FINANCIAL ACCOUNTING-I
(BACM 15C)
Alied paper
II BCA

by: N.ELAVARASAN

ACCOUNTING

- **Meaning of Accounting**
- Accounting, is an information system is the **process of identifying, measuring and communicating** the economic information of an organization to its users who need the information for decision making.

- **Definition of Accounting**
- American Institute of Certified Public Accountants (AICPA) which defines 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".

Objective of Accounting

- To keeping **systematic record**
- To **ascertain** the **results** of the operation
- To **ascertain** the **financial position** of the business
- To portray (show / describe) the **liquidity position**
- To **protect business properties**
- To facilitate **rational decision – making**
- To satisfy the requirements of **law**

Advantages of Accounting

1. Complete record of all business Transactions
2. Information about Profit/ Loss and Financial Positions
3. Information for important economic decisions
4. Comparative study.
5. Helps to judge managements abilities.
6. Provides factual and interpretive information.
7. Helps in legal compliance.

Limitations of Accounting

1. It gives historical facts not current worth.
2. It reports monetary and financial information not the non monetary and qualitative information.
3. It depends upon personal judgment and conventions.
4. The accounting principles are not fixed and therefore accept different alternatives. So they are not comparable.

Limitations of Accounting

5. Its cost based and changes in prices are not accepted. It does not reflect true money value.
6. It does not show the effect of inflation.
7. The increase in value of assets is not considered unless realised.

Accounting concepts and conventions

ACCOUNTING CONCEPTS

- Business entity concept
- Money measurement concept
- Going concern concept
- Accounting period concept
- Accounting cost concept
- Dual aspect concept
- Matching concept
- Realisation concept
- Accrual concept

ACCOUNTING CONCEPTS

- Accounting concepts define the assumptions on the basis of which financial statements of a business entity are prepared.
- Concepts are those basic assumptions and condition which form the basis upon which the accountancy has been laid.

Business entity concept

This concept assumes that, for accounting purposes, the business enterprise and its owners are two separate independent entities. Thus, the business and personal transactions of its owner are separate. For example, when the owner invests money in the business, it is recorded as liability of the business to the owner. Similarly, when the owner takes away from the business cash/goods for his/her personal use, it is not treated as business expense.

Money measurement concept

- This concept assumes that all business transactions must be in terms of money, that is in the currency of a country. In our country such transactions are in terms of rupees. Thus, as per the money measurement concept, transactions which can be expressed in terms of money are recorded in the books of accounts. For example, sale of goods worth Rs.200000, Rent Paid Rs.10000 etc. are expressed in terms of money, and so they are recorded in the books of accounts. But the transactions which cannot be expressed in monetary terms are not recorded in the books of accounts.
- For example, sincerity, loyality are not recorded in books of accounts because these cannot be measured in terms of money although they do affect the profits and losses of the business concern.

Accounting period concept

- **All the transactions are recorded in the books of accounts on the assumption that profits on these transactions are to be ascertained for a specified period. This is known as accounting period concept. Thus, this concept requires that a balance sheet and profit and loss account should be prepared at regular intervals. This is necessary for different purposes like, calculation of profit, ascertaining financial position, tax computation etc.**

Going concern concept

- This concept states that a business firm will continue to carry on its activities for an indefinite period of time. Simply stated, it means that every business entity has continuity of life. Thus, it will not be dissolved in the near future. This is an important assumption of accounting, as it provides a basis for showing the value of assets in the balance sheet.

Accounting cost concept

- It states that all assets are recorded in the books of accounts at their purchase price, which includes cost of acquisition, transportation and installation and not at its market price. It means that fixed assets like building, plant and machinery, furniture, etc are recorded in the books of accounts at a price paid for them.

Matching concept

- **The matching concept states that the revenue and the expenses incurred to earn the revenues must belong to the same accounting period. So once the revenue is realised, the next step is to allocate it to the relevant accounting period. This can be done with the help of accrual concept** If the revenue is more than the expenses, it is called profit. If the expenses are more than revenue it is called loss. This is what exactly has been done by applying the matching concept.

Dual aspect concept

- Dual aspect is the foundation or basic principle of accounting. It provides the very basis of recording business transactions in the books of accounts. This concept assumes that every transaction has a dual effect, i.e. it affects two accounts in their respective opposite sides. Therefore, the transaction should be recorded at two places. It means, both the aspects of the transaction must be recorded in the books of accounts. Thus, the duality concept is commonly expressed in terms of fundamental accounting equation :

Assets = Liabilities + Capital

.. Therefore, the matching concept implies that all revenues earned during an accounting year, whether received/not received during that year and all cost incurred, whether paid/not paid during the year should be taken into account while ascertaining profit or loss for that year.

