Machinery and Furniture to be depreciated at 10%.
- Bad Debts and Reserve to be raised to 2½% on Debtors.
- Provide for outstanding liabilities of Factory Rent Rs. 300 and Office Rent of Rs. 600.
- Insurance includes Rs. 100 in respect of 2006-07.
- The provision for Bad Debts is to be made equal to 5% on Debtors.

[Ans. Gross Profit Rs. 1,60,450; Net Profit Rs. 98,450; B/s Total Rs. 1,85,350]

Q.21 Prepare Trading and Profit & Loss Account and Balance Sheet from the following particulars as on 31 Dec, 2006.

Capital	**Dr. Rs.**	**Cr. Rs.**
Cash in Hand	1,500	10,000
Bank Overdraft @ 5%		
Purchases and Sales	12,000	2,000
Returns	1,000	15,000
Establishment Charges	2,500	2,000
Taxes and Insurance	500	
Bad Debts Reserve		1,000
Bad Debts	500	
Sundry Debtors and Creditors	5,000	1,850
Commission		500
Investments	4,000	
Stock on 1.1.2006	3,000	
Drawings	1,400	
Furntitures	600	
Bills Receivable & Bills Payable	3,000	2,500
Collected Sales Tax		150
	35,000	**35,000**

Further, you are required to take into consideration the following

- Salary Rs. 100 and Taxes Rs. 400 are outstanding but insurance of Rs. 50 prepaid.
- Commission amounting to Rs. 100 has been received in advance for work to be done next year.
- Interest accrued on investment Rs. 210.
- Bad Debts Reserve is to be maintained at Rs. 1,000.
- Depreciation on Furniture is to be charged at 10%.
- Stock on 31 December 2006 was valued at Rs. 4,500.

[Ans. Gross Profit Rs. 5,500; Net Profit Rs. 2,000; Total of Balance Sheet Rs. 17,800]

CHAPTER 7

Taxation

Direct and Indirect Taxes

Learning Objectives

After studying this chapter you will be able to

- understand the meaning of direct tax and indirect tax
- explain the meaning of various terms used like income tax, previous year, assessment year, financial year, residential status, assessee, etc.
- appreciate the objectives of Sales Tax, Value Added Tax (VAT), Central Sales Tax (CST), Exercise, Service Tax, Fringe Benefit Tax (FBT), Banking Transaction Tax (BTT), Canvat Credit etc.
- For meeting its expenses and for providing funds for the development of the economy the government of every country imposes taxes of different types on entities like individuals, firms, companies etc. Broadly these taxes can be divided into the following two categories
  - Direct Taxes
  - Indirect Taxes

7.1 Direct Taxes

A direct tax is paid by a person upon whom it is legally imposed; its effect is borne by the tax payer, for example, income tax. Income tax is paid by an individual, a Hindu undivided family, a company, a firm, and local bodies etc. on their incomes. The effect of this tax is borne by these tax payers themselves, the tax payer cannot shift the incidence of the tax upon somebody else. In other words a direct tax is demanded from the very person who it is intended or devised for. Another example of a direct tax is wealth tax. We will be discussing income tax in detail here.

7.2 Income Tax

Income tax is a direct tax which is levied on the incomes of individuals and registered bodies. It is a very big source of government revenues. This tax is collected by the income tax department of the government mostly from such pointor p;aces where the income is generated. For example the income tax on the salary income of individuals is deducted from their salaries by their employers who, in turn, deposit it with the government. Following are the various terms used in income tax.

(i) **Previous year :** According to Section 3 of the Income Tax Act a previous year means a financial year immediately preceeding the assessment year. For example, for the assessment year, 2006 - 2007, the year 2005 - 2006 will be the previous year, i.e, for the assessment year 2006 - 07 the year starting from 1 April, 2005 and ending on 31 March, 2006 will be the previous year.

(ii) **Assessment year :** According to Section 2(a) of the Income Tax Act, an assessment year means a period of twelve months beginning from 1 April and ending on 31 March. For example, the assessment year 2006 - 2007 will include the period starting from 1.4.2006 and ending on 31.3.2007. The assessment year starts from 1 April of a year and ends on 31 March of the next year.

