Study Material

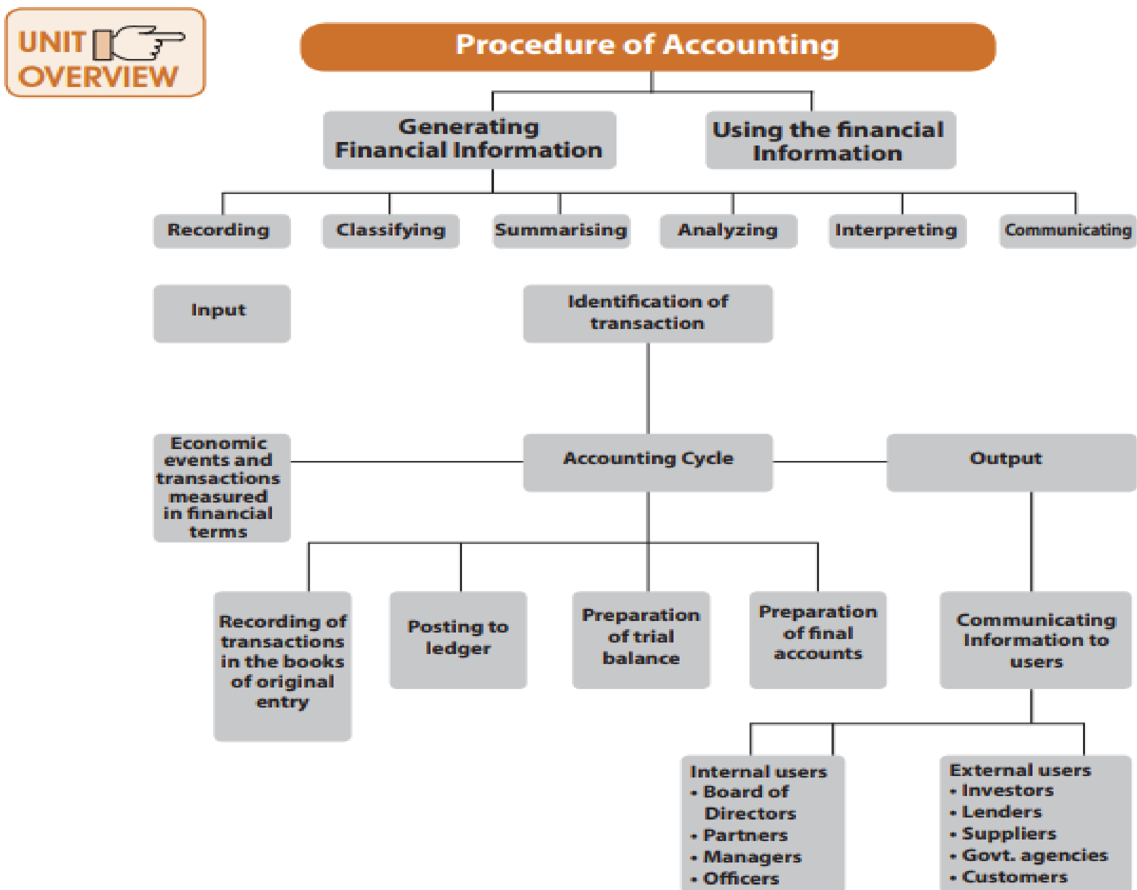
Financial Accountancy

UNIT – 1

FINANCIAL ACCOUNTING

Objectives:

The need of scientific accounting being focal point in the day today business, the fundamental accounting concept is introduced with double entry book keeping. The basics of accounting system such as maintenance of journal, ledger, cash book and trial balance are taught. The final accounts of trading and non-trading concerns are explained with examples to enable the students appreciate the principles of Accountancy.



Every individual performs some kind of economic activity. A salaried person gets salary and spends to buy provisions and clothing, for children's education, construction of house, etc. A sports club formed by a group of individuals, a business run by an individual or a group of individuals, a local authority like Calcutta Municipal Corporation, Delhi Development Authority, Governments, either Central or State, all are carrying some kind of economic activities. Not necessarily all the economic activities are run for any individual benefit; such economic activities may create social benefit i.e. benefit for the public, at large. Anyway such economic activities are performed through '**transactions and events**'. **Transaction** is used to mean 'a business, performance of an act, an agreement' while event is used to mean 'a happening, as a consequence of transaction(s), a result.'

An individual invests ₹2,00,000 for running a stationery business. On 1st January, he purchases goods for ₹ 1,15,000 and sells for ₹ 1,47,000 during the month of January. He pays shop rent for the month ₹ 5,000 and finds that still he has goods worth ₹ 15,000 in hand. The individual performs an economic activity. He carries on a few transactions and encounters with some events. Is it not logical that he will want to know the result of his activity?

Accountancy is the practice of recording, classifying, and reporting on business transactions for a business. It provides feedback to management regarding the financial results and status of an organization.

Meaning of Accounting

Lucas Pacioli is considered to be the Father of modern bookkeeping. The only recording of financial transactions in bookkeeping is not enough to achieve the commercial objective, but also it is important to know the financial result.

Definitions of Accounting

- Some prominent definitions of accounting to help us better understand the meaning of basic accounting.
- *According to the Committee of Terminology of American Institute of Certified Public Account:*" **Accounting is the art of recording, classifying summarizing in a significant manner and in terms of money, transaction, and events which are, in part at least of a financial character and interpreting the results thereof."**

- *According to Bierman and Drebin:*" Accounting may be defined as identifying, measuring, recording and communicating of financial information."

NEED FOR ACCOUNTING

- It is not possible for a human being to remember all the transactions which occur during a year.
- As a result of above it will not be possible to ascertain the correct results and financial position unless a record of all transactions are made
- To indicate the earning capacity and financial position of concerned business unit.
- To satisfy government and income tax authorities
- To assist management in decision making.
- To depict true position of a business as a whole.

Objectives & Advantages of Accounting

- To know the profit or loss of the business
- To know the assets and liabilities of the business on a particular date
- To know what amount is payable to any person or what amount is receivable from any person
- To know the quantity and value of stock
- To know errors and frauds committed by the employees
- To satisfy the taxation authorities

USERS OF ACCOUNTING INFORMATION

- 1) Management or Managers
- 2) People with direct financial interest
- 3) People with indirect financial interest

Limitations

- 1. It records only Monetary Transactions
- 2. Effect of Price Level Change are not recorded – example of a fixed asset
- 3. Historical in Nature

- 4. Unrealistic Information – Accounting concepts and Conventions- Going Concern
- 5. No real test of Managerial Performance – Can conceal profit
- 6. Permits alternatives Treatments
- 7. Personal bias of the Accountant

Accounting Principles

- Accounting Principles are man made and therefore do not have the authoritativeness as universal principles like physics or chemistry. They are mere best possible guidelines based on reason and observation.
- Accounting a social science
- 1) Accounting Concepts
- 2) Accounting Conventions

Accounting Concepts

- 1) Money Measurement Concept
- 2) Business Entity Concept
- 3) Going Concern Concept
- 4) Cost Concept
- 5) Dual Aspect Concept
- 6) Accounting Period Concept
- 7) Matching Concept
- 8) Realisation Concept
- 9) Accrual Concept
- 10 Objective Evidence Concept
- **Matching** principle is the **accounting** principle that requires that the expenses incurred during a period be recorded in the same period in which the related revenues are earned. This principle recognizes that businesses must incur expenses to earn revenues.

Conservatism

- **:** Playing it safe is both an accounting principle and convention. It tells accountants to err on the side of caution when providing estimates for assets and liabilities. That means that when two values of a transaction are available, the lower one should be favored. The general concept is to factor in the worst-case scenario of a firm's financial future.

  Provide for all possible losses and anticipate no Gain.

Consistency

A company should apply the same accounting principles across different accounting cycles. Once it chooses a method it is urged to stick with it in the future, unless it has a good reason to do otherwise. Without this convention, investors' ability to compare and assess how the company performs from one period to the next is made much more challenging.

Full disclosure:

- Information considered potentially important and relevant must be revealed, regardless of whether it is detrimental to the company.

Accounting Standards

- Accounting Standards are guidelines laid down by the expert Accounting Body as to how business transactions are to be recorded in the books of accounts and the manner in which business transactions are to be exhibited in the financial statements. Accounting standards provide rules, regulations and guidelines that should be observed while preparing the accounts and presentation of financial Information.

Importance of Accounting Standards

- 1. They laydown uniform accounting policies and practices that should be followed by all business organization, in respect of particular transaction.
- 2. They enable easy comparability of financial statements of various business organization as uniform accounting standards are followed by all
- 3. Financial Statements prepared as per the guidelines laid down by the ASB are more accurate and reliable
- 4. As accounting standard are formulated and issued by apex expert accounting body in country, they are scientific and rational
- 5. They increase and improve the credibility and reliability of accounting information.

- 6. They curb unlimited flexibility in the adoption of accounting policies and practices.
- 7. The financial Statements prepared as per Accounting Standard would be useful to investors in judging the yield and risk involved in alternative investment in different companies
- 8. Accounting reports prepared as per Accounting Standards are regarded by Govt Officials, Income tax authorities etc. as reliable and acceptable.