- Significance

1. It guides how the expenses should be matched with revenue for determining exact profit or loss for a particular period.
2. It is very helpful for the investors/shareholders to know the exact amount of profit or loss of the business.

- Let us study the following examples
- A Jeweller received an order to supply gold ornaments worth Rs.500000. They supplied ornaments worth Rs.200000 up to the year ending 31st December 2005 and rest of the ornaments were supplied in January 2006. The revenue for the year 2005 for a Jeweller is Rs.200000. Mere getting an order is not considered as revenue until the goods have been delivered.

- Bansal sold goods for Rs.1,00,000 for cash in 2006 and the goods have been delivered during the same year

The revenue for Bansal for year 2005 is Rs.1,00,000 as

Realisation concept

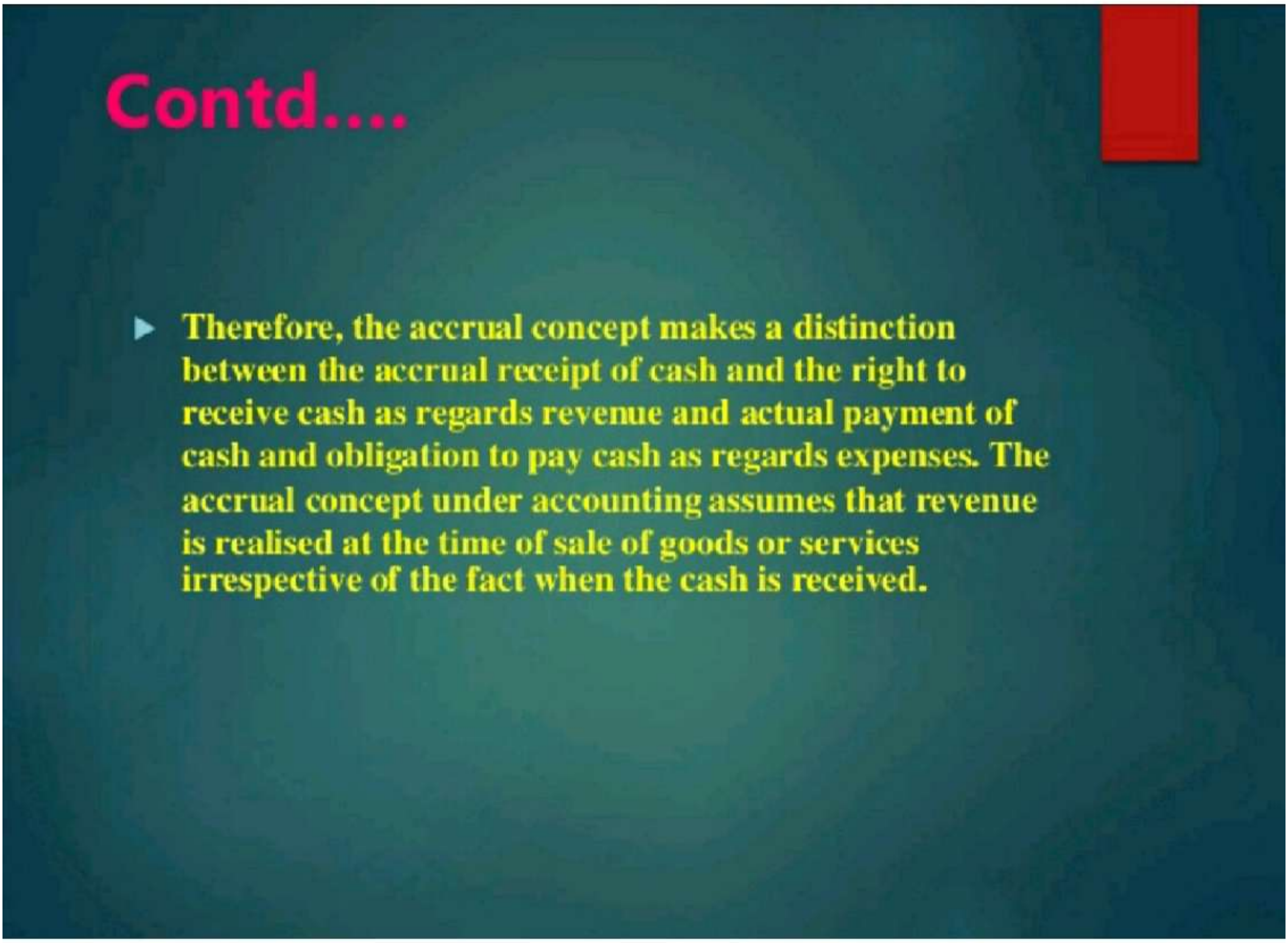
- This concept states that revenue from any business transaction should be included in the accounting records only when it is realised. The term realisation means creation of legal right to receive money. Selling goods is realisation, receiving order is not. In other words, it can be said that : Revenue is said to have been realised when cash has been received or right to receive cash on the sale of goods or services or both has been created.
- The concept of realisation states that revenue is realized at the time when goods or services are actually delivered.