The income earned in a year is assessed for the payment of tax in the next year. For example, Mohan earned an income of Rs 10,00,000 during the financial year starting from 1.4.2005 and ending on 31.3.2006. He is supposed to pay tax on this income during the next year starting from 1.4.2006 and ending on 31.3.2007. Here the year starting from 1.4.2005 and ending on 31.3.2006 (2005 - 2006) will be the previous year and the year starting from 1.4.2006 and ending on 31.3.2007 (2006 - 2007) will be the assessment year. Therefore, the year in which income is taxable is called the assessment year. In other words we can say that previous year is a year immediately preceeding the assessment year and the assessment year is a period twelve months starting 1 April of a year and ending on 31 March of the next year.

(iii) **Calendar year :** It is the year having twelve months beginning from 1 January and ending on December 31. This means that the calendar year 2007 is the year which began on 1.1.2007 and will end on 31.12.2007.

(iv) **Financial year :** It is the period of twelve months starting from 1 April of calendar year and ending on March 31 of the next calendar year. It means that financial year 2006 - 2007 is a period of twelve months which started from 1.4.2006 and ended on 31.3.2007.

(v) **Accounting year :** It is a period of twelve months beginning from any date. It may be from 1 January to 31 December; from April 1 to March 31 ; from July 1 to June 30; from October 1 to September 30.

(vi) **Persons :** According to Section 2(31) of the Income Tax Act a person includes the following

- An individual
- A hindu undivided family
- A company
- A firm
- An association of persons, a body of individuals, whether incorporated or not
- A local authority, and
- An artificial jurisdical person not included in any of the above.

(vii) **Assessee :** According to Section 2(7) of the Income Tax Act an assessee means a person

- Who is liable to pay any tax or any other sum of money (interest, fine, penality etc). Under this Act iirrespective of whether any proceeding under this Act has been undertaken for assessment of his income, or the income of any other person in respect of which he is assessable or, of the loss sustained by him or by such other person, or the amount of refund due to him or to such other.

7.2.1 Residential Status

Individual Resident (Sec. 6(1))

An individual is said to be resident in India in the previous year if he fulfils any one of the following two basic conditions.

Category A : Basic Conditions

(a) He has been in India in that year for a period, or periods Amounting in all to 182 days or more ; or

(b) That within 4 years immediately preceding that year, he has been in India for a period or periods amounting in all to 365 days or more and is in India for a period or periods amounting in all to 60 days or more in that year.

Explanation

- Where an individual, being a citizen of India, leaves India in any previous year as member of the crew of an Indian ship or for the purpose of employment outside India, the period of 60 days or more mentioned in (b) above will be 182 days or more.
- Where an individual being a citizen of India or a person of Indian origin, who being outside, comes on a visit to India in any previous years, the period of 60 days or more mentioned in (b) above will be 182 days or more.

Resident and ordinarily Resident

A resident individual will be treated as ordinarily resident assessee if he satisfies at least one of the basic conditions of category A and both the following conditions.

Category B : Additional Conditions

(a) He has been resident in India (by satisfying at least one of the conditions of Category A) in two out of the 10 previous years preceding the relevant previous year; and

(b) He has been in India for a period or periods amounting in all to 730 days or more during seven previous years preceding the relevant previous year.

Resident but not Ordinarily Resident (Sec. 6 (6) (a)

If an individual satisfies at least one of the two basic conditions of Category A (a or b) but does not satisfy both the conditions of Category B, he is said to be 'resident' but not ordinarily resident.

Another Approach to identify 'not ordinarily resident'

If an individual satisfies at least one of the two basic conditions of Category A and satisfies any one of the following conditions he is classified as not ordinarily resident;

(a) He has been a non-resident in India in 9 out of 10 previous year preceding that year: or

(b) He has been during the 7 years preceding that year in India for a period of or periods amounting in all 729 days or less.

7.2.2 Tax Liablity

[Sec. 5]

The tax liability of different classes of assessees on the basis of their residence is as given below.

Resident : The total income of a person, who is a resident in the relevant previous year includes all incomes from whatever sources derived which

(i) is received or is deemed to be received in India in such year by or on behalf or such person, or

(ii) accrues or arises or is deemed to accrue or arise to him in India during such year, or

(iii) accrues or arises to him outside India during such year.