List of Accounting Standards

- IAS (International Accounting Standards)
- Indian Accounting Standards (Ind AS)

Indian Accounting Standards

- Accounting Standard 1 : Disclosure of Accounting Policies
  Accounting Standard 2 : Valuation of Inventories
  Accounting Standard 3 : Cash Flow Statements
  Accounting Standard 4 : Contingencies and Events Occurring after the Balance Sheet Date
  Accounting Standard 5 : Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
  Accounting Standard 6 : Depreciation Accounting
  Accounting Standard 7 : Construction Contracts
  Accounting Standard 8 : (Deleted)
  Accounting Standard 9 : Revenue Recognition
  Accounting Standard 10 : Property, Plant and Equipment
- Accounting Standard 11 : The effects of changes in Foreign Exchange Rates
  Accounting Standard 12 : Accounting for Government Grants
  Accounting Standard 13 : Accounting for Investments
  Accounting Standard 14 : Accounting for Amalgamations
  Accounting Standard 15 : Employee benefits
  Accounting Standard 16 : Borrowing Costs
  Accounting Standard 17 : Segment Reporting
  Accounting Standard 18 : Related Party Disclosures
  Accounting Standard 19 : Leases
- Accounting Standard 20 : Earnings Per Share
  Accounting Standard 21 : Consolidated Financial Statements

Accounting Standard 22 : Accounting for Taxes on Income
Accounting Standard 23 : Accounting for Investments in Associates in Consolidated Financial Statements
Accounting Standard 24 : Discontinuing Operations
Accounting Standard 25 : Interim Financial Reporting
Accounting Standard 26 : Intangible Assets
Accounting Standard 27 : Financial Reporting of Interest in Joint Ventures
Accounting Standard 28 : Impairment of Assets
Accounting Standard 29 : Provisions Contingent Liabilities and Contingent Assets
Accounting Standard 30 : Financial Instruments : Recognition and Measurements*
Accounting Standard 31 : Financial Instruments : Presentation*
Accounting Standard 32 : Financial Instruments : Disclosures*

- ** AS-30, AS-31, AS-32 are not mandatory as these have not been notified under Companies Accounting Standards Rules, 2006*

Indian Accounting Standard

- IAS are converged standards for IFRS (International Financial Reporting Standards). These are popularly known as Ind AS. Indian Accounting Standard provides principles for recognition, measurement, treatment, presentation and disclosures of accounting transactions in financial statements prepared as per Indian Accounting Standard.
- For example: Indian Accounting Standard 38 on Intangible asset will provide principles regarding recognition of intangible asset, what all cost will form part of such asset, how to treat those cost and how to present intangible asset in the financial statement and relevant disclosures.

Cash Flow Statement

- What Is a Cash Flow Statement?
- A cash flow statement is a financial statement that provides aggregate data regarding all cash inflows a company receives from its ongoing operations and external investment sources. It also includes all cash outflows that pay for business activities and investments during a given period.

AS 4: Contingencies & Events After Balance Sheet Date

- Contingencies
- Events occurring after the balance sheet date

- Further, there are certain subjects which can lead to contingencies. However, these issues are outside the scope of this accounting standard on account of special considerations that apply to them. These include:
- Liabilities of Life Assurance and General Insurance enterprises resulting from policies issued
- Obligations under Retirement Benefit Plans
- Commitments arising from long term lease contracts

Accounting Standard 5 (AS 5)

- Accounting Standard 5 (AS 5) deals with the classification and disclosure of specific items in the Statement of Profit and Loss.
- The purpose of AS 5 is to suggest such a classification and disclosure in order to bring uniformity in the preparation and presentation of statement of net profit or loss across enterprises.
- This enables the enterprises to compare their financial statements over time as well as draw comparison of their financial statements with other enterprises.
- Thus, the statement of net profit or loss requires:
- Disclosure of certain items within profit or loss from ordinary activities
- Classification and disclosure of extraordinary and prior period items
- Accounting treatment and disclosure for changes in the accounting estimates
- Disclosure of changes in the accounting policies

AS – 6 DEPRECIATION ACCOUNTING

Depreciation is a measure of the wearing out, consumption or other loss of value of a depreciable asset arising from use, passage 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. Depreciation includes amortisation of assets whose useful life is predetermined.

Depreciable assets are assets which

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[1] are expected to be used during more than one accounting period; and
[2] have a limited useful life; and
[3] are held by an enterprise for use in the production or supply or for administrative purposes.

Depreciable amount of a depreciable asset is its historical cost, or other amount substituted for historical cost less the estimated residual value.

AS 9 Revenue Recognition

- As per the AS 9 Revenue Recognition issued by ICAI "Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, rendering of services & from various other sources like interest, royalties & dividends"

AS 10 Property, Plant and Equipment

- AS 10 Property, Plant and Equipment prescribe the accounting treatment for properties, P&E (Plant and Equipment) so that the users of financial statements could recognize and appreciate the information about the investment made by any enterprise in property, P&E and the also understand the changes made in such investments.

- It is also important to note that AS 6 – Accounting for Depreciation stands withdrawn and such matters related to depreciation is included in AS 10.

Accounting for Amalgamations

1. This standard deals with accounting for amalgamations and the treatment of any resultant goodwill or reserves. This Standard is directed principally to companies although some of its requirements also apply to financial statements of other enterprises.
2. This standard does not deal with cases of acquisitions which arise when there is a purchase by one company (referred to as the acquiring company) of the whole or part of the shares, or the whole or part of the assets, of another company (referred to as the acquired company) in consideration for payment in cash or by issue of shares or other securities in the acquiring company or partly in one form and partly in the other. The distinguishing feature of an acquisition is that the acquired company is not dissolved and its separate entity continues to exist.

Bookkeeping

- Bookkeeping involves the recording, on a daily basis, of a company's financial transactions. With proper bookkeeping, companies are able to track all information on its books to make key operating, investing, and financing decisions.

- Bookkeepers are individuals who manage all financial data for companies. Without bookkeepers, companies would not be aware of their current financial position, as well as the transactions that occur within the company.
- Accurate bookkeeping is also crucial to external users, which includes investors, financial institutions, or the government – people or organizations that need access to reliable information to make better investments or lending decisions. Simply put, the entire economy relies on accurate and reliable bookkeeping for both internal and external users.

Objectives of book keeping

- To have permanent record of all the business transaction
- To show the effect of each business transaction and combined effect of all transactions on the financial position of the trader
- -to find profit or loss during a particular period
- To ascertain financial position as on a date
- To know how much he owes to others and how much others owe him
- To know his incomes, expenses, losses , gains assets and liabilities

Distinction between Book keeping and Accounting

- One of the sub divisions of accounting is book keeping . .Book keeping refers to recording financial transactions of a business in a systematic manner so that information on point
- 1) Book keeping is refers to recording of business transaction in an orderly manner Bookkeeping refers to recording of business transaction in an orderly manner, in the journal or subsidiary books or posting them to ledger accounts.
- accounting on the other hand involves not only recording of transactions but presenting the same in the form of financial statements and interpret in the same for forming judgments. Accounting therefore is more analytical
- A book keeper only maintains information about a business, in a set of books but an account and analyses the same so accounting begins where bookkeeping ends. Bookkeeping act as basis for accounting

- Accounting includes the design of accounting system preparation of financial statements and Audit development of forecast cost studies Income Tax works analysis and interpretation of accounting information

Branches of accountancy

Accounting has three branches

1) financial accounting

2) cost accounting number

3) Management Accounting

Financial Accounting

Financial accounting it is concerned with the preparations of accounts. Such accounts enable the management to prepare the financial statements showing a profit or loss for a particular period and the financial state of affairs on a particular day . Financial accounting therefore provides information to the managers of the business shareholders suppliers customers employees the government and the public in general

Cost accounting.

It is concerned with classification recording allocation and summarization of current and prospective costs. Cost accounting enables the ascertainment of the total cost of any particular unit of a production or service, with reasonable degree of accuracy it discloses what constitutes cost and thus helps in controlling or reducing cost.

Management Accounting

it refers to the use of accounting data collected with the help of cost and financial accounting for the purpose of planning controlling decision making and formulating policies by the management accounting presents to the management accounting information in the form of process data with the help of which proper decisions are taken.

Relationship of accountancy with other disciplines

- Accountancy and economics
- Enquire about the money that one earns and the way in which it is spent by him.As against this, an account and maintains and records all the transactions of an individual or firm or Association or a company. Naturally therefore, II both should know each others subject. An account and will understand his subjects but if he can understand economic concepts like value, cost of production, production cost etc. Similarly an economist will

understand his subjects better if he is aware of accounting concepts. therefore accountancy and economics are related to each other

Accountancy and Engineering

an accountant and an engineer associated with the production unit of An engineering form work together to solve several day today problems. The figures and values which and engineered uses for preparing his statements and Designs are presented in different accounting reports which are prepared by the accountant naturally there for for performing his duties properly an accountant should possess some knowledge of engineering and an engineered wood for some knowledge of accounting in this way engineering and accountancy are related.

Accountancy and law

most of the accounting functions can be performed only with the sound knowledge of law. Accounts of a partnership firm or a joint stock company can be maintained only if the concerned acts are known. Likewise an accountant should have sufficient knowledge of sale of goods act the sales tax Act and the Income Tax Act

UNIT – 2

JOURNAL

A JOURNAL ENTRY records a business transaction in the accounting system for an organization. Journal entries form the building blocks of the double-entry accounting method that has been used for centuries to keep financial records. They make it possible to to track what a business has used its resources for, and where those resources came from.

The double-entry accounting method requires every transaction to be recorded in at least two accounts. For example, when a business buys supplies with cash, that transaction will show up in the supplies account and the cash account.

A journal entry has these components:

- The date of the transaction
- The names of the accounts impacted plus the account number, where relevant
- The amounts to be credited and debited
- A reference number that serves as a unique identifier for the transaction
- A description of the transaction

Under the double-entry bookkeeping method, debits and credits in a journal entry must be equal. Journal entries must also be consistent with the general accounting equation which describes the balance sheet:

Assets = Liabilities + Owner's Equity

Using this equation, debits are recorded on the left, and credits on the right. This means that debiting an account on the left side of the equation — an asset account — increases that account. Debiting an account on the right side of the equation — a liability or an equity account — will decrease the balance in that account.