Accrual concept

- The meaning of accrual is something that becomes due especially an amount of money that is yet to be paid or received at the end of the accounting period. It means that revenues are recognised when they become receivable. Though cash is received or not received and the expenses are recognised when they become payable though cash is paid or not paid. Both transactions will be recorded in the accounting period to which they relate.

ACCOUNTING CONVENTIONS

- Consistency
- Full Disclosure
- Materiality
- Conservatism


Contd….
Therefore, the accrual concept makes a distinction between the accrual receipt of cash and the right to receive cash as regards revenue and actual payment of cash and obligation to pay cash as regards expenses. The accrual concept under accounting assumes that revenue is realised at the time of sale of goods or services irrespective of the fact when the cash is received.

ACCOUNTING CONVENTION

- An accounting convention refers to common practices which are universally followed in recording and presenting accounting information of the business entity.
  Conventions denote customs or traditions or usages which are in use since long. To be clear, these are nothing but unwritten laws.
  The accountants have to adopt the usage or customs, which are used as a guide in the preparation of accounting reports and statements. These conventions are also known as doctrine.

Convention of consistency

- The convention of consistency means that same accounting principles should be used for preparing financial statements year after year. A meaningful conclusion can be drawn from financial statements of the same enterprise when there is comparison between them over a period of time. But this can be possible only when accounting policies and practices followed by the enterprise are uniform and consistent over a period of time. If different accounting procedures and practices are used for preparing financial statements of different years, then the result will not be comparable.

Convention of full disclosure

Convention of full disclosure requires that all material and relevant facts concerning financial statements should be fully disclosed. Full disclosure means that there should be full, fair and adequate disclosure of accounting information. Adequate means sufficient set of information to be disclosed. Fair indicates an equitable treatment of users. Full refers to complete and detailed presentation of information. Thus, the convention of full disclosure suggests that every financial statement should fully disclose all relevant information. Let us relate it to the business.

Contd.....

The business provides financial information to all interested parties like investors, lenders, creditors, shareholders etc. The shareholder would like to know profitability of the firm while the creditor would like to know the solvency of the business. In the same way, other parties would be interested in the financial information according to their requirements. This is possible if financial statement discloses all relevant information in full, fair and adequate manner.

Convention of materiality

- The convention of materiality states that, to make financial statements meaningful, only material fact i.e. important and relevant information should be supplied to the users of accounting information. The question that arises here is what is a material fact. The materiality of a fact depends on its nature and the amount involved. Material fact means the information of which will influence the decision of its user.

Convention of conservatism

- This convention is based on the principle that "Anticipate no profit, but provide for all possible losses". It provides guidance for recording transactions in the books of accounts. It is based on the policy of playing safe in regard to showing profit .
- The main objective of this convention is to show minimum profit. Profit should not be overstated. If profit shows more than actual, it may lead to distribution of dividend out of capital. This is not a fair policy and it will lead to the reduction in the capital of the enterprise.

Contd......

Thus, this convention clearly states that profit should not be recorded until it is realised. But if the business anticipates any loss in the near future provision should be made in the books of accounts for the same.

. For example, valuing closing stock at cost or market price whichever is lower, creating provision for doubtful debts, discount on debtors, writing off intangible assets like goodwill, patent, etc. The convention of conservatism is a very useful tool in situation of uncertainty and doubts.

Methods of Accounting

- Business transactions are recorded in two different ways.

1 Single Entry

2 Double Entry

1 Single Entry: It is incomplete system of recording business transactions. The business organization maintains **only cash book and personal accounts of debtors and creditors**. So the complete recording c
cannot be made and trail bala
prepared.

Count....,

- **2. Double Entry:** It this system every business transaction is having a **two fold effect** of benefits giving and benefit receiving aspects. The recording is made on the basis of both these aspects. Double Entry is an accounting system that records the effects of transactions and other events in at least two accounts with equal debits and credits.

(a) Preparation of Journal: Journal is called the book of original entry. It records the effect of all transactions for the first time. Here the job of recording takes place.

(b) Preparation of Ledger: Ledger is the collection of all accounts used by a business. Here the grouping of accounts is performed. Journal is posted to ledger.

Count....,

c) **Trial Balance preparation:** Summarizing. It is a summary of ledge balances prepared in the form of a list.

(d) Preparation of Final Account: At the end of the accounting period to know the achievements of the organization and its financial state of affairs, the final accounts are prepared.