Not Ordinarily Resident : If the assessee is a not ordinarily resident, the total income of the relevant previous year includes all incomes from whatever sources derived which

i) is received or is deemed to be received in India in such year by or on behalf of such person, or

ii) accrues or arises or is deemed to accrue or arise to him in India during such year, or

iii) accrues or arises to him outside India during such year and is derived from business controlled in or a profession set up in India.

Non-resident: If he is a non-resident in India, the total income of the relevant previous year includes all incomes from whatever sources derived which

(i) is received or is deemed to be received in India in such year by or one behalf of such person, or

(ii) accrues or arises or is deemed to accrue or arise to him in India during such year.

Note

- Income accruing or arising outside India shall not be deemed to be received in India by reason only of the fact that it is taken into account in a balance sheet prepared in India.
- If a particular income has once been included in the total income on accrual basis, it cannot be included in total income again either in the same year, or in a subsequent year, on the basis of received or deemed to be received by him in India.
- Any Income is to be included in the total income if it is taxable as per provisions of Income Tax Act, and shall be computed as per provisions of the Act.

7.2.3 Salary as a Source of Income

Any remuneration paid by an employer to his employee in consideration of his services is called salary. It includes monetary value of those benefits and facilities which are provided by the employer and are taxable.

Sec. 15 : The following incomes shall be chargeable to income tax under the head 'salaries'.

i) Any salary due from an employer or a former employer to an assessee in the previous year, whether paid or not.

ii) Any salary paid or allowed to him in the previous year by an employer or a former employer, whether paid or not, and

iii) any arrears of salary paid or allowed to him in the previous year by an employer or a former employer, if not charged to income tax for any earlier previous year.

Computation of income under the head "salaries" : 'Salary' is made up of the following. Basic Pay + Dearness Allowance + Commission + Bonus + Allowance

(a) Specific / Notified Special Allowances

- Allowances which are exempted to the extent of actual amount received or the amount spent for the performance of the duties of an office or employement of profit, whichever is less: like traveling allowance, daily allowance, conveyance allowance, etc.
- Allowances which are exempted to the extent of amount received or the limit specified, whichever is less: like children, education allowance, hostel expenditure allowance, transport allowance etc.
- Allowances where exemption is allowed upto a certain percentage of the amount received like allowance to transport employees.

(b) Allowances which are exempted in case of certain persons like sumptuary allowance to High Court and Supreme Court judges, allowance received by an employee of UNO from his employer.

\+ Perquisites

- Perquisites taxable in the hands of all categories of employees, for example, services of sweeper, gardener, etc.
- Perquisites that are taxable only in the case of specified employees, for example, services of sweeper, gardener, etc.
- Tax free perquisites like medical facility or medical reimbursement, recreational facilities, loans to employees, etc.

+	Profits in lieu of salary like gratuity, pension
+	Provident funds like statutory provident fund, recognised provident fund, unrecognised provident fund
=	Gross Salary
Less :	Deduction

Standard Deduction u/s/16(i)

-	For those with salary income upto Rs. 1.5 Lakh.	-	1/3% of the salay subject to maximum Rs. 30,000
-	More than Rs. 1.5 Lakh and upto Rs. 3 Lakh	-	Rs. 25,000
-	More than Rs. 3 Lakh and upto Rs. 5 Lakh	-	Rs. 20,000
-	More than Rs. 5 Lakh	-	Nil

Section 16(ii) Entertainment Allowance

Section 16 (iii) Tax on Employment

7.2.4 Taxable Income

(a)	INCOME FROM SALARIES	Amount
	Salary/Bonus/Commission, etc.	………..
	Taxable allowance	………..
	Value of taxable perquisites	………..
	Gross salary	………..
	Less : Deductions under Section 16	………..
	Net taxable income from salary	………..

(b) INCOME FROM HOUSE PROPERTY

Net annual value of House property

Less : Deductions under section 24

Net taxable income from house property

(c) PROFITS AND GAINS OF BUSINESS AND PROFESSION

Net profit as per P & L Account

Less/Add : Adjustments required to be made

As per the provisions of Income Tax Act

Net profit and gain of business and profession

(d) CAPITAL GAINS

Capital gains as computed

Less : Exemptions under Section 54/54B/54D, etc.