A credit amount has the opposite effect. Crediting an asset account decreases the balance, while crediting a liability or equity account increases it. Over on the income statement, revenue accounts are increased by credits, and expense accounts are increased by debits.

Type of Account	Golden Rules
Real Account	*Debit what comes into the business *Credit what goes out from the business
Personal Account	*Debit the receiver *Credit the giver
Nominal Account	*Debit the expense or loss of the business *Credit the income or gain of the business

The Three Golden Rules of Accounting – Real, Personal and Nominal Accounts

Traditional Approach consists of rules popularly known as the Three Golden Rules of Accounting. These rules are applicable irrespective on all categories of the transaction. These three most talked about and basic Golden rules of accounting are to make debit and credit in accounting ledger by categorising each and every transaction or entry into either

Real

Personal or

Nominal Accounts

Now let us take each accounting rule in detail.

Real Account

Real Accounts is a set of tangible aspects of business like furniture, cash, etc.

- If the item that belongs to the real account is coming into the business then while making the accounting entries it should be written on the Debit side.
- If the item of real account is going out of the business then while making the accounting entries it should be written on the Credit side.

Personal Accounts

- If the person/ group of persons/ legal body is receiving something from the business then – Debit the receiver

- If the person/ group of persons/ legal body is paying something to the business – Credit the payer or giver

Nominal Accounts

Nominal Accounts represents all the Expenses, Loses, Income and gains incurred while doing business.Some common e.g. are,

- Electricity Expenses,
- Telephone Expenses,
- Interest Received,
- Profit on Sale of Machines, etc.

If it's an expense or loss for the business – Debit
If it's an income or gain for the business – credit

The above three golden rules can be better decoded with the help of some illustrative accounting transactions like:

- Goods amounted to Rs. 15000 purchased from Mr. Mohan on Credit
- Cash paid to Mr. Mohan for credit purchases
- Goods sold to Mr. Rehman for Rs. 20000
- Rs. 10000 withdrawn from the bank
- The machinery of Rs. 50000 purchased from M/s Bharti Traders and paid Rs. 25000 in cash and remaining to be paid on the future date.
- Balance amount of Rs. 25000 to M/s Bharti Traders is paid in full
- Machinery is sold to John for Rs. 55000.

Transactions	Accounts Involved	Types of Accounts
Goods Purchased from Mr. Mohan on Credit	Mr. MohanInventory (Stock)	Personal AccountReal Account
Cash paid to Mr. Mohan	Mr. MohanCash	Personal AccountReal Account
Goods sold to Mr. Rehman	BankInventory (Stock)	Real AccountReal Account
Cash withdrawn from Bank	CashBank	Real AccountReal Account
Machinery Purchased from M/s Bharti Traders	M/s Bharti TraderMachineryBank	Personal AccountReal AccountReal Account
Cash paid to M/s Bharti Traders	M/s Bharti TraderCash	Personal AccountReal Account
Machinery Sold to John at a Profit	JohnMachineryGain on sale of Machine	Personal AccountReal AccountNominal Account

Goods amounted to Rs. 15000 purchased from Mr. Mohan on Credit

The Golden rule for Real and Personal Accounts:

- a) Debit what comes in
- b) Credit the giver

The Journal entry will be:

Inventory A/c	Dr.	15000	
To Mr. Mohan			15000

Cash paid to Mr. Mohan for credit purchases

The Golden rule for Real and Personal Accounts:

- a) Debit what comes in
- b) Credit the giver

The Journal entry will be:

Mr. Mohan	Dr.	15000	
To Cash A/c			15000

Goods sold to Mr. Rehman for Rs. 20000 in cash

The Golden rule for Real and Real Accounts:

- a) Debit what comes in
- b) Credit what Goes out

Bank A/c	Dr.	20000	
To Inventory			20000

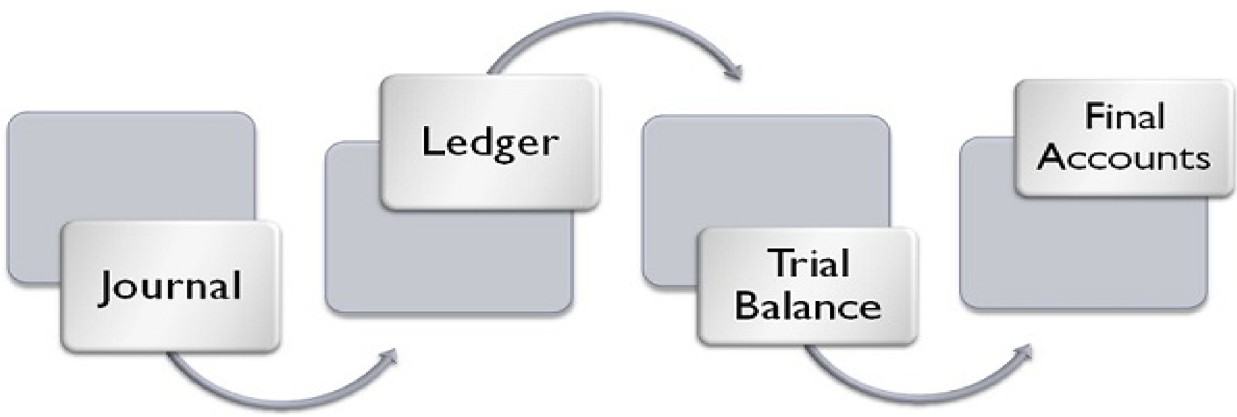
FORMAT OF JOURNAL ENTRY AND AN EXAMPLE

Transactions	Accounts involved	Nature of accounts	How affected in business	Debit / Credit
Withdrew cash for personal use ₹ 8,000	Drawings A/c Cash A/c	Personal A/c Real A/c	Propreitor is the receiver Cash goes out	Debit Credit

Journal entry

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Drawings A/c Dr.		8,000	
	To Cash A/c			8,000
	(Cash withdrawn for personal use)			

LEDGER



- Double entry system of bookkeeping says that every transaction affects two accounts. There is a proper procedure for recording each financial transaction in this system, called as accounting process
- .The process starts from journal followed by ledger, trial balance, and final accounts. Journal and Ledger are the two pillars which create the base for preparing final accounts. The **Journal** is a book where all the transactions are recorded immediately when they take place which is then classified and transferred into concerned account known as **Ledger**.

MEANING OF LEDGER

- Ledger is a book which contains accounts.
- It is a book in which various accounts are opened and maintained.
- The word Ledger has its origin from Dutch word called "Legger". Which means to lie, So, Ledger means a book where various accounts lie. It contains all types of accounts – Real, Personal and Nominal.

Features of Ledger

- 1) It is book where similar transactions are brought together in one place. It is therefore an analytical record of transactions.
- It is usually prepared after journal and therefore it is a secondary or derived record
- It is a book of final entry , in the sense that all transactions finally find their place in the ledger.
- It is the most important book for businessmen, as it is from the ledger that a trial balance can be prepared and from the trial balance final accounts are prepared. Because of the importance of ledger, it is called the King of books of accounts.
- Ledger serves as a permanent record of transactions

Need and importance of ledger

- Hundreds of transactions takes place everyday. A book called journal is maintained in which transactions are recorded as and when they occur. Naturally, journal cannot give the net effect of similar transactions on any particular date.
- The ledger makes up this shortcoming of the journal. In the ledger , Transactions of similar nature are written in one place called an account.
- Thus, all transactions relating to cash are written in the Cash Account, rent paid over year are entered in the Rent account so on.

Importance of Ledger arises from the fact that it answers the following Questions

- 1) What are the purchases made during the year
- 2) What are the total purchases from an individual supplier during a particular period
- 3)What are the sales during the period
- 4) What are the sales to a particular Individual

- 5)How much is owed to others
- 6) What is final position of the firm on a given particular date

Difference between JOUNRAL AND LEDGER

BASIS FOR COMPARISON	JOURNAL	LEDGER
Meaning	The book in which all the transactions are recorded, as and when they arise is known as Journal.	The book which enables to transfer all the transactions into separate accounts is known as Ledger.
What is it?	It is a subsidiary book.	It is a principal book.
Also known as	Book of original entry.	Book of second entry.
Record	Chronological record	Analytical record
Process	The process of recording transactions into Journal is known as Journalizing.	The process of transferring entries from the journal to ledger is known as Posting.
How transactions are recorded?	Sequentially	Account-wise
Debit and Credit	Columns	Sides
Narration	Must	Not necessary.
Balancing	Need not to be balanced.	Must be balanced.

FORMAT OF LEDGER ACCOUNT

Dr. Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)

TRIAL BALANCE

Meaning and Features

- Its already been seen that in double entry system every debit has equal and corresponding credit.
- Trial Balance is a statement containing the balances of all ledger accounts, as at any given date, arranged in the form of debit and credit columns, placed side by side and prepared with the object of checking the arithmetical accuracy of ledger posting.

Purpose of Trial Balance

- 1) A trial Balance makes a list of all accounts in one place. This will help in finding out of the balance of any accounts easily, without going through ledger.
- 2) The agreement of Trial Balance will mean that books of accounts are reasonably be reliable

Features of Trial Balance

- Trial Balance is only a statement and not an account
- It is prepared as on a particular date and not for a particular period.

