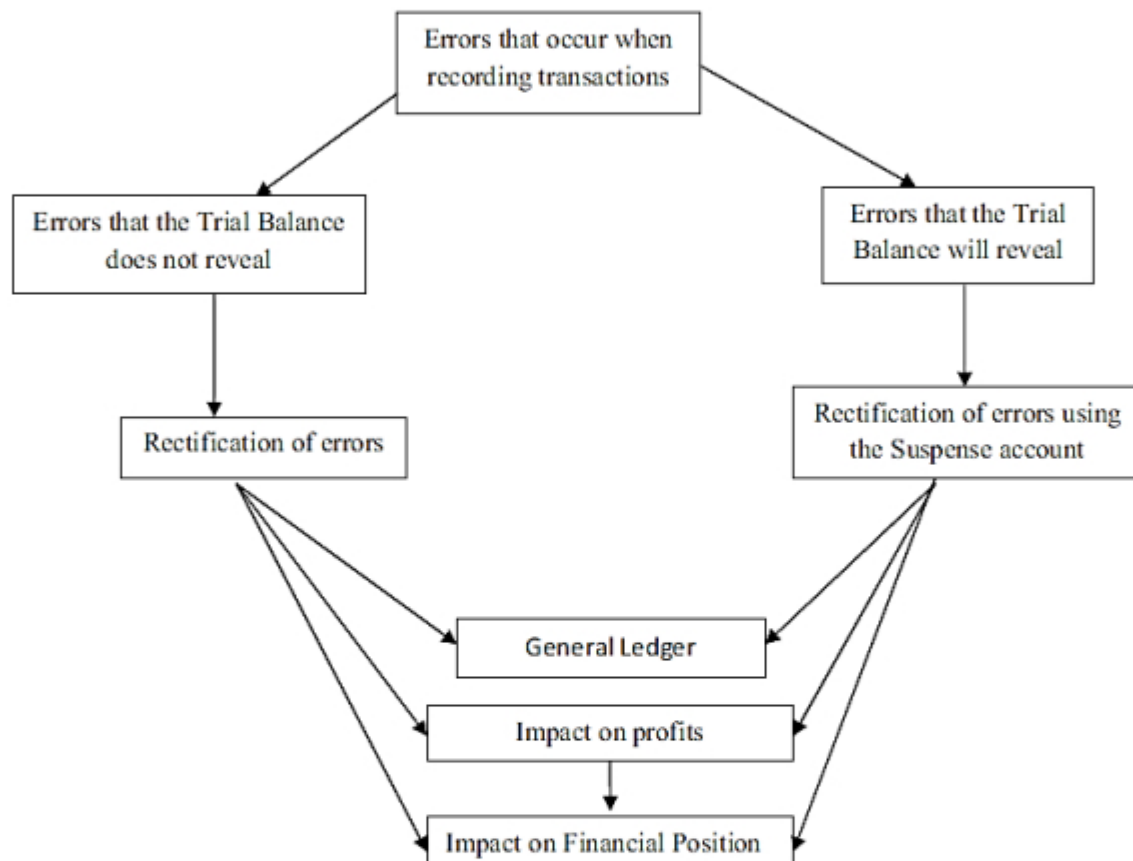


**4.10 | Errors in accounting**

- Errors in accounting
- Errors that are not revealed from a Trial Balance
- Errors that are revealed from a Trial Balance
- Rectifying errors using General Journal
- Impact on financial performance and financial position

**Summary****Errors in accounting**

- Occasions when errors can occur:
  - When recording transactions in the prime entry books
    - 20,000 credit purchases not recorded in the Purchases Journal
  - When posting transactions to the ledgers
    - Purchases Journal total of 50,000 not posted to the Purchases a/c
  - When balancing ledger accounts
    - Purchases a/c total understated by 5,000
  - When preparing the Trial Balance
    - Purchases a/c balance not extracted to the Trial Balance
- Importance of correcting accounting errors:
  - Errors should be corrected before preparing financial statements to provide accurate information to stakeholders to make effective decisions.

**Types of errors**

- There are two types of errors that can occur when posting transactions:
  - Errors that are not revealed by the Trial Balance
  - Errors that are revealed by the Trial Balance
- Whichever way the error is made, it is necessary to use the General Journal to make the necessary correcting entries.