Income from capital gains

(e) INCOME FROM OTHER SOURCES

Gross income

Less : Deductions

Net income from other sources

Gross Total Income [a +b +c +d +e)

Less: Deductions available under

Chapter VIA (Sections 80C to 80U)

7.2.5 Total Income

Tax Rates for an individual

Taxable slab (Rs)	**Rate (%)**
1,00,000	
1,35, 000(for women)	Nil
1,85,000(for senior citizens)	
1,00,001-1,50,000	10%
1,50,001-2,50,000	20%
2,50,001 upwards	30%
10,00,000 upwards	30%

Surcharge of 10% for those whose taxable income is Rs 10 lakhs or more. An education cess is charged at 2% of the aggregate of tax and surcharge.

In other words, the rates of tax for the assessment year 2006-07 for an individual can be stated as follows:

(a) In case of individual being resident in India, who is of the age of 65 years or more

upto Rs 1,85,000	Nil
Rs 1,85,001 to Rs 2,50,000	20%
Above Rs. 2,50, 000	30%

(b) In case of a woman below 65 years of age

upto Rs 1,35, 000	Nil
Rs 1,35,000 to Rs 1,50,000	10%
Rs 1,50,000 to Rs 2,50,000	20%
Above Rs 2,50,000	30%

(c) For other individuals

Upto Rs 1,00,000	Nil
Rs 1,00,000 to Rs 1,50,000	10%
Rs 1,50,000 to Rs. 2,50,000	20%
Above Rs 2,50,000	30%

Illustration 1. Krishna has a total salary income of Rs 1,20,000. He contributes Rs 500 per month towards providend fund. Calculate the amount of income tax he has to pay.

Solution : Total salaried income = Rs 1,20,000

Standard deducation of Rs 1,20,000 limited to Rs 30,000 = Rs 30,000

Taxable income = Rs. (1,20,000 - 30,000) = Rs. 90,000

Tax upto Rs 50,000 = Nil

Tax for next Rs. 10,000 = Rs 1,000 (1)

Tax for Rs (90,000 -60,000) @ 20%

$= \text{Rs } 30{,}000 \times \frac{20}{100} = \text{Rs } 6{,}000$ (2)

Total Tax [sum of (1) and (2)] = Rs 7,000

Contributions to Provident Fund = Rs 500 × 12 = Rs 6,000

Tax rebate on account of savings = Rs 6,000 = Rs 1,200

Therefore, tax to be paid = Rs (7,000 - 1,200) = Rs 5,800

Sucharge at the rate of 5% $= \text{Rs } 5{,}800 \times \frac{5}{100} = \text{Rs } 290$

Net tax payable = Rs (5,800 + 290) = Rs 6,090.

Illustration 2. Savita's monthly salary is Rs 12,000. She contributes Rs 600 per months towards Provident Fund and Rs 3000 as annual LIC premium. Find the amount of tax she has to pay.

Solution : Total annual salary of Savita = Rs 12,000 × 12 = Rs 1,44,000

Standard deduction $= \frac{1}{3}$ of Rs. 1,44,000 limited to Rs 30,000 = Rs 30,000

Taxable income = Rs (1,44,000 - 30,000) = Rs 1,14,000

Tax upto Rs. 50,000 = Nil

Tax for next Rs 10,000 = Rs 1,000 (1)

Tax for Rs. (1,14,000 - 60,000) @ 20%

$= \text{Rs } 54{,}000 \times \frac{20}{100} = \text{Rs } 10{,}800$ (2)

Total tax [sum of (1) and (2)] = Rs 11,800

Rebate for women = Rs 50,000

PF = Rs. 600 × 12 = Rs 7,200

Savings (PF + LIC) Rs 7,200 + Rs 3,000 = Rs 10,200

Rebate on account of savings @ 20% $= \text{Rs } \frac{20}{100} \times 10200 = \text{Rs } 2{,}040$

Total rebate = Rs (5,000 + 2,040) = Rs 7,040

Tax to be paid = Rs (11,800 - 7,040) = Rs 4,760)

Sucharge @ 5% $= \frac{5}{100} \times 4{,}760 = \text{Rs } 238$

Net tax payable = Rs. (4,760 + 238) = Rs. 4,998.

Illustration 3. Annual income from salary of Maryam is Rs 2,40,000. She contributes Rs 2,000 per month to Provident Fund, pays annual LIC premium of Rs 5,000, invests Rs 15,000 in NSC's, and donates Rs 5,000 to P.M.'s National Relief Fund carrying 100% relief. Calculate the income tax she has to pay for the year.