- It is usually prepared at the end of a year so that the preparation of final accounts can be proceeded with easily. The Trial balance can however be prepared at the end of any period,,,say a month or a quarter.
- It shows various accounts maintained by the business organization concerned as also the balance it has
- It helps check the arithmetical accuracy of the books of accounts
- Mere agreement of trial balance is no proof of correctness of the books of accounts because trial balance does not reveal certain types of errors.

Objectives of Trial Balance

- Since, Trial Balance is list of balances of various accounts , it helps in finding out the balance on any particular date
- IT is prepared to check whether books of accounts are maintained properly, if trial balance agrees it may be assumed that the books of accounts are properly maintained
- It helps to locate errors. A disagreement of trial balance is an indication that there are errors and they be located and corrected before preparation of final accounts.
- Helps in preparation of Final Accounts

Limitations of Trial Balance

- A transaction that is completely missing, was not even journalized.
- When the wrong amount was written in both the accounts.
- If a posting was done in the wrong account but in the right amount.
- An entry that was never posted in the ledger altogether.
- Double posting of entry by mistake.

FORMULA TO REMEMBER TRIAL BALANCE

- Debit – Assets, expenses and losses
- Credit – Liabilities , Incomes and gains

FORMAT OF TRIAL BALANCE

WITH AN EXAMPLE

NSBHandicraft

Trial Balance as on March 31st, 2019

Sr.No.	Particulars	Amount (INR)	
		Dr.	Cr.
1	Bill Payable		5,000
2	Insurance Charges	5,000	
3	Owner Investments		80,000
4	Unearned Revenue		4,000
5	Bank Loan		25,000
6	Marketable Security	10,000	
7	Accumulated Depreciation- Equipment		14,000
8	Depreciation Expenses – Equipment	3,000	
9	Rent	15,000	
10	Outstanding Salaries		5,000
11	Machinery	30,000	
12	Prepaid Rent	4,000	
13	Sundry Debtors	15,000	
14	Accrued Revenue	20,000	
15	Unexpired Insurance	10,000	
16	Vendor Payable		4,000
17	Drawings	2,000	
18	Equipment	20,000	
19	Maintenance Expenses	3,000	
20	Accrued Expenses		1,000
21	Mics Expenses	2,000	
22	Sales		42,250
23	Purchase	30,000	
24	Taxes	11,250	
	Total	**1,80,250**	**1,80,250**

EXAMPLE 2

Trial Balance XYZ Trading as at 30 June 2010		
General Ledger Accounts	[Dr.-Debit]	[Cr.-Credit]
Cash at bank	10,000	
Inventory	40,000	
Vehicles	30,000	
Fixtures & Fittings	32,000	
Accounts Receivable	15,000	
Credit Cards payable		12,000
Accounts Payable		15,000
Bank Loan		50,000
Sales		175,000
Purchases	60,000	
Advertising	5,000	
Wages	65,000	
Rent	15,000	
Electricity	5,000	
Owners Capital		25,000
TOTAL	**277,000**	**277,000**

EXAMPLE 3

Trial Balance Showing Closing Stock

S.No.	Heads of Accounts	LF.	Debit	Credit
1	Purchases A/C		xxxx	
2	Salaries A/C		xxxx	
3	Land & Building A/C		xxxx	
4	Cash A/C		xxxx	
5	Capital A/C			xxxx
6	Opening Stock		xxxx	
7	Sales A/C			xxxx
8	Bank A/C		xxxx	
9	Rent A/C		xxxx	
10	Carriage Inwards		xxxx	
11	Carriage Outwards		xxxx	
12	Bad Debts		xxxx	
13	Investments		xxxx	
	Total		**xxxx**	**xxxx**

3 COLUMN CASH BOOK

POINTS TO NOTE WHILE PREPARING 3 COLUMN CASH BOOK

- 1. A Cheque or bank draft received on a particular day not deposited into the bank on the same day, should be treated as cash received and entered in the cash columns
- **“TO Concerned head of the accounts”**
- 2. A Cheque or bank draft received on a particular day, if deposited into the bank same day , has to be entered into the bank column on the debit side.
- 3. Cheque or bank draft received by someone into our bank account should be entered in the bank column on debit side.

CONTRA ENTRY

- A cheque received on any previous day deposited into the bank will result in 2 entries in the cash book
- On the credit side of the cash book an entry should be made showing reduction of cash as “**BY BANK A/C” (Amount is naturally put into cash column”) . Secondly in the debit side of the cash book in the bank column should be recorded the receipt side of the cash by bank column on each side against the entry. This indicates that an entry appears both side of the cash book.**

FORMAT OF THREE COLUMN CASH BOOK

Page No:___

Dr. (Receipts) **CASH BOOK** **Cr. (Payments)**

Date	Description	VN	PR	Disc	Cash	Bank	Date	Description	VN	PR	Disc	Cash	Bank

EXAMPLE OF 3 COLUMN CASH BOOK

Page No: 36

Dr. (Receipts) **CASH BOOK** **Cr. (Payments)**

Date	Description	VN	PR	Cash	Bank	Date	Description	VN	PR	Cash	Bank
2018						2018					
Mar.01	Balance b/d		-	1,450	1,500	Mar.02	Mark & Co.		60		120
Mar.04	John & Co.		25	400		Mar.05	Bank		C	400	
Mar.05	Cash		C		400	Mar.08	Stationary		440	25	
Mar.13	Sales		405	1,800		Mar.12	Purchases		420	525	
Mar.15	Cash		C		850	Mar.15	Bank		C	850	
Mar.20	Bank		C	150		Mar.17	Drawings		445		40
Mar.22	Peter & Co		30		880	Mar.19	Purchases		420		630
Mar.29	Sales		405	650		Mar.20	Cash		C		150
Mar.30	Bank		C	145		Mar.25	Daniel Inc.		65		270
						Mar.26	Furniture		425	175	
						Mar.28	Rent		435		120
						Mar.30	Cash		C		145
						Mar.31	Salaries		415		300
						Mar.31	Balance c/d		-	2,620	1,855
				4,595	3,630					4,595	3,630
Apr.01	Balance b/d			2,620	1,855						

SUBSIDIARY BOOKS

Introduction

- Subsidiary books actually saves a lot of man-hours and tiresome clerical work. Instead of journalizing each entry, they are recorded into various subsidiary books. Think of your subsidiary book as sub-journals that record only one type of transaction.
- There is no separate entry for these transactions in the general ledger. The posting to the Ledger Accounts is done from the subsidiary book itself. This method of recording is known as the Practical System of Accounting or sometimes the English System.

Meaning

- subsidiary Books are those books of original entry in which transactions of similar nature are recorded at one place and in chronological order. In a big concern, recording of all transactions in one Journal and posting them into various ledger accounts will be very difficult and involve a lot of clerical work.
- This is avoided by sub-dividing the journal into various subsidiary journals or books. The subdivisions of journal into various subsidiary journals for recording transactions of similar nature are called as 'Subsidiary Books.'

The different subsidiary books and their purpose are shown below:

- 1. Purchases Day Book – for recording credit purchase of goods only. Cash purchase or assets purchased on credit are not entered in this book.
- 2. Sales Day Book – for recording credit sales of goods only. Assets sold or cash sales are not recorded in this book.
- 3. Purchases Returns Book – for recording the goods returned to the suppliers when purchased on credit.
- 4. Sales Returns Books – for recording goods returned by the customers when sold on credit.
- 5. Bills Receivable Book – for recording the bills received [Bills Receivables] from customers for credit sales.
- 6. Bills Payables Book – for recording the acceptances [Bills Payables] given to the suppliers for credit purchases.
- 7. Cash Book – for all receipts and payments of cash.
- 8. Journal Proper – for recording any transaction which could not be recorded in the above-mentioned subsidiary books. For example, assets purchased or sold on credit and opening entry etc., are entered in this book.

Advantages of Subsidiary Books:

- **1. Saving of Clerical Labour:**
- Subsidiary books effect considerable saving of clerical labour in postings and narration. Transactions of any one class such as credit purchases, credit sales, cash transactions etc., are recorded through separate subsidiary journals and there is no need for giving narration.

- For example, by recording the transactions in the Purchase Day book 50% of the labour in postings is saved. The periodical total of this book is to be debited to the Purchases a/c. Only the personal accounts of the suppliers are to be credited.

2. **Division of Clerical Work:**

- As separate journals are used for recording the transactions of each particular type, the division of clerical labour amongst several office clerks becomes possible. This makes speedy record of day-to-day transactions practicable.
- **3. Minimizes Frauds:**
- These books make possible the introduction of internal check system under which the system of rotation of writing up books can be adopted. This helps minimizing errors and detecting frauds.
- **4. Facilitates Further Reference:**
- As transactions of similar nature are grouped together in a separate book, the further reference to any particular item is considerably facilitated.

Purchase book

- Purchase book is a Subsidiary book. The Purchase book or Purchase day book contains the record of all credit-purchase. Cash book accommodates the records of all goods-purchase.
- A Purchase book does not hold the record of purchases of assets. The Journal proper contains those records. The entries are recorded in the Purchase book from source documents. Invoices or bills received from the suppliers of goods serve as the source documents.
- We make the entries in the Purchase book with the net amount of the invoice. Which is why a Purchase book does not contain trade discount and other details which are there on the invoice.
- Every month the total of the Purchase book is posted on the Debit side of the Purchases A/c. Purchases A/c is a ledger A/c. However, the individual accounts of the suppliers may be posted daily. Also, where the volume of transactions is too large, the entries in the ledger can be posted weekly or fortnightly. Given below is the performa of the Purchase book:

Purchase Return Book

- When the goods purchased on credit are returned to the supplier, these are recorded in the Purchase return book. Sometimes, goods purchased can be defective or of low quality, etc. and hence, need to be returned. A separate book is maintained for the purchase return and these are not deducted from the purchases in the Purchase book. Also, Purchase return is recorded at the net amount on the invoice.
- Debit note is prepared for every return of goods. It is prepared in duplicate. The original one is sent to the supplier while the duplicate copy is kept for our own records. The Debit note contains the name of the supplier, details of goods returned and the reason thereof. Each debit note is dated and serially numbered.