CHAPTER AT A GLANCE (Chapter 5)

CHAPTER AT A GLANCE (Chapter 5)

5.07 Ledger

- 5.08.01 Meaning
- 5.08.02 Form of a Ledger
- 5.08.03 Mechanics of Posting
- 5.08.04 Balancing of Ledger Accounts

5.01
Meaning of an Account

An account is a

- summarised record of relevant transactions
- at one place relating to a particular head.
- It records not only the amount of transactions but also their effect and direction.

An account has column for date, particulars, folio number, debit amount and credit amount.

Specimen of Account

Specimen of Account

Name of the Account				
Date	Particular	J.F	Amount(Debit)	Amount(Credit)
Date of Transaction	Name of the Other Account	Page of the Ref. Number of the Sub-journal where it was first recorded	Amount of the Transaction	Amount of the Transaction

5.02
Meaning of Debit and Credit

Under double entry system of book keeping each transaction has two aspects.

- **Debit Aspect** and **Credit Aspect**

- Debit and credit aspects of a transaction form the basis of double entry system.

5.02

Meaning of Debit and Credit

An item recorded

- on the debit side of an account is said to be debited to the account and
- a balance resting on this side is said to be a debit balance.

An item recorded

- on the credit side of an account is said to be credited to the account and
- the balance resting on this side is said to be a credit balance.

5.04
JOURNAL

- **Meaning**
- Journal is that book of accounts in which
- transactions are originally recorded in a chronological order, i.e., as they occur.
- It is the first book of account in which the transactions are recorded.
- An entry made in the Journal is known as a '**Journal Entry'.**

5.04
JOURNAL

- The process of recording a transaction in a Journal is known as **'Journalising'.**
- **The transfer of** Journal entry to a Ledger account is known as 'Posting'.

Specimen of Journal

5.04
JOURNAL

5.05.03 Simple and Compound Journal Entries

Journal entries are of two types namely:

1. Simple Entry and
2. Compound Entry.

5.04
JOURNAL

1. Simple Entry:

A simple entry is one in which only two accounts are affected, viz.,

- one account is debited and
- another is credited with an equal amount.

2. Compound Entry

A compound entry is one in which

- two or more accounts are debited and
- one or more accounts are credited.

5.05
OPENING ENTRY

Opening Entry

The entry passed to record the closing balances of the previous year is called the **Opening Entry.**

- While passing an opening entry all Assets Accounts are debited and
- all Liabilities Accounts are credited.

5.06
SUB-DIVISION OF JOURNAL

Journal is sub-divided into subsidiary Journal books. These are

- **Cash Book** – to record cash and bank transactions.
- **Purchases Book** – to record credit purchases of goods dealt in or used in manufacturing.
- **Purchase Returns Book** – to record return of purchased goods.
- **Sales Book** – to record credit sale of goods dealt in.

5.06
SUB-DIVISION OF JOURNAL

- **Sales Returns Book** – to record return of goods sold.

- **Bills Receivable Book** – to record Bills Received.

- **Bills Payable Book** – to record Bills Payable.

- **Journal Proper** – to record all other transactions that are not recorded in any of the above sub-journals.

5.07
LEDGER

5.08.01 Meaning

A Ledger can be defined as

- a "book or register which contains,
- in a summarised and classified form,
- a permanent record of all transactions."
- It is an important book of accounts, as the Trial Balance is drawn from it and with the help of Trial Balance Final Account is prepared.

Specimen of Ledger

5.08
LEDGER

5.08.04 Balancing of Ledger Accounts

- After posting the transactions,
- accounts are balanced every year or
- after a certain period.

Balancing an account means

- that the two sides of account are totalled and
- the difference in total of the two sides is
- written on the side whose total is short.

What do you know about Trial Balance ?

INTRODUCTION AND DEFINITION.

- Trial balance is a list of debit and credit balances of all ledger accounts. It is prepared at the end of an accounting period.
- **Trial balance is prepared in the statement form which shows debit balances and credit** balances of all accounts in the ledger, therefore it is called as a ***"Statement of Balance"***
- "**Trial balance is a statement, prepared with the debit and credit** balances of ledger accounts to test the arithmetical accuracy of the books" – **J.R. Batliboi.**

INTRODUCTION AND DEFINITION:

"It is a list or abstract of the balances or of total debits and total credits of accounts in a ledger, with the purpose being to determine the quality of posted debits and credits and establish a basic summary for final statements" **By Eric Kohler.**

"It is schedule or list of those debit and credit balances which are extracted from various accounts in the ledger and balances of cash in hand, Cash at bank as shown by Cash Book are also included in it**." By R N Carter**

Advantages of Trial Balance

The advantages of the trial balance are:

i. It helps to ascertain the arithmetical accuracy of the book-keeping work done during the period.

ii. It supplies in one place ready reference of all the balances of the ledger accounts.

iii. If any error is found out by preparing a trial balance, the same can be rectified before preparing final accounts.

iv. It is the basis on which final accounts are prepared.