Solution : Total salaried income = Rs 2,40,000

Standard deduction = Rs 25,000 [Why? see as per 16(i)]

Deducation on donation to P.M.'s National Relief Fund = Rs 5,000.

Taxable income = Rs (2,40,000 - 25,000 - 5,000) = Rs 2,10,000

Total income tax $= \text{Rs } 190{,}00 + \frac{30}{100}(2100000 - 150000)$

$= \text{Rs } 19{,}000 + \frac{30}{100}(60{,}000)$

= Rs [19,000 + 18,000]

= Rs 37,000

Saving = Rs (2,000 × 12 + 5,000 + 15,000) = Rs 44,000

Rebate on savings $= \text{Rs } 44{,}000 \times \frac{15}{100} = \text{Rs } 6{,}600$

Tax rebate for women = Rs 5,000

Total rebate = Rs (6,600 + 5,000) = Rs 1,1600

Tax to be charged = Rs (37,000 - 11,600)

= Rs 25,400

Surcharge = Rs 25,400 × $\frac{5}{100}$ = Rs 1,270

Net tax payable = Rs (25,400 + 1,270) = Rs 26,670

Illustration 4. Md. Wakil, aged 67 years, gets a pension of Rs 18,000 per month. He contributes Rs 60,000 towards PPF and purchases NSC's worth Rs 10,000. He also donates Rs 10,000 towards PM's National Relief Fund. Calculate the income tax he has to pay in the year.

Solution : Total income = Rs (18000 × 12) = Rs 21,600

Standard deduction = Rs 25000 (Why?) [see as per 16(i)]

Deduction on account of donation to PM's National Relief Fund = Rs 10,000

Total taxable income = Rs (2,16,000 - 25,000 - 1000) = Rs 1,81,000

Tax upto Rs 50,000 = Nil

Tax for next Rs 10,000 = Rs 1,000

Tax for next Rs 90,000 = Rs 18,000

Tax for next Rs (1,81,000 - 1,50,000 or Rs 31,000) @ 30% = Rs 9,300

Total income tax = Rs (1,000 + 18,000 + 93,000) = Rs 28,300

Savings = Rs (60,000 + Rs 10,000) Rs 70,000

Tax rebate for savings = Rs 70,000 × $\frac{15}{100}$ = Rs 10,500

Tax rebate to senior citizens = Rs 15,000

Total rebate = Rs (10,500 + 15,000) = Rs 25,500

Total Tax to be charged = Rs (28,300 - 25,500)

= Rs 2800

Surcharge @ 5% = Rs 140

Net tax payable = Rs (2,800 + 140) = Rs 2,940

Illustration 5. Mrs Nazish earns Rs. 35,000 per month (excluding HRA). She donotes Rs. 30,000 to Prime Minister Relief Fund (100% exemption) and Rs. 40,000 to a charitable Hospital (50% exemption). She contributes Rs 5,000 per month to provident fund and Rs 25,000 per annum towards LIC premium. She purchases NSC worth Rs 20,000. She pays Rs 2,300 per month towards income tax for Eleven months. Find the amount of income tax she has to pay in 12th month of the year. Use the following to calculate income tax.

(a) Savings : 100% exemption for permissible saving upto Rs 1,00,000.

(b) Rates of Income Tax for ladies :-

	Slab	Income Tax
(i)	Upto Rs 1,35,000	No tax
(ii)	From Rs 1,35,0001 tom exceeding Rs 1,35,000	Rs 150000 10% of taxable income
(iii)	From Rs 1,50,001 to Rs 2,50,000	Rs 1500 + 20% of the amount exceeding Rs 1,50,000

(iv) Rs 2,50,001 and above — Rs 21,500 + 30% of the Rs. 2,50,000.

c) Education Cess — 2% of income tax payable

Solution

(a) Ms. Nazish is a female.