**Errors that are not revealed by the Trial Balance**

<b>Error of omission</b>	<ul style="list-style-type: none"> <li>• Occurs when a source document related to a transaction is completely omitted from the prime entry books.</li> <li>• Transaction is omitted in the prime entry books and therefore not posted to ledgers. Hence, no impact on the Trial Balance.               <ul style="list-style-type: none"> <li>○ Example: Credit sales of 20,000 omitted from accounts</li> <li>○ <i>Correction: Enter double entry in the relevant accounts</i></li> </ul> </li> </ul>
<b>Error of commission</b>	<ul style="list-style-type: none"> <li>• Occurs when the value of a transaction is recorded higher (overstatement) or lower (understatement) than the original value.</li> <li>• Transaction value entered is incorrect. However, both DR &amp; CR sides are equal numerically, so no impact on the Trial Balance.               <ul style="list-style-type: none"> <li>○ Example: Credit sales of 20,000 recorded as 10,000 in accounts</li> <li>○ <i>Correction: Adjust the figures in both accounts accordingly</i></li> </ul> </li> </ul>
<b>Error of principle</b>	<ul style="list-style-type: none"> <li>• Occurs when transactions are recorded contrary to accounting fundamentals.</li> <li>• Transaction is entered in the wrong account. However, both DR &amp; CR sides are equal numerically, so no impact on the Trial Balance.               <ul style="list-style-type: none"> <li>○ Example: Purchases of furniture 50,000 debited to Purchases a/c</li> <li>○ <i>Correction: Enter to the correct a/c and then reverse the incorrect a/c</i></li> </ul> </li> </ul>
<b>Error of compensation</b>	<ul style="list-style-type: none"> <li>• Occurs when one error is compensated by another error of similar value.</li> <li>• Transaction entered incorrectly in two different accounts. However, the numerical effect is cancelled out, so no impact on the Trial Balance.               <ul style="list-style-type: none"> <li>○ Example: Interest income is overstated by 2,000 whilst rent income is also overstated by 2,000 in accounts</li> <li>○ <i>Correction: Reverse the incorrect entries accordingly</i></li> </ul> </li> </ul>
<b>Error of double posting</b>	<ul style="list-style-type: none"> <li>• Occurs when the double entry for one transaction is posted twice.</li> <li>• Transaction is posted twice, but DR &amp; CR sides remain equal, so no impact on the Trial Balance.               <ul style="list-style-type: none"> <li>○ Example: Credit sales of 20,000 entered twice in accounts</li> <li>○ <i>Correction: Reverse the second entry in both accounts</i></li> </ul> </li> </ul>

**Errors that are revealed by the Trial Balance**

Omission of one entry in the transaction	<ul style="list-style-type: none"> <li>Occurs when only one entry is recorded in accounts.               <ul style="list-style-type: none"> <li>Example: Credit sales of 20,000 recorded only in Sales a/c</li> <li><i>Correction: Enter in the other a/c and reverse the Suspense a/c</i></li> </ul> </li> </ul>
Recording values as two different amounts	<ul style="list-style-type: none"> <li>Occurs when the amounts recorded in both accounts are different               <ul style="list-style-type: none"> <li>Example: Credit sales of 20,000 credited to Sales a/c correctly but debited to Debtors a/c as 2,000</li> <li><i>Correction: Adjust the difference in the relevant a/c and reverse the Suspense a/c</i></li> </ul> </li> </ul>
Recording double entry in the same side of accounts	<ul style="list-style-type: none"> <li>Occurs when the amounts are recorded in the same side of accounts.               <ul style="list-style-type: none"> <li>Example: Credit sales of 20,000 credited to both Sales a/c and Debtors a/c</li> <li><i>Correction: Reverse the double effect and remove from Suspense a/c</i></li> </ul> </li> </ul>
Errors when balancing an account in the ledger	<ul style="list-style-type: none"> <li>Occurs when the totals are posted erroneously when balancing ledgers.               <ul style="list-style-type: none"> <li>Example: Sales a/c total of 20,000 erroneously posted as 40,000 in Sales a/c</li> <li><i>Correction: Adjust the difference and remove from Suspense a/c</i></li> </ul> </li> </ul>
Errors when preparing the Trial Balance	<ul style="list-style-type: none"> <li>Occurs when preparing the Trial Balance:               <ul style="list-style-type: none"> <li>➤ omitting a balance from the ledgers to the Trial Balance</li> <li>➤ posting an incorrect value to the Trial Balance</li> <li>➤ entering in the incorrect column in the Trial Balance                   <ul style="list-style-type: none"> <li>Example: Sales a/c total 20,000 erroneously posted as 40,000 in Trial Balance</li> <li><i>Correction: Error is in the Trial Balance only; not ledgers. So adjust only the Trial Balance value and reverse the Suspense a/c</i></li> </ul> </li> </ul> </li> </ul>

**Suspense account**

- When there is a difference between the DR & CR balances in the Trial Balance, a balancing figure is posted to a Suspense account temporarily until the errors are identified and corrected. When the errors are resolved, the Suspense account balance will become zero.
- Process of creating a suspense account:
  - Identify the difference in the Trial Balance (whether DR or CR side)
  - Insert the difference in the respective deficit side
  - Create the suspense a/c accordingly

**Impact on financial performance and financial position**

- The errors may result in an understatement/overstatement of financial performance (profits) and financial position (assets and liabilities).
- The errors made when posting transactions can impact financial results, whilst accurate financial statements can be produced once the errors are corrected.
- In order to arrive at accurate financial results, a profitability reconciliation statement can be prepared, taking into account only the errors that impact income and expenses.