Objectives of trial balance

The objectives of preparing a trial balance are:

- **To check the arithmetical accuracy of the ledger accounts.**
- **To locate the errors.**
- **To facilitate the preparation of final accounts.**

Format of Trial Balance

Trial balance of a XYZ Ltd as on……………..

Particulars / Name of the account	L.F.	Dr. Amount	Cr. Amount
Total			

Particulars	L.F.	Dr. Amount	Particulars	L.F.	Cr. Amount
Total			Total		

Points to be noted :

- ✓ Date on which trial balance is prepared should be mentioned at the top.
- ✓ Name of Account column contains the list of all ledger accounts.
- ✓ Ledger folio of the respective account is entered in the next column.
- ✓ In the debit column, debit balance of the respective account is entered.
- ✓ Credit balance of the respective account is written in the credit column.
- ✓ The last two columns are totalled at the end.
- ✓ A debit balance is either an asset or loss or expense; and
- ✓ A credit balance is either a liability or income or gain.

Limitations of Trial Balance

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

Prepare Trial Balance as on 31.12.2016 from the following balances of Mr. Balan.

Capital	3,40,000	Purchases	94,000
Creditors	13,000	Sales Returns	3,400
Drawings	4,000	Purchases Return	2,400
Salaries	38,200	Carriage inwards	1,400
Bill Receivable	5,800	Printing & Stationery	5,000
Bills Payable	7,000	Stock	29,900
Debtors	16,000	Machinery	50,000
Sales	1,44,000	Wages	5,000
Insurance	2,200	Rent	1,600
Land	2,50,000	Interest received	1,700
Commission received	800	Electricity charges	2,400

[Answer : Rs. 5,08,900]

Prepare Trial Balance as on 31.12.2012 from the following balances of Ms. Fathima.

Drawings	74,800	Purchases	2,95,700
Stock (1.1.2012)	30,000	Discount received	1,000
Capital	2,50,000	Discount allowed	950
Furniture	33,000	Sales	3,35,350
Sundry creditors	75,000	Rent	72,500
Printing charges	1,500	Sundry expenses	21,000
Bank loan	1,20,000	Bills receivable	52,500
Freight	3,500	Carriage outwards	1,500
Income tax	9,500	Insurance 1,200	
Machinery	2,15,400	Bills payable 31,700	

[Answer : Rs. 8,13,050]

Prepare trial balance as on 31.3.2013 from the following balances of Mrs. Sujatha.

Drawings	43,000	Purchases	2,98,000
Capital	2,12,000	Sales	3,64,000
Sundry creditors	61,500	Salaries	44,950
Bills Payable	22,000	Sales return	500
Sundry Debtors	55,000	Purchases return	2,550
Bills Receivable	72,600	Travelling expenses	12,300
Loan from Shameem	2,50,000	Commission paid	250
Furniture & Fittings	12,250	Discount earned	2,000
Opening stock	2,23,500	Cash in hand	65,450
Cash at bank	86,250		

[Answer : Rs. 9,14,050]

Prepare a Trial balance from the following as on March 31st, 2016.

Particulars	Amount	**Particulars**	Amount
Stock	60,000	General Trade Expenses	1,350
Purchases	1,50,000	Returns Inwards	5,400
Capital	70,000	Discount allowed	600
Drawings	22,000	Interest & Commission	
Sales	2,50,000	paid	430
Traveling Expenses	1,320	Bad Debts	800
Salaries	11,200	Sundry Creditors	60,000
Rent, Taxes & Insurance	5,600	Cash in hand	2,060
Returns Outwards	2,600	Sundry Debtors	92,000
Advertising	840	Furniture	10,000
Wages	7,000	Plant & Machinery	20,000
Bank Overdraft	20,000	Buildings	12,000

The following balances are extracted from the books of Mr.Senthil. Prepare Trial Balance as on 30.6.2014.

Capital	4,70,200	Machinery	1,58,800
Cash in hand	6,000	Sundry Debtors	48,000
Building	3,20,000	Repairs	5,400
Stock	33,000	Insurance premium	3,300
Sundry creditors	26,000	Sales	2,90,000
Commission paid	750	Telephone charges	6,450
Rent & Taxes	6,300	Furniture	11,000
Purchases	1,65,000	Discount earned	1,100
Salaries	70,600	Loan from Mohammed	51,000
Discount allowed	650	Reserve fund	5,900
Drawings	5,000	Bills receivable	8,600
Bad debts	1,350	Bills payable	6,000

[Answer : Rs. 8,50,200]

Following are the balances extracted from the ledger of Mr. Ketan. Prepare a Trial Balance as on 31st Dec. 2015.