SALES DAY BOOK

- 1) Only Credit sale of goods are entered in the book
- 2)Cash sales are not recorded
- 3) Sale of items like machinery, furniture are recorded in the journal proper and not in this book.

PURCHASE BOOK

Date	Invoice No.	Name of the Supplier (Account to be credited)	L.F.	Details	Total Amount
		Purchase A/c Dr.			

Sales Book

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

Format of Purchases Return Book

Purchase Returns Book						
Date	Particulars	Debit Note No.	L.F.	Amount R.S.		Remarks
				Details	Total	

Sales Return Book

Date	Particulars	Credit Note No.	L.F.	Amount Rs.

DIFFERENCE BETWEEN TRIAL BALANCE & BALANCESHEET

Basis	Trial balance	Balance sheet
2. Purpose	Trial balance is prepared to check the arithmetical accuracy of the accounting entries made.	Balance sheet is prepared to ascertain the financial position of a business.
3. Contents	It is a summary of balances of all accounts – personal, real and nominal accounts.	It is a statement showing the closing balances of only personal and real accounts.
4. Format	The trial balance contains columns for debit balances and credit balances.	The items are grouped as assets and liabilities.
5. Stage	It is prepared before the preparation of final accounts.	It is prepared after preparing trial balance and trading and profit and loss account.
6. Period	It can be prepared periodically, say at the end of the month, quarterly, half yearly, etc.	It is generally prepared at the end of the accounting period.
7. Order	Balances shown in the trial balance need not be in order.	Balances shown in the balance sheet must be in order.
8. Compulsion	Preparation of trial balance is not compulsory.	Preparation of the balance sheet is compulsory in certain cases.

Difference Between Single Entry & Double Entry System of Book Keeping

Single entry system	Double entry system
1. Personal account and cash account alone are maintained.	Personal account, real account and nominal accounts are maintained properly.
2. It involves less clerical labour.	It involves more clerical labour.
3. Only one aspect of a transaction is recorded.	Two aspect of a transaction are recorded.
4. There may be debit without a corresponding credit and vice versa.	For every debit there is a corresponding equal credit.
5. Trading account, Profit and loss account and Balance sheet cannot be prepared as it has incomplete record.	They can be prepared.
6. It is an imperfect way of book-keeping.	It is a perfect and scientific system.
7. Approximate net profit can be indirectly calculated.	Accurate net profit can be calculated directly.
8.As the ledger does not contain all accounts, trial balance cannot be prepared.	To test the arithmetical accuracy a trial balance can be prepared.
9.Tax authorities do not accept it as such	Tax authorities accept this method.
10.Internal check is not possible	It is possible in this system.
11. Balance sheet cannot prepare. So, financial position is difficult to ascertain.	Reliable financial position can be found through balance sheet.
12. The Accounting records are not acceptable as evidence.	In case of disputes, accounting records can be produced in courts of law
13.It is suitable for small businessmen.	It is suitable for any type of businessmen. s

UNIT – 3

BILLS OF EXCHANGE (This unit is only for BBA Students)

Meaning of bill of exchange

According to the Negotiable Instruments Act 1881, a bill of exchange is defined as “an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument”.

Features of bill of exchange

- It is important to have a bill of exchange in writing
- It must contain a confirm order to make a payment and not just the request
- The order should not have any condition
- The bill of exchange amount should be definite
- Fixed date for the amount to be paid
- The bill must be signed by both the drawee and the drawer
- The amount stated on the bill should be paid on-demand or on the expiry of a fixed time
- The amount is paid to the beneficiary of the bill, specific person, or against a definite order

Parts Of A Bill Of Exchange

- *Date*
- *Term*
- *Amount*
- *Stamp*
- *Parties*

Parties to a Bill Of Exchange

Drawer

The person who orders a bank to withdraw money from an account to pay a designated person a specific sum according to the term of the Bill.

- Drawee
- The person on whom the Bill is drawn (The *Debtor). He is the person who accepts the Bill of Exchange. To him the bill is considered as Bill payable.*
- *Payee*

- *The person to whom the Bill-money is payable. In most of the cases the drawer of the Bill himself is the Payee. To him*

- *The Bill is considered as Bill Receivable.*

Advantages of Bill of Exchange

- **Legal Document-** It is a legal document, and if the drawee fails to make the payment, it will be easier for the drawer to recover the amount legally.
- **Discounting Facility-** In cases where the drawer is in immediate need of money, the bill can be converted into cash by discounting it from a bank by paying some nominal charges.
- **Endorsement Possible-** This bill of exchange can be exchanged from one individual to another for the adjustment of the debt.

Promissory Note

The promissory note is defined as an instrument in writing (not being a banknote or a currency note), containing an unconditional undertaking signed by the maker, to pay a certain sum of money only to or to the order of a certain person, or to the bearer of the instrument.

Importance of Promissory note in Bill of Exchange

According to the Negotiable Instruments Act 1881, the meaning of promissory note is 'an instrument in writing (not being a banknote or a currency note), containing an unconditional undertaking signed by the maker, to pay a certain sum of money only to or to the order of a certain person, or to the bearer of the instrument. However, according to the Reserve Bank of India Act, a promissory note payable to bearer is illegal. Therefore, a promissory note cannot be made payable to the bearer.'

IMPORTANT TERMS IN BILL OF EXCHANGE

(a) Term of Bill or Period of Bill	It is the time period between the date on which a bill is drawn and the date on which it is payable.
(B) Due Date	It is the date on which the payment of the bill is due.
(C) Days of Grace	These are the three extra days added to the period of bill.
(D) Date of Maturity	The date which comes after adding three days of grace to the period of bill.

(a) Discounting of Bill	• It means encashment of bill before the date of its maturity. • The bank deducts its charges from the bill.
(B) Endorsement of Bill	• Endorsement means the transfer of bill or promissory note to another person. • It is transferred on account of the settlement of debts and dues.
(C) Bill Sent for Collection	• When a bill is sent to the bank for collection with instruction, that it will be retained till the maturity date. • Bill will be realised on its due date. It is known as 'Bill sent for collection'.

(a) Dishonour of Bill	• When payment is not made by the acceptor of the bill on its due date. It is known as 'Dishonor of Bill'. • Non-payment may be due to insufficient balance or insolvency.
(B) Noting of a Bill	• On dishonour of a bill, when this fact is brought to the notice of a Notary Public, it is termed as 'Noting of a bill'. • Notary public charges to record or take a noting of dishonour.
(C) Noting Charges	• It is the fee paid to the Notary Public for noting of dishonour of a bill.

(a) Retiring of a Bill	• When the Drawee pays the bill before its due date, It is termed as the retirement of a bill. • It happens with the mutual understanding between the Drawer and the Drawee. • To encourage Retiring of the bill, the holder allows some discount called Rebate on the bill amount from the date of retiring the bill to the maturity.
(B) Renewal of a Bill	• When the holder of a bill is not in a position to meet the bill on its due date, Drawee approaches the Drawer with a request of extension of time for payment. • If Drawer agrees, the old bill is cancelled, and a fresh bill with the new terms of payment is drawn and duly accepted and delivered. This is called Renewal of the Bill.

Q.2 Distinguish Between an Accommodation Bill and a Trade Bill.

Answer:

Parameters	**Trade Bills**	**Accommodation Bills**
Objectives	These bills are drawn to facilitate the trade transactions of sale and purchases of goods.	These bills are drawn to help someone in need of financial assistance.
Consideration	There is a definite consideration for which the bill is accepted.	These bills are drawn without consideration.
Extension of Credit	Trade bills are a form of credit extension.	These bills are not a form of credit extension.
Proceeds	When trade bills are discounted, the proceeds remain with the holder.	When these bills are discounted, the proceeds may be shared by two parties in an agreed ratio.
Recovery	If trade bills are dishonoured, the amount may be recovered easily through the court.	In case of dishonour of these bills, the drawer cannot file a suit against the drawee.