(b) Annual Income = Rs 35,000 × 12 = Rs 4,20,000 -----(i)

(c) Donations (i) PM,s Relief Fund = Rs 30,000 (100%).
(ii) Charitable hospital = Rs 40,000 (50%)

(d) Rebate on donations

$30,000 \times \frac{100}{100} + \frac{40,000 \times 50}{100}$

= Rs 50,000 ___________________________ (ii)

(e) Total Savings :

GPF = 5000 × 12 =		Rs 60,000
LIC		25,000
NSC		20,000
Total Saving	=	Rs 1,05,000
		1,00,000

Rebate on savings = Rs.1,00,000 _____________________________ (iii)

(f) Taxable income = (i) - [(ii) + (iii)]
= Rs 4,20,000 - Rs 1,50,000
= Rs 2,70,000

(g) Tax = Rs 21,500 + $\frac{30}{100}$ × (Rs 2,70,000 - Rs 2,50,000)
= Rs 21,500 + Rs 20,000 x $\frac{30}{100}$ = Rs 27,500

(h) Ed. cess = $\frac{2}{100}$ × Rs 27,500 = Rs 550

(i) Net tax = Rs 27,500 + Rs 550 = Rs 28,050

(j) Advance tax paid = 2,300 × 11 = Rs 25,300

(k) Tax liability for the last month = Rs 28,050 - Rs 25,300 = Rs 2,750

7.3 Indirect Taxes

An indirect tax is a tax which is imposed on one person and is paid partly or wholly by another party. This means that the effect or incidence of an indirect tax is not upon the party who pays the tax but on someone else. For example, sales tax is imposed on the sales of a business. This tax is collected by the seller from his customers and paid to the government. Here the seller does not bear the impact of the tax, rather he simply collects the tax and deposits the same with the sales tax department. The impact of the tax is borne by the customer who actually purchases the goods. Since this tax is paid not by the buyer himself, but by the seller, it is called indirect tax. Other examples of indirect taxes are value added tax, excise duty, service tax etc.

7.3.1 Sales Tax

A sales tax is a state or locality imposed percentage tax on the selling or renting of certain property or services. Because the tax is collected from the customer, it is a consumption tax.

The Centrel Sales Tax Act, 1956

An Act to formulate principles for determining when a sale or purchase of goods takes place in the course of inter-state trade or commerce, or outside a state, or in the course of import into or export from India, is the central sales Tax Act of 1956. The primary objective of the Act is to provide for the levy, collection and distribution of taxes on sale of goods in the course of inter-state trade or commerce and to declare certain goods to be of special importance in inter-state trade or commerce, and specify the restrictions and conditions to which laws imposing taxes on the sale or purchase of such goods of special importance.

7.3.2 Value Added Tax

Value Added Tax (VAT) is a modern and progressive form of sales tax. It is charged and collected by dealers on the price paid by the customer. VAT paid by dealers on their purchase is usually available for set-off against the VAT collected on sales. VAT applies to all types of businesses including

- Importers
- Manufactures
- Distributors
- Wholesalers
- Retailers
- Works Contractors
- Lessors

There are four main rates of VAT.

- 4% for items consisting mainly of raw materials used in the manufacturing process, its products and some goods of common consumption.
- 12.5% for all goods unless they are listed under the other rates. Food grains including pulses, milk, vegetables and books are not subject to VAT.
- 1% for gold, silver, other precious metals, precious and semi-precious stones and their jewellery.
- 20% for liquor. The only exception to these rates is for the sale of motor spirits, which have special tax rates based on the existing Bombay Sales of Motor Spirit Taxation Act, 1958, subject to a floor rate of 20%.

7.3.3 Central Excise Duty

Excise duty is levied on the production or manufacture of those goods which are manufactured or produced in India and which are subject to excise duty. It is levied by the central government. It is an indirect tax which is recovered from the producers and manufactures and which has nothing to do with the sale and purchase of goods.

7.3.4 Central Value Added Tax (CENVAT)

CENVAT refers to that duty which is payable by a tax payer on the value added to the goods by him during the production. He has to pay excise duty not on the final value of the finished product but only on that value which he has added to the raw material he purchased.

7.3.5 Service Tax

According to the Service Tax Act, a tax @ 12% shall be levied on the value of all taxable services. The value of taxable services shall be the gross amount charged by the service provider for such service provided or to be provided by him. An education cess of 2% on 12% service tax is also charged.

7.3.6 Fringe Benefit Tax (FBT)

The taxation of perquisites or fringe benefits provided by an employer to his employees, in addition to the cash salary or wages paid, is fringe benefit tax. Any benefits or perks that employees (current or past) get as a result of their employment are to be taxed, but in this case in the hands of the employer. This includes employee compensation other than wages, tips, health insurance, life insurance and pension plans.