Particulars	Rs.	Particulars	Rs.
Capital A/c	40,000	Purchases	26,500
Drawings A/c	4,000	Printing & Stationery	3,000
Sundry Creditors	18,440	Rent & Taxes	2,500
Motor Car Expenses	3,000	Office Expenses	7,000
Sales	29,560	Commission paid	5,000
Trade Expenses	8,500	Sundry Debtors	18,000
Insurance	1,030	Discount Allowed	2,970
Opening Stock	8,500	Interest Received	2,000

1. Prepare a trial balance from the following balances of Sh. Keshav Chand as at 31st march, 2016 :-

Name of Accounts	₹	Name of accounts	₹
Opening stock	20,000	Sales return	10,000
Purchases	80,000	Rent	2,000
Purchases return	10,000	Salaries	5,000
Furniture	1,00,000	Drawing	8,000
Machinery	50,000	Capital	1,50,000
Debtors	30,000	Cash in hand	20,000
Sales	1,60,000	Creditors	2,000

Sol :- Trial Balance of Sh. Keshav Chand
as at 31st March, 2016

Name of Accounts	L.F.	Dr. Balance ₹	Cr. Balance ₹
Opening stock		20,000	
Purchases		80,000	
Purchases return			10,000
Furniture		1,00,000	
Machinery		50,000	
Debtors		30,000	
Sales			1,60,000
Sales return		10,000	
Rent		2,000	
Salaries		5,000	
Drawing		8,000	
Capital			1,50,000
Cash in hand		20,000	
Creditors			2,000
Total		3,22,000	3,22,000

2. From the following ledger balances prepare trial balance :-

Capital = ₹ 30,000

Rent Outstanding = ₹ 2,000

Amount due to Jyoti = ₹ 10,000

Amount due from Rahul = ₹20,000

Drawing = ₹ 5,000

Goodwill = ₹ 10,000

Purchases = ₹ 1,00,000

Sales = ₹ 1,50,000

Discount allowed = ₹ 1,000

Discount received =₹ 2,000

Land & Building = ₹ 50,000

Advertisement = ₹4,000

Sol. Trial Balance of ....
as at ....

Name of Accounts	L.F.	Dr. Balance ₹	Cr. Balance ₹
Capital			30,000
Rent outstanding		2,000	
Amount due to Jyoti			10,000
Amount due from Rahul		20,000	
Drawing		5,000	
Goodwill		10,000	
Purchases		1,00,000	
Sales			1,50,000
Discount allowed		1,000	
Discount received			2,000
Land & Building		50,000	
Advertisement		4,000	
Total		1,92,000	1,92,000

2. Prepare a trial balance from the following balances taken as at 31st march 2016 :-

	₹		₹
Capital	2,50,000	Miscellaneous receipt	3,600
Drawings	24,000	Bad debts	7,100
Debtors	57,000	Bills receivables	5,000
Creditors	28,500	Loan from X	20,000
Land & Building	1,80,000	Interest on X's loan	3,000
Plant	1,20,000	Cash in hand	8,400
Stock 1-4-2015	22,800	Goodwill	10,000
Factory expenses	16,600		
Office expenses	7,700		
Purchases return	6,000		
Stationery	500		
Freight	2,500		
Purchases	2,15,300		
Sales	3,80,000		
Miscellaneous expenses	8,200		

EXERCISE (DO IT YOURSELF)

1. From the following ledger balances prepare trial balance :-

Capital = ₹ 20,800

Creditors = ₹ 15,000

Goodwill = ₹ 12,000

Rent outstanding = ₹ 1,480

Interest received = ₹ 2,000

Discount received = ₹ 1,680

Debtors = ₹ 26,000

3. The following is incorrect trial balance. Redraft it in a correct form :-

Trial Balance of ....
for the year ending 31st march 2017

Name of Accounts	L. F.	Dr. Balance ₹	Cr. Balance ₹
Sundry Debtors		12,200	
Sundry Creditors			9,200
Opening stock		15,600	
Purchases		53,500	
Purchases return		2,100	
Cash in hand		11,000	
Machinery		40,200	
Goodwill			10,000
Sales			86,200
Sales return			7,800
Loan from Ram		20,000	
Interest on Ram's Loan		3,000	
Bill receivables			6,400

Continue....

Name of Accounts	L. F.	Dr. Balance ₹	Cr. Balance ₹
Capital		57,000	
Life Insurance Premium		5,600	
Carriage		1,600	
Advertisement		2,500	
Discount received		1,500	
Investment		8,000	
Interest on investment		800	
Total		1,77,000	1,77,000

RECTIFICATION OF ERRORS

What to Learn?

- Meaning of Rectification of error
- Types of Errors:
  - One Sided Errors
  - Two Sided Errors
- Suspense Account
- Problems of Rectification of errors

What is Rectification of Error?