Accounting Entries for Bills of Exchange

CASE - 1

Accounting entries - Summary

When bill is retained till maturity

Transaction	*Books of Creditor/Drawer*	*Books of Debtor/Acceptor*
Sale/Purchase of goods	Debtor's A/c Dr. Sales A/c	Purchase A/c Dr. Creditor's A/c
Receiving/Accepting the bill	Bills Receivable A/c Dr. Debtor's A/c	Creditor's A/c Dr. Bills Payable A/c
Collection of the bill	Cash/Bank A/c Dr. Bills Receivable A/c	Bills Payable A/c Dr. Cash/Bank A/c

CASE – 2

Accounting entries - Summary

When bill is endorsed to a third party

Transaction	*Books of Creditor/Drawer*	*Books of Debtor/Acceptor*
Sale/Purchase of goods	Debtor's A/c Dr. Sales A/c	Purchase A/c Dr. Creditor's A/c
Receiving/Accepting the bill	Bills Receivable A/c Dr. Debtor's A/c	Creditor's A/c Dr. Bills Payable A/c
Endorsing the bill	Creditor's A/c Dr. Bill Receivable A/c	**No Entry**
On maturity of the bill	**No Entry**	Bills Payable A/c Dr. Bank A/c

CASE – 3

Accounting entries - Summary

When bill is endorsed to a creditor but is subsequently dishonoured

Transaction	*Books of Creditor/Debtor*	*Books of Acceptor*
Sale/Purchase of goods	Debtor's a/c Dr To Sales a/c	Purchase a/c Dr To Creditor
Receiving/ Accepting the bill	Bills Receivable a/c Dr To Debtor	Creditor a/c Dr To Bills Payable
On endorsing of the bill	Creditor a/c Dr To Bills Receivable	No entry
On dishonour and noting charges incurred	Debtor a/c Dr To Creditor (bill amount + noting charges	Bills Payable a/c Dr Noting Charges a/c Dr To Creditor

CASE – 4

Accounting entries - Summary

When bill is retained till maturity but dishonoured

Transaction	*Books of Creditor/Debtor*	*Books of Acceptor*
Sale/Purchase of goods	Debtor's a/c Dr To Sales a/c	Purchase a/c Dr To Creditor
Receiving/ Accepting the bill	Bills Receivable a/c Dr To Debtor	Creditor a/c Dr To Bills Payable
On dishonour and noting charges incurred	Debtor a/c Dr To Bills Receivable To Cash	Bills Payable a/c Dr Noting Charges a/c Dr To Creditor

Noting

. When a promissory note or bill of exchange ha s been dishonoured by non-acceptance or non-payment, the holder may cause such dishonour to be noted by a notary public upon the instrument, or upon a paper attached thereto, or partly upon each.

Such note must be made within a reasonable time after dishonour, and must specify the date of dishonour, the reason, if any, assigned for such dishonour, or, if the instrument has not been expressly dishonoured, the reason why the holder treats it as dishonoured, and the notarys charges.

Protest.

When a promissory note or bill of exchange has been dishonored by non-acceptance or non-payment, the holder may, within a reasonable time, cause such dishonour to be noted and certified by a notary public. Such certificate is called a protest.

Protest for better security. When the acceptor of a bill of exchange has become insolvent, or his credit has been publicly impeached, before the maturity of the bill, the holder may, within a reasonable time, cause a notary public to demand better security of the acceptor, and on its being refused may, within a reasonable time, cause such facts to be noted and certified as aforesaid. Such certificate is called a protest for better security.

UNIT – 3 (ONLY FOR B.COM STUDENTS)

Computerized Accounts

Computerized accounting system refers to the system of maintaining accounts using computers. It involves the processing of accounting transactions through the use of hardware and software in order to keep and produce accounting records and reports.

Features of computerized accounting

Simple and integrated

It is designed to automate and integrate all the business operations such as purchase, sales, finance, inventory and manufacturing. The CAS may be integrated with enhanced Management Information System (MIS), multi-lingual and data organization capabilities to simplify all the business processes of the organization easily and cost-effectively.

- **Speed**

It can perform functions at much higher speed than doing the same manually.

- **Accuracy**

Computers perform functions with high degree of accuracy. If hardware, software and input by people are proper, the computerized accounting system can assure of accurate outcome.

- **Reliability**

Computers are used to process large volumes of data and hence, data provided by it are reliable.

- **Versatility**

Computer and accounting software have the ability to perform diverse tasks. For example, by simply recording accounting entries through accounting software, one can get trial balance, trading account, profit and loss account, balance sheet and diverse reports.

- **Transparency**

With computerized accounting, the organization will have greater transparency of day-today business operations and access to the vital information.

- **Scalability**
- computerized accounting enables processing of any volume of data in tune with the change in the size of the business.

- **On-line facility**

  Computerized accounting offers online facility to store and process transaction and data so as to retrieve information to generate and view financial reports in any part of the world.

- **Security**
- In computerized accounting, only the authorized users are permitted to have access to accounting data. Under manual accounting system, it is very difficult to secure such information as it is open to inspection by any person dealing with the books of accounts.

Components of Computerised Accounting System

Components of Computerized Accounting can be classified into six categories, namely,

i)Hardware

ii) Software

iii) People

iv) Procedure

v) Data and

vi) Connectivity.

Advantages of Computerised Accounting

- **Better Quality Work:** The accounts prepared with the use of computerized accounting system are usually uniform, neat, accurate, and more legible than a manual job.
- **Lower Operating Costs:** Computer is a reliable and time-saving device. The volume of job handled with the help of computerized system results in economy and lower operating costs. The overall operating cost of this system is low in comparison to the traditional system.
- **Improves Efficiency:** This system is more efficient in comparison to the traditional system. The computer makes sure speed and accuracy in preparing the records and accounts and thus, increases the efficiency of employees.
- **Facilitates Better Control:** From the management point of view, there is greater control possible and more information may be available with the use of the computer in accounting. It ensures efficient performance in accounting records.

- **Greater Accuracy:** Computerized accounting make sure accuracy in accounting records and statements. It prevents clerical errors and omissions in records.
- **Relieve Monotony:** Computerized accounting reduces the monotony of doing repetitive accounting jobs. Which are tiresome and time-consuming.
- **Facilitates Standardization:** Computerised accounting provides standardization of accounting routines and procedures. Therefore, it ensures standardization in the accounting records.
- **Minimizes Mathematical Errors:** While doing mathematical work with computers, errors are virtually eliminated unless the data is entered improperly in the system.
- **Legibility** : The data displayed on computer monitor is legible. This is because the characters (alphabets, numerals, etc.) are type written using standard fonts. This helps in avoiding errors caused by untidy written figures in a manual accounting system.
- **Efficiency** : The computer based accounting systems ensure better use of resources and time. This brings about efficiency in generating decisions, useful information's and reports.
- **Quality Reports** : The inbuilt checks and untouchable features of data handling facilitate hygienic and true accounting reports that are highly objective and can be relied upon.
- **speed** : Accounting data is processed faster by using a computerized accounting system than it is achieved through manual efforts. This is because computers require far less time than human beings in performing a task.

Disadvantages of Computerized Accounting:

Reduction of Manpower:

The introduction of computers in accounting work reduces the number of employees in an organization. Thus, it leads to greater amount of unemployment.

High Cost:

A small firm cannot install a computer accounting system because of its high installation and maintenance cost. To be more economical there should be large volume of work. If the system is not used to its full capacity, then it would be highly uneconomical.

Require Special Skills:

- Computer system calls for highly specialized operators. The availability of such skilled personnel is very scarce and very costly.

Other Problems:

- Frequent repair and power failure may affect the accounting work very much. Computers are prone to viruses. Often time's people will assume the computer is doing things correctly and problems will go unchecked for long period of time.

Cost of Training:

- The sophisticated computerised accounting packages generally require specialised staff personnel. As a result, a huge training costs are incurred to understand the use of hardware and software on a continuous basis because newer types of hardware and software are acquired to ensure efficient and effective use of computerised accounting systems.

- **Staff Opposition** :
- Whenever the accounting system is computerised, there is a significant degree of resistance from the existing accounting staff, partly because of the fear that they shall be made redundant and largely because of the perception that they shall be less important to the organisation.

  - **Disruption** :

- The accounting processes suffer a significant loss of worktime when an organisation switches over to the computerised accounting system. This is due to changes in the working environment that requires accounting staff to adapt to new systems and procedures

  - **System Failure** :

- The danger of the system crashing due to hardware failures and the subsequent loss of work is a serious limitation of computerized accounting system. However, providing for back-up arrangements can obviate this limitation. Software damage and failure may occur due to attacks by viruses. This is of particular relevance to accounting systems that extensively use Internet facility for their online operations. No full-proof solutions are available as of now to tackle the menace of attacks on software by viruses.

TALLY

Tally ERP 9 is accounting software that has been **used** to record several financial transactions and events. As it is a multi-functional software, it includes inventory management, accounting, payroll preparation, multiple go-downs management, cost center management,

- Tally software is used for storing all the business transactions of each account in detail. Tally has made calculations simple. Tally has become part of all businesses.
- Small scale enterprises believe that Tally software carries out efficient business transactions, provides accuracy, and saves a lot of time.
- Manual calculations are time-consuming; that's why all the organizations use Tally.
- Because of Tally, the chances of error are reduced to a great extent. The Tally software can learn at home or designated institutes. It is self-explanatory and easy to learn.
- Tally is cost-effective and time-saving. It also ensures accuracy in business management. It enables the digitalization of bills and signatures, thus staying up-to-date with the latest technology.
- Using the Tally ERP 9 Training, the owner of a small shop can also manage his store, keep records of customer bills, and manage financial transactions efficiently.

HOW TO CREATE A COMPANY IN TALLY

How to create a company

- Go to Gateway of Tally > Alt + F3 > Create Company
- Enter the basic information, i.e., name, mailing name and address of the company, currency symbol etc.
- In the ‘maintain field’, select Accounts Only or Accounts with Inventory as per the company requirements.
- In the Financial Year from, the first day of the current financial year for e.g., 1-4-2017 will be displayed by default, which can be changed as per requirement.
- Enter the Tally Vault Password if required.
- Press Y or Enter to accept and save.

UNIT – 4

Preparation of Final Accounts of Sole Trading Concerns

Trading and Profit and Loss Account

In order to arrive at the balance sheet of a business, one needs to prepare the trading account and profit and loss account first. This account is prepared to arrive at the figure of revenue earned or loss incurred during a period. Let us understand the trading account and profit and loss account in detail.

A trading account helps in determining the gross profit or gross loss of a business concern, made strictly out of trading activities. Trading involves buying and selling activities. In the trading account, the cost of goods sold is subtracted from net sales for the period to calculate gross profit. Only direct revenue and direct expenses are considered in it. Trading account is prepared mainly to know the profitability of the goods bought by the businessman.