Fringe benefits mean any privilege, service, facility or amenity directly or indirectly provided by an employer to his employees (including former employees) by reason of their employment. They also include reimbursements made by the employer either directly or indirectly to the employees for any purpose, contributions by the employer to an approved superannuation fund as well as any free or concessional tickets provided by the employer for private journeys undertaken by the employees or their family members.

7.3.7 Banking Transaction Tax

The Finance Act 2005 introduced the banking cash transaction tax. Taxable banking transaction has been defined to mean

(i) Transaction being withdrawal of cash (by whatever mode) on any single day from an account (other than a savings bank account) by a person from scheduled bank exceeding
- Rs 20,000 in case the cash withdrawn is from an account of an individual or an HUF.
- Rs one lakh, in case the withdrawal is from an account of a person other than an individual or an HUF.

(ii) A transaction being receipt of cash from any scheduled bank on any single day by a person on encashment of term deposit, whether on maturity or otherwise, from that bank exceeding
- Rs 25,000 if such deposits are in the name of an individual or an HUF.
- Rs one lakh in case such term deposit or deposits are by any person other than any individual or HUF.

The law provides for the taxability, from 1 June 2005, in respect of the taxable banking transactions, at the rate of 0.1% of the value of such transaction.

Key Words Used In This Chapter

- Direct Taxes
- Indirect Taxes
- Bargaining
- Assessment Year
- Financial Year
- Assessee
- Calender Year
- Accounting Year
- Persons
- Resident Status
- Resident
- Resident but not ordinarily resident
- Central Sale Tax (CST)
- Central Value Added Tax (CENVAT)
- Individual
- Allowances

- Perquisites
- VAT (Value Added Tax)
- Reimbursement
- Licence

Summary with Reference to Learning objectives

1. **Classification of Taxes**
   - (a) **Direct Tax** to paid by a person on whom it is legally imposed and includeS Income Tax.
   - (b) **Indirect Tax** to paid by another person and not by the person on whom it is legally imposed. It include Sales Tax, Excise Duty, Service Tax, Value Added Tax etc.
2. **Assessment year :** The year in which the income of previous year (1 April to 31 March) is assessed for income tax purpose.
3. Perquisites are additional allowances with the actual pay provided by the employer to employees. It may be in cash or kind.
4. **Assessee :** A person who is liable to pay any tax on his income.
5. **VAT :** It is charged or collected by dealers on the price paid by a customer.

Questions for Practice

Short Answer questions

1. Classify Taxes.
2. Explain the meaning of
   - (i) Calendar year
   - (ii) Previous year
   - (iii) Financial year
   - (iv) Assessment year
3. Who is an assessee?
4. Discuss the meaning of bargaining.
5. What are perquisites?
6. Classify the residential status of an individual.
7. Describe the meaning of allowance.
8. What type of taxes are included in direct Taxes?
9. What type of taxes are included in indirect taxes?
10. Discuss the meaning of VAT.

Long Answer questions

1. Explain the meaning of direct taxes with appropriate examples.
2. Define person as per Section 2(31) of income Tax Act.
3. Who is an assessee as per sec 2(7) of Income Tax Act?
4. What is legal residential status of an individual as per section 6(1) of income Tax act?
5. Which incomes are included in Salary head as per Sec-15 of Income Tax Act.?
6. Explain indirect taxes briefly.
7. Explain Banking Transaction Tax.

Practical Questions

Q1. Aslam's salary is Rs 26,000 per month. He contributed Rs 54,000 towards GPF and PPF during the year. He also purchased NSC's worth Rs 16,000. He donated. Rs 8,000 to a charitable trust, thus earning a deduction of 50% on the donation. Calculate income tax to be paid by him.

[Ans. Rs 52,395]

Q2. Anil's salary is Rs. 50,000 per month. He contributes Rs 3,000 per month towards PF and pays Rs 15,000 as annual LIC premium. He invests Rs.14,000 in NSC's. He contributes Rs 8,000 towards P.M.'s National Relief Fund and also donates Rs. 5,000 to the school where he studied, earning deductions of 100% and 50% on the amount donated respectively. Find the total income tax to be paid by him for the year.