- Once an error is error is located. It should be properly corrected. The correction of accounting error in a systematic manner is called rectification of errors.

For verifying: C = W + R

Types of Errors:

- Two Sided Errors (Not effecting Trial balance agreement)
  - Error of Omission
  - Error Of Commission
  - Error of Original Entry
  - Compensating Error
  - Error of Principal
- One Sided Errors (Effecting Trial balance agreement)
  - Suspense Account

Trial Balance:

- **Trial balance** is a list of closing balances of Ledger account on a certain date and is the first step towards the preparation of financial statements

Example:

- Purchase of goods from Arshad & Co Rs. 4000 was omitted to be recorded in the books.

Correct Entry	Wrong Entry	Rectify Entry
Purchases 4000	Nil	Purchases 4000
Arshad & Co 4000	Nil	Arshad & Co 4000

Two Sided Error

- **Error of Omission:**

It means that a transaction has been completely omitted from the original books of accounts.

- ✓ It will neither appear on the debit side nor on Credit side of the Trial balance.

Two Sided Error

- **Error of Omission:**

It means that a transaction has been completely omitted from the original books of accounts.

✓ It will neither appear on the debit side nor on Credit side of the Trial balance.

Two Sided Error:

- **Error of Commission:**

It means that a transaction instead of being recorded in the right account, has been recorded in the wrong account of the same class.

Example:

- Purchase of goods from Arshad & Co Rs. 4000 was omitted to be recorded in the books.

Correct Entry	Wrong Entry	Rectify Entry
Purchases 4000	Nil	Purchases 4000
Arshad & Co 4000	Nil	Arshad & Co 4000

Example:

- A sale of Rs. 3000 to A was wrongly debited to the account of B.

Correct Entry	Wrong Entry	Rectify Entry
A 3000	B 3000	A 3000
Sales 3000	Sales 3000	B 3000

Two Sided Error:

- **Error of Original Entry:**

It means that the amount of a transaction has been wrongly recorded in the journal and the same wrong amount was also posted in the Ledger.

Example:

- Goods sold to Mr. Naeem for Rs. 5000 was wrongly recorded in the sales journal at Rs. 500 and the same amount of Rs. 500 is posted both in the Mr. Naeem A/c and in sales A/c.

Correct Entry	Wrong Entry	Rectify Entry
Mr. Naeem 5000	Mr. Naeem 500	Mr. Naeem 4500
Sales 5000	Sales 500	Sales 4500

Two Sided Error:

- **Error of Principal:**

Error of principle mean errors caused due to violation of generally accepted accounting principles e.g., incorrect allocation between capital and revenue items.

- ✓ Treating capital expenditure as a revenue expenditure.
- ✓ Treating revenue expenditure as a capital expenditure.

Errors of principle:

- **Revenue Expenditure**
  - Short term benefits
  - Routine Expenses

  (occurrence again and again to continue business operation)

- **Capital Expenditure**
  - Long term benefits
  - Not in routine

Example:

- Paid wages on installation of new Machinery on Rs. 10,000 but recorded as a wages expenses.

Correct Entry	Wrong Entry	Rectify Entry
Machinery 10,000	Wages Exp. 10,000	Machinery 10,000
Cash 10,000	Cash 10,000	Wages Exp. 10,000

Two Sided Errors:

- **Compensating Errors:**

It means that some errors in amount have occurred on the opposite side of two or more accounts and have cancelled themselves in the net result.

✓ Compensate

One Sided Errors:

- When these words like wrongly debited, wrongly credited and posted are used in any statements then there is error in one account. This is called **One Sided Error**.

Examples:

- Purchase A/c has been wrongly debited with Rs.5000 instead of Rs.4000. On the other hand Asif A/c has been wrongly credited with Rs.1500 instead of Rs.1000 and Sales A/c has been wrongly credited with Rs.6000 instead of Rs.5500.

Correct Entry	Wrong Entry	Rectify Entry
Purchase 4000	Purchase 5000	Purchase 1000
Asif 1000	Asif 1500	Asif 500
Sales 5500	Sales 6000	Sales 500

BANK RECONCILIATION STATEMENT

LEARNING OBJECTIVES

- Distinguish and explain items appearing in the Bank Statement/Pass Book and Cash book (Bank Column).
- Understand the need and the purpose of preparing the Bank Reconciliation Statement
- Prepare the Bank Reconciliation Statement

Reporting cash in the balance sheet

- Cash is listed first in balance sheet
- The term Liquid Assets.
- Current asset section of balance sheet.
- Purpose of balance sheet.

Non considered Cash Equivalents

- Cash equivalent investment in stocks, bonds.
- Marketable Securities.

CASH EQUIVALENTS

- Short term investments.

- Similar items in the balance sheet.

- First asset shown in balance sheet.