The difference between selling price and cost of goods sold is the earning for the businessman, which is also known as gross profit. Whereas, net profit means all revenues minus all expenses including the cost of goods sold, the selling, general and administrative expenses, and the non-operating expenses. Thus in order to calculate the gross earning, it is necessary to know the cost of goods sold and sales figures. Also,

Gross Profit = Sales – COGS (Sales + Closing Stock) – (Stock in the beginning + Purchases + Direct Expenses)

Items included on the debit side are opening stock, purchases, and direct expenses and on the credit side is sales and closing stock. The resultant figure is either gross profit or gross loss.

The profit and loss account is opened by recording the gross profit on the credit side or gross loss on the debit side.

For earning the net profit, a businessman has to incur many more expenses in addition to the direct expenses. Those expenses are deducted from profit or added to a gross loss and thus, the resultant figure will be net profit or a net loss.

Expenses included in the profit and loss account are Selling and distribution expenses, Freight & carriage on sales, Sales tax, Administrative Expenses, Financial Expenses, Maintenance, depreciation and Provisions and more. On the credit side, Discount received, Commission received, Profit on sale of assets and more appear.

PROFORMA OF TRADING ACCOUNT

Trading Account

(For the year ended…)

Dr. Cr.

Particulars		Amount	Particulars		Amount
To Opening stock		Xxx	By Sales	xxx	
To Purchases	xxx		Less: Return Inwards	(xxx)	Xxx
Less: Return Outwards	(xxx)	Xxx	By Closing stock		Xxx
To Wages		Xxx	By Gross Loss		Xxx
To Carriage Inwards		Xxx			
To Freight Inwards/cartage		Xxx			
To Gross Profit c/d		Xxx			
		xxx			xxx

PROFORMA OF PROFIT AND LOSS ACCOUNT

Income Statement or Profit & Loss Account			
Particulars	**Amount**	**Particulars**	**Amount**
To Gross Loss (Brought From Trading A/C)		*By Gross Profit (Brought From Trading A/C)*	
To Salaries (Adjust O/S & Prepaid)		By Rent Received	
To Rent, Rates & Taxes		By Discount Received	
To Travelling Expenses		By Interest Earned (Accruals Adjusted)	
To Stationery & Printing		By Bad Debts Recovered	
To Postage		By Commission Earned	
To Audit & Legal Charges		By Dividends Received	
To Telephone Expenses		By Income From Other Sources	
To Insurance Premium (Prepaid Adjusted)		*By Net Loss (Transferred to Capital A/C)*	
To Marketing & Advertisement			
To Interest Paid			
To Discount Allowed			
To Sundry Expenses			
To Carriage Outwards			
To Bad Debts			
To Depreciation			
To Repairs & Renewals			
To Commission			
To Other Expenses			
To Loss by Fire or Theft			
To Net Profit (Transferred to Capital A/C)			

Manufacturing Account Format

The manufacturing account helps to better the cost-effectiveness of manufacturing activities. After the ascertainment of the costs of finished goods, we need to transfer this cost to Trading Account.

The trading account shows Gross Profit. Whereas, the Manufacturing Account depicts the cost of goods sold and also includes direct expenses. Manufacturing account addresses the raw material and work in progress and does not deal with the finished goods.

We debit all the direct production expenses such as depreciation on plant and machinery and factory building, repairs on plant and machinery and factory building, salary to the factory manager, wages, cartage on raw-materials, etc.

Thus, the cost of finished goods includes the cost of raw materials and all direct expenses. All indirect expenses form a part of the Profit and Loss A/c.

Solved Example

Mr. Prasad runs a factory which produces caps. Following are the details available in respect of his manufacturing activities for the year ended on 31.03.2018

Opening work-in-progress (4,000 units)	8,000
Closing work-in-progress (5,000 units)	10,000
Opening stock of Raw materials	75,000
Closing stock of Raw materials	85,000
Purchase of raw material	4,20,000
Hire charges of machine@₹0.50 per unit manufactured	
Rent of factory	1,50,000
Direct wages- @₹0.70 per unit manufactured and @₹0.30 per unit of closing	

W.I.P	
Repairs and maintenance	100,000
units produced-2,60,000	

Prepare a manufacturing Account of Mr. Prasad for the year ended 31.03.2018.

Solution : -

In the Books of Mr. Prasad

Manufacturing Account for the year ended 30.03.2018

Particulars	Units	Amount	Particulars	Units	Amount
To Opening Work-in-progress	4000	8000	By Closing Work-in-Progress	5000	10000
To Raw material consumed:			By Trading A/c		971500
Opening inventory		75000	(transfer of Cost of production)		
Add: Purchases		420000			
Less: Closing inventory		(85000)			
		410000			

To Direct Wages	183500		
To Direct expenses (hire charges of machinery)	130000		
Prime Cost	**723500**		
To Factory expenses:			
Factory rent	150000		
Repairs & Maintenance of plant and machinery	100000		
	981500		**981500**

Working Notes:

Direct Wages= 260000 units@₹0.70=. ₹182000

5,000 units@₹ 0.30=. ₹ 1500

Total ₹183500

Hire charges on machinery:-260000 unit @ ₹0.50 ₹130000

BALANCE SHEET

A **balance sheet** is a **financial statement** that reports a company's assets, liabilities and shareholders' equity at a specific point in time, and provides a basis for computing rates of return and evaluating its capital structure.

The balance sheet is one of the three fundamental financial statements and is key to both financial modeling and accounting. The balance sheet displays the company's total assets, and how these assets are financed, through either debt or equity. It can also be referred to as a statement of net worth, or a statement of financial position. The balance sheet is based on the fundamental equation: **Assets = Liabilities + Equity**.

A balance sheet reports the assets, liabilities and shareholders equity of your business at a given point in time. The items reported on the balance sheet correspond to the accounts outlined on your chart of accounts. A balance sheet is made up of the following elements:

ASSETS

The assets section of the balance sheet breaks down what your business owns of value that can be converted into cash. Your balance sheet will list your assets in order of liquidity; that is, it reports assets in order of how easily they can be converted to cash. There are two main categories of assets included on your balance sheet:

Current Assets: Current assets can easily be converted to cash within a year or less. Current assets are further broken down on the balance sheet into these accounts:

Cash and cash equivalents: These are your most liquid assets, including currency, checks and money stored in your business's checking and savings accounts

Marketable securities: Investments that you can sell within a year

Accounts receivable: Money that your clients owe you for your services that will be paid in the short term

Inventory: For businesses that sell goods, inventory includes finished products and raw materials

Prepaid expenses: Things of value that you've already paid for, like your office rent or your business insurance

Long-Term Assets: Long-term assets won't be converted to cash within a year. They can be further broken down into:

Fixed assets: Includes property, buildings, machinery and equipment like computers

Long-term securities: Investments that can't be sold within one year

Intangible assets: Assets that aren't physical objects, such as copyrights, franchise agreements and patents

LIABILITIES

The next section of a balance sheet lists a company's liabilities. Your liabilities are the money that you owe to others, including your recurring expenses, loan repayments and other forms of debt. Liabilities are further broken down into current and long-term liabilities.

Current liabilities include rent, utilities, taxes, current payments toward long-term debts, interest payments and payroll.

Long-term liabilities include long-term loans, deferred income taxes and pension fund liabilities.

SHAREHOLDERS EQUITY

Shareholders equity refers to the amount of money generated by a business, the amount of money put into the business by its owners (or shareholders) and any donated capital. Shareholders equity is your net assets. On your balance sheet it's calculated using this formula:

Stakeholders Equity = Total Assets – Total Liabilities

Balancing a Balance Sheet

When creating a balance sheet for your business it's important to understand that, as the name suggests, your balance sheet must always be balanced. A balance sheet is divided into two sections, with one side representing your business's assets and the other showing its liabilities and shareholders equity.

The total value of your assets must be equal to the combined value of your liabilities and equity. When that's the case, your document is said to be in balance. This idea is represented by the foundational formula of balance sheets:

Assets = Liabilities + Shareholder Equity

Why Is a Balance Sheet Important?

A balance sheet is an important financial statement that gives a snapshot of the financial health of your business at a point in time. You can also look at your balance sheet in conjunction with your other financial statements to better understand the relationships between different accounts. A balance sheet is important because it provides the following insights about your business:

By comparing your business's current assets to its current liabilities, you'll get a clear picture of the liquidity of your company, or how much cash you have readily available. You always want to have a buffer between your current assets and liabilities to cover your short-term financial obligations, with assets always greater than liabilities.

EFFICIENCY

By comparing your income statement to your balance sheet, you can measure how efficiently your business uses its assets. For example, you can get an idea of how well your company is able to use its assets to generate revenue.

SAMPLE TRADING, P&L ACCOUNT AND BALANCESHEET

Trading and Profit and Loss Account

Dr as on 31st March, 2011 Cr

Particulars	Amt. (₹)	Particulars		Amt. (₹)
To Opening Stock	50,000	By Sales	4,21,000	
To Purchase	3,50,000	(–) Sales Return	5,000	4,16,000
To Carriage on Purchase	12,000	By Closing Stock		2,500
To Wages	8,000	By Gross Loss c/d (b/f)		1,500
	4,20,000			4,20,000
To Gross Loss b/d	1,500	By Commission		4,000
To Rent	15,000	By Net Loss		41,500
To Bad Debts	7,000			
To Stationery	6,000			
To Travelling Expenses	2,000			
To Insurance	7,000			
To Discount	5,000			
To Office Expenses	2,000			
	45,500			45,500

Balance Sheet

as on 31st March, 2011

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital	3,00,000		Cash in Hand	32,000
(–) Net Loss	41,500		Furniture	1,28,000
	2,58,500		Debtors	1,40,000
(–) Drawings	24,000	2,34,500	Plants	60,000
			Closing Stock	2,500
Creditors		1,00,000		
Bank Overdraft		28,000		
		3,62,500		3,62,500

UNIT – 5

FINAL ACCOUNTS OF NON TRADING CONCERNS

Accounting for Non-Trading Concerns:

Definition and Explanation of Non trading Concerns:

Individuals or institutions with activities other than trade are known as **non-trading concerns**. Examples of non trading concerns are clubs, hospitals, libraries, colleges, athletic clubs etc.