[Ans. Rs. 158,393]

Q3. Naaz's monthly salary is Rs 19,250. She contributes Rs 2,500 per month towards GPF and 20,000 in PPF. She donates Rs 11,000 to a school and gets a relief of 50% on the donation. Calculate the income tax deducted from her salary in the last month of the year if tax deduction is made from her salary for 11 months at the rate of Rs 1,700 per month.

[Ans. Rs. 4,033]

Q4. Sujatha gets monthly salary of Rs 30,000. She contributes Rs. 3,000 per month to GPF and Rs 34,000 towards PPF. She also invests Rs 30,000 in Infrastructure Bonds getting tax relief upto a saving of Rs 1,00,000 . She contributes Rs 11,000 to P.M.'s National Relief Fund and donated Rs 5,000 to the college where she studied, getting a relief of 100% and 50% on the donation respectively. If Rs 4,500 is the tax deducted each month from her salary for 11 months, find the tax deducted from her salary in the last month of the year.

[Ans. Rs. 5,048]

Q.5 The annual income of Ms Nisha for the year is Rs 2,40,000 (including HRA). She contributes Rs. 5,000 as annual premium to LIC and Rs 4,000 per month to G.P.F. Further she invests Rs 5,000 in N.S.C. She donates Rs 4,000 to Prime Minister's Relief Fund earning 100% relief. Compute the income tax payable by Nisha.

Use the following information for calculating income tax.

(a.) Savings: 100% exemption for permissible savings upto Rs 1,00,000.

(b.) Rate of Income Tax for ladies

	Slab	**Income Tax**
(i)	Upto Rs 1,35,000	No tax
(ii)	From Rs 1,35,001 to Rs 1,50,000	10% of the taxable income exceeding Rs 1,35,000
(iii)	From Rs 1,50,0001 to Rs 2,50,000	Rs 1500 + 20% of the amount exceeding Rs 1,50,000
(iv)	From Rs 2,50,0001 and above	Rs 21,500+ 30% of the amount exceeding Rs 2,50,000

(c.) Educational cess — 2% of the income tax

Q6 Annual income from salary of Mrs Usha, who is a senior citizen, is Rs 3,85,000. She donates Rs 10,000 to Prime Minister's Relief Fund (100% exemption) and Rs 10,000 to a Charitable Society (50% exemption). She contributes Rs 70,000 towards PPF annually and pays a quarterly premium of Rs 3,500 towards Life Insurance. She also purchases NSC for Rs 2,000. She pays Rs 1,600 per month towards income tax for 11 months. What is the tax liability for the last month of the financial year?

Use the following for calculating income tax.

(a.) Savings : 100% exemption for savings upto Rs 1,00,000

(b.) Rate of income tax for senior citizens

	Slab	Income Tax
i)	Upto Rs 1,85,000	No tax
ii)	From Rs 1,85,001 to Rs. 2,50,000	20% of the taxable income above Rs 1,85,000
iii)	From Rs 2,50,001 and above	Rs.13,000 + 30% of the income exceeding Rs 2,50,000

(c.) Education Cess : 2% of the income tax

Q6. Sunit's annual income is Rs 3,65,000 per annum (HRA excluded). He contributes Rs 7,000 per month towards his provident fund and pays premium of Rs. 20,000 p.a. on his LIC policy. In addition, he invests Rs. 30,000 in NSC. If Rs. 2,200 be the tax deducted each month from his salary for 11 months, calculate the tax deducted from his salary in the last month of the year.

Use the following for calculating the tax.

(a) Savings : 100% exemption for permissible upto Rs 1,00,000.

(b) Rate of Income tax

Slab	Income Tax
From Rs 1,00,001 to Rs 1,50,000	10% of the taxable exceeding Rs 1,00,000.
From Rs 150,001 to Rs 2,50,000	Rs 500 + 20% of the taxable Income exceeding Rs 1,50,000
Rs 2,50,001 and above	Rs 25,000 + 30% of the taxable Income exceeding Rs 2,50,000

(c) Education Cess : 2% of the income tax.

CENTRAL BOARD OF SECONDARY EDUCATION

Shiksha Kendra, 2, Community Centre, Preet Vihar, Delhi - 110092, India
Tel.: 91-11-22509252-59 Fax : 91-11-22515826
E-mail : cbseedusat12@rediffmail.com website : www.cbse.nic.in