Evaluating Solvency

- Study of Balance Sheet.
- Users of a company financial statement.
- Creditors need to know the amount of liquid resources.

Line of Credit

- Arrangements of the Line of Credit.
- The meanings of Line of Credit.
- Borrow Money.
- Liability to the Bank.

1.THE DEFINITION OF THE BANK RECONCILIATION STATEMENT

- A bank reconciliation is a schedule explaining any differences between the balance shown in bank statement and the balance shown in Cash book.

2.THE PURPOSE OF THE BANK RECONCILIATION STATEMENT

- It reflects actual bank balance position
- Detect mistake in cash book or Pass book
- Prevent frauds in recording banking transactions
- Explain any delay collection of checks
- It identifies valid transaction recorded by one party but not by other

Cash book

- A book in which record all the transaction relating to cash receipt and payments in detail is called cash book
- Prepared or maintain by company

Kinds:

1. Simple : maintained by small enterprise
2. Cash book with discount
3. Cash book with discount and cash column
4. Petty cash book

Bank statement

- Report released (on a fixed date every month) by banks that lists deposits, withdrawals, checks paid, interest earned, and service charges or penalties incurred on an account. It shows the cumulative effect of these transactions the account's balance, up to the date the report was prepared

4. NATURE OF THE CASH BOOK AND THE BANK STATEMENT.

- The balance in the cash book is an asset to the company, therefore:

Cash book

(A debit represents an increase)	(A credit represents a decrease)

3. REASONS FOR DIFFERENCES BETWEEN THE CASH BOOK AND THE BANK STATEMENT.

- The bank balances as shown in the cash book and the bank statement seldom agree. There are various reasons for this. A statement is used to reconcile the two balances.

- There are some transactions recorded by the depositor but missed by the bank.

- Similarly, there are transactions appearing on the bank statement and not recorded by the company.

- **The balance as per the bank statement is a liability to the bank, therefore:**

Bank statement

	Dr.	Cr.	Balance
	(represents decreases)	(represents increases)	(represents the amount owed to the clients)

Reasons

- Unpresented cheques
  - They are cheques issued by the firm that have not yet been presented to its bank for payment.
- Deposit transit/uncredited cheques
  - Cash receipts recorded by the depositor but not included in bank statement.

Reasons

- Service charges
  - They are charges made by the bank to the company for banking services used.
- Dishonored cheques/NSF cheques
  - They are cheques deposited but subsequently returned by the bank due to the failure of the drawer to pay.

Reasons

- Interest allowed by the bank
  - They are interest received for deposits or fixed deposits.
- Miscellaneous bank charges and credits
  - banks charge for services – such as printing cheques, handling collection of notes receivable and processing NSF cheques.

Rules

- Some important rules for debit and

	CR	(-)	(+)
4. Dishonored cheques • Cheques received and deposited but dishonor • Cheque issued but dishonor	DR	(+)	(-)
5. If anything C. in the bank statement only	Dr	(+)	(-)
6. If anything Dr. in the bank statement only	Cr	(-)	(+)
7. Overstated/overcast			
• Payment side of cashbook overstated	Dr	(+)	(-)
• Receipts side of cashbook overstated	Cr	(-)	(+)
8. Expenses paid by bank Cr. (-) (+) 9. expenses charged by bank	Cr.	(-)	(+)
• Bills directly paid bank charges			
• Insurance premium service charges			
• Interest charged by bank interest on overdraft			

Scanned by CamScanner

	DR/Cr	D	C
1. **Unpresented cheques** • **Cheques issued but not yet presented** • **Cheques drawn but not enchased** • **Cheques paid for payment but not cleared** • **Cheques issued returned by bank on technical grounds**	Dr	+	-
2. Uncredited cheques • Cheques deposit but not credited by the bank • Cheques paid into the bank but not cleared by bank • Cheques sent to bank but not collected by bank	Cr	-	+
3. All types of income/credit memo/memorandum • Income given by bank • Income collected by bank	Dr	+	-

In BANK STAEMENT.

ADD:-
- Deposit in Transit.
- Bank errors.
- Wrongly recorded cheques.

LESS:-
- Outstanding cheques
- Unpresented cheques
- Unpaid cheques.

etc.

Steps

1. Check the bank statement and the cash book to see the items which have been omitted.
2. Arrange the paid cheques in sequence by serial number and compare each cheque with the corresponding entry in the cheque register.
3. Add balance to the depositor's accounting record(credit memorannda) issued by the bank.
4. Deduct from the balance per the depositor record which have not been recorded by the depositor.
5. Make appropriate additions or deductions to correct errors.

IN CASH BOOK :-

ADD :-

- Interest Earned
- Interest Received
- Notes Receivable
- Recording Error

LESS:-

- NSF cheques
- Service Charges
- Interest Allowed.