These institutions are started not for carrying on a business and making a profit but for some charitable, religious or similar purpose. Their income, which is derived from donations, subscriptions, entrances fees etc., is spent on the objects for which they are started.

Final Accounts of Non-Trading Concerns:

Non-trading concerns usually maintain their accounts by the double entry system and periodically prepare their final accounts for the submission to their members and subscribers. The method of preparing final accounts by non trading concerns is different than trading concerns.

The method of preparing final accounts by non trading concerns is different than trading concerns. As these concerns do not deal in any goods like trading concerns, so they cannot prepare a trading and profit and loss account. At the end of the year they make out an account called an Income and expenditure account and balance sheet. The Income and expenditure account serve the same purpose as the profit and loss account in the case of trading concerns and is made out exactly in the same manner.

Usually the **non-profit making institutions** do not maintain a full set of books but merely a cash book in which all receipts and payments are entered. At the end of the year the cash book is summarised under suitable heads and the summary thus prepared is called a Receipt and Payment Account. In order to know the result of the year's working it should be converted into Income and expenditure account.

Receipt and Payment Account:

Receipt and payment account is a mere summary of cash book for a year. It begins with the cash in hand at the commencement and ends with that at the close of the year. Similarly to cash account, in receipts and payments account receipts are shown on the debit side while payments are shown on the credit side.

Receipt and payment account is a mere summary of cash book for a year. It begins with the cash in hand at the commencement and ends with that at the close of the year. Similarly to cash account, in receipts and payments account receipts are shown on the debit side while payments are shown on the credit side, without any distinction between capital and revenue. Moreover, it does not include an unpaid expenditure not any unrealized income relating to the period under review and so fails to reveal the financial position on the concern.

Format of Receipt and Payment Account:

Receipts	**Rs**	**Payments**	**Rs**

Example:

Receipt and Payment Account

Receipts	**Rs.**	**Payments**	**Rs.**
To Balance b/d	4,240	By general expenses	5,550
To subscription	4,630	By salaries and wages	3,550
To Life membership fees	1,250	By furniture	1,800
To Entrance fees	1,240	By rent, rates & taxes	500
To interest received	1,180	By printing & stationary	125
To misc. receipts	1,050	By Repairs	150
		By Balance c/d	915
	13,590		13,590

Income and expenditure account:

Income and expenditure account is merely another name for profit and loss account. Such type of profit and loss account is generally adopted by non trading concerns like clubs, societies, hospitals, and like etc. This account is credited with all earnings (both realized and unrealized) and debited with all expenses (both paid and unpaid) The difference represents a surplus of deficiency for a given period which is carried to the capital account. It should be noted that items of receipts or payments of capital nature such as legacies, purchases or sales of any fixed assets must not be included in this account.

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How to Convert a Receipt and Payment Account into Income and Expenditure Account:

The following steps will be necessary to convert a receipt and payment account into an *income and expenditure account*:

1. Opening and closing balances of receipt and payment account should be excluded.
2. All items of capital receipts and payments should be excluded.
3. All incomes of previous years or for years to come should be excluded.
4. All expenditures of previous years and years to come should be excluded.
5. All accrued income and outstanding expenditures relating to the period should be included.
6. Item such as bad debts, depreciation, etc. will have to be provided.

Treatment of Peculiar Items:

Generally in exercises the instructions are given as to the treatment of special items. Such instructions are based on the rules of the concern. These should be followed while solving questions. In cases where no specific instructions are given the following guidelines may be considered.

Legacy:

It is the amount received by the concern as per the will of the donor. It appears in the receipt side of receipt and payment account. It should not be considered as as an income but should be treated as capital receipt i.e., credited to capital fund account.

Donation:

Amount received from any source by way of gift is described as donation. It appears on the receipts side of receipt and payment account. Donations are usually credited to income. Rules of the association may provide that a part of donations are to be treated as capital. However, if donations are received for a specific purpose viz., building, free dispensary etc., then it should require special treatment. Donations for specific purposes should not be credited to income and expenditure account. Similarly donations representing heavy amount may also be treated as capital receipts.

Subscription:

The members of the associations, as per rules, are generally required to make annual subscription to enable it to serve the purpose for which it was created. It appears on the receipts side of the receipt and payment account and is usually credited to income. Care must be exercised to take credit for only those subscriptions which are relevant.

Life Membership Fees:

Generally the members are required to make the payment in a lump sum only once which enables them the members for whole of life. Life members are not required to pay the annual membership fees. As life membership fees is substitute for annual membership fees therefore, it is desirable that life membership fees should be credited to separate fund and fair portion be credited to income in subsequent years. In the examination question if there is no instruction as to what portion be treated as income then whole of it should be treated as capital.

Entrance Fees:

Entrance fees is also an item to be found on the receipt side of receipts and payments account. There are arguments that it should be treated as capital receipt because entrance fees is to be paid by every member only once (i.e., when enrolled as member) hence it is non-recurring in nature. But another argument is that since members to be enrolled every year and receipt of entrance fees is a regular item, therefore, it should be credited to income. In the absence of the instructions any one of the above treatment may be followed but students should append a note justifying their treatment.

Sale of News Papers, Periodicals etc.

As the old newspapers, magazines, and periodicals etc. are to be disposed of every year, the receipts on account of such sales should be treated as income, and therefore to be credited to income and expenditure account.

Sales of Sports Material:

Sale of support materials (used) is also a regular feature of the clubs. Sales proceeds should be treated as income, and therefore to be credited to income and expenditure account.

Honorarium:

Persons may be invited to deliver lectures or artists may be invited to give their performance by a club (for its members). Any money so paid is termed as honorarium and not salary. Such honorarium represents expenditure and will be debited to income and expenditure account.

Special Fund:

Legacies and donations may be received for specified purchases. As discussed above these should be credited to special fund and all expenses related to such fund are shown by way of deduction from the respective fund and not as expenditure in income and expenditure account.

Capital Fund:

Any concern - whether profit seeking or non profit seeking - requires money for conducting day to day functions. In the case of profit seeking concerns such money is called "capital", while in the case of non - profit seeking concerns it is called "capital fund". The excess of total assets over total external liabilities of a concern is called capital fund. Capital fund is created with surplus revenue and capital receipts and incomes. It is shown on liabilities side of balance sheet.

Format of Income and Expenditure account:

Income and Expenditure Account

Expenditures	Rs	Income	Rs

Example:

Prepare income and expenditure account and balance sheet form the following receipt and payment account of a nursing society.

Receipt and Payment Account

Receipts	Rs.	Payments	Rs.
To Balance at bank - 1-7-90	2,010	By Salaries of nurses	656
To Subscriptions	1,115	By Board, laundry and domestic help	380
To Fees from non members	270	By Rent, rates and taxes	200
To Municipal grant	1,000	By Cost of car	2,000
To Donation for building fund	1,560	By Car expenses	840
To Interest	38	By Drugs and incidental exp.	670
		By Balance c/d	1,247
	5,993		5,993

The society owns freehold land costing $8,000 on which it is proposed to build the nurse's hostel. A donation of $100 received to building fund was wrongly included in subscription account. A bill for medicine purchased during the year amounting to $128 was outstanding.

Solution:

Nursing Society
Income and Expenditure Account

Expenditures	Rs.	Income	Rs.

To Salaries of nurses To Board, laundry and domestic help To Rent, rates and taxes To Cost of car To Car expenses To Drugs and incidental exp. To Outstanding expenses	656 380 200 2,000 840 670 798	By Subscriptions 1,115 Less Wrong inclusion 100 By Fees from non members By Municipal grant By Interest By Deficit	1,015 270 1,000 38 551
	2,874		2,874

Nursing Society
Balance Sheet on 31st December, 1991

Liabilities	**Rs.**	**Assets**	**Rs.**
Building fund 1,560 Add omission 100 Outstanding expenses Capital fund 10,010 Less deficiency 551	1,660 128 9,459	Cash Motor car Land	1,247 2,000 8,000
	11,247		11,247

Difference Between Receipts and Payments and Income and Expenditures Account

Receipts & Payment Account	**Income & Expenditure Account**
1 It is a summary of the cash book	1 It takes the place of profit and loss account in non-trading concerns.
2 It begins with an opening balance and ends with a closing balance.	2 Does not commence with any balance
3 It records all sums received and paid whether they relate to revenue or capital items	3 It includes revenue items only
4 It include all sums actually received during	4 It includes the items relating to year for

	the year whether they relate to the past, current or next year.		which it is prepared. Provision is made for all outstanding expenses and accrued income.
5	The receipts are shown on the debit side and the payments on the credit side.	5	Income is shown on the credit side and expenses on the debit side.
6	It simply ends with a closing balance of cash and does not show the result for the period.	6	It definitely shows whether there has been an excess of income over expenditures or vice versa.
7	It is not accompanied by a balance sheet.	7	It is always accompanied by a balance sheet.

NOTE : PRACTICE MORE SUMS IN THE TEXT FOR BETTER UNDERSTANDING

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