

Financial Accounting

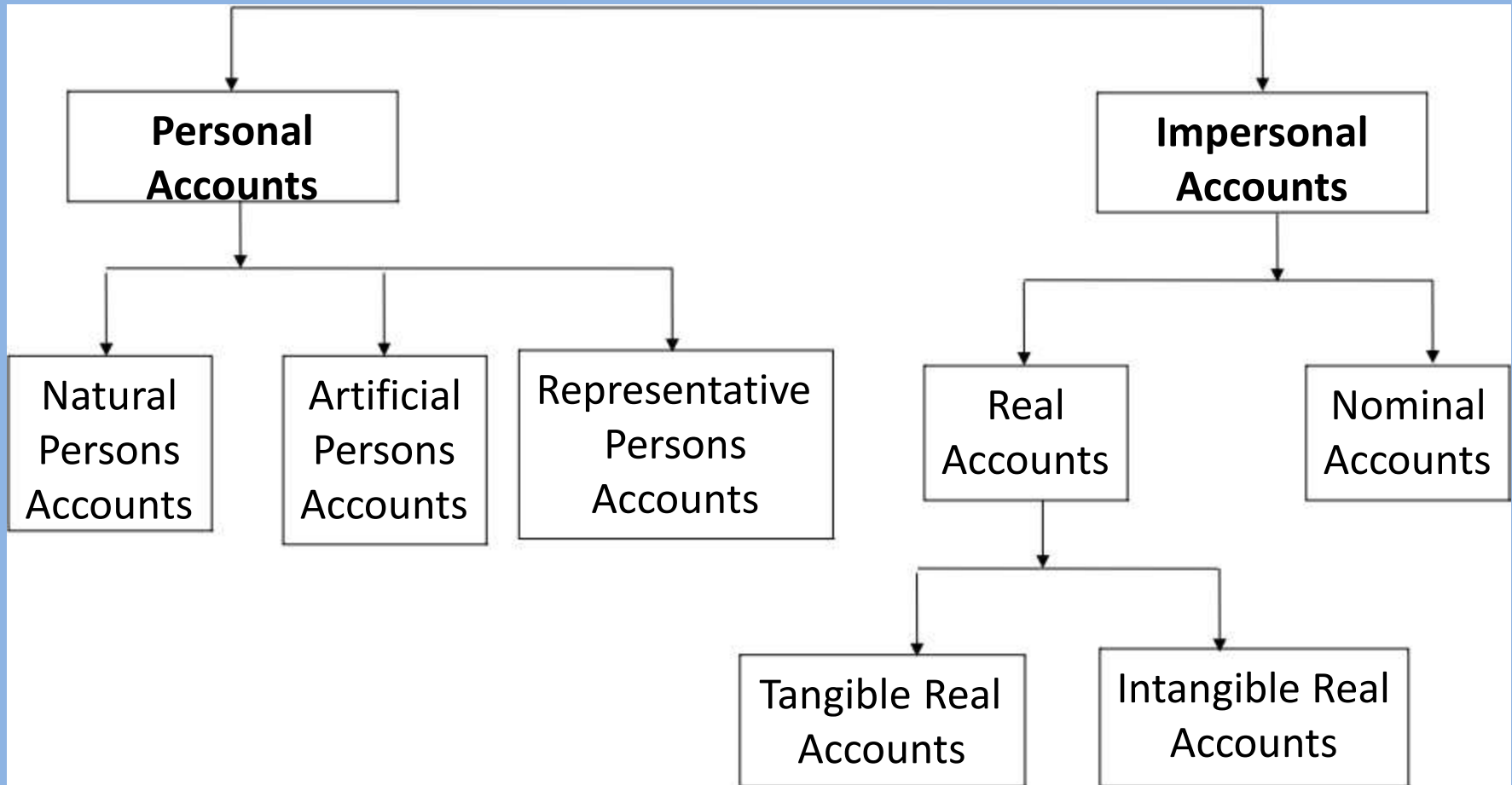
ACCOUNTING PRINCIPLES

JOURNAL & LEDGER PREPARATION

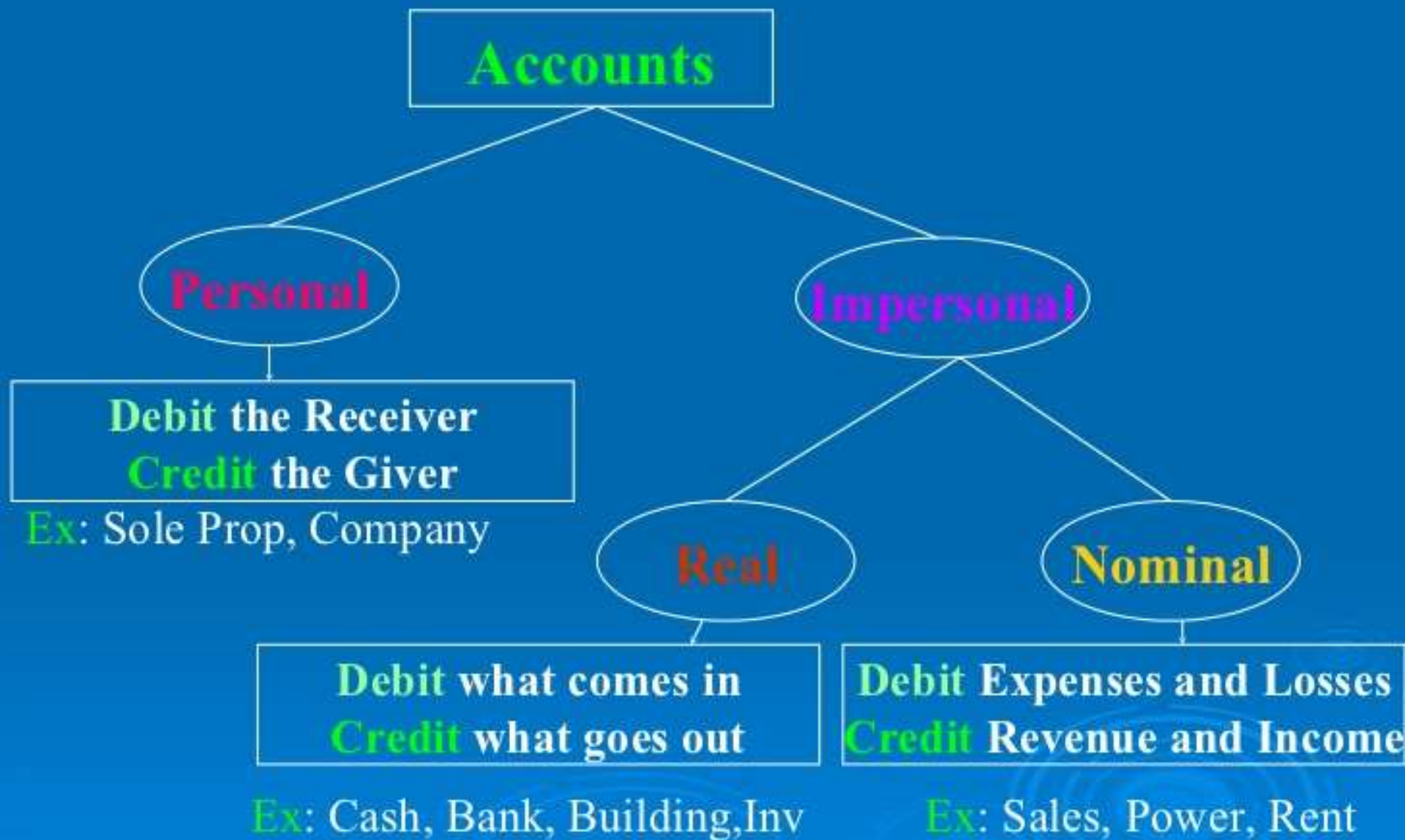
Account

- It is a unit of information that represents business records.
- There are five types of accounts: Asset, Liability, Equity, Revenue and Expense.

Classification of Accounts



Rules of Accounting



Combination of Rules

Dr Personal A/c

Cr Real A/c

Ex: Drawings or Advance to Employee,
Payment to Supplier

Dr Real A/c

Cr Personal A/c

Ex: Capital invested, Payment Received
from Customer

Dr Real A/c

Cr Real A/c

Ex: Purchase of Inventory by Cash

Dr Real A/c

Cr Real A/c

Ex: Cash withdrawal or Deposit

Dr Real A/c

Cr Nominal A/c

Ex: Interest Recd by Cash, Cash Sales

Dr Nominal A/c

Cr Real A/c

Ex: Rent Paid by Cash

Dr Personal A/c

Cr Nominal A/c

Ex: Interest Accrued on Investment,
Dividend accrued on Investment

Dr Nominal A/c

Cr Personal A/c

Ex: Hire Purchase Charges accrued, Interest
Payable, Salary Payable

Combination of Accounting Rules

		Debit			
Credit	Combination	Personal	Real	Nominal	
	Personal	X	✓	✓	
	Real	✓	✓	✓	
	Nominal	✓	✓	X	

Combination of Accounting Rules

➤ Both **Debit and Credit cannot be Personal Accounts**

- EX 1: Siva paid Cash to Ajay. The Entry Cannot be
 - Ajay A/c Dr
 - Siva A/c Cr
- The Correct entries are as follows. In Ajay set of Books

Cash A/c Dr	1000
Siva A/c Cr	1000

In Siva set of Books

Ajay A/c Dr	1000
Cash A/c Cr	1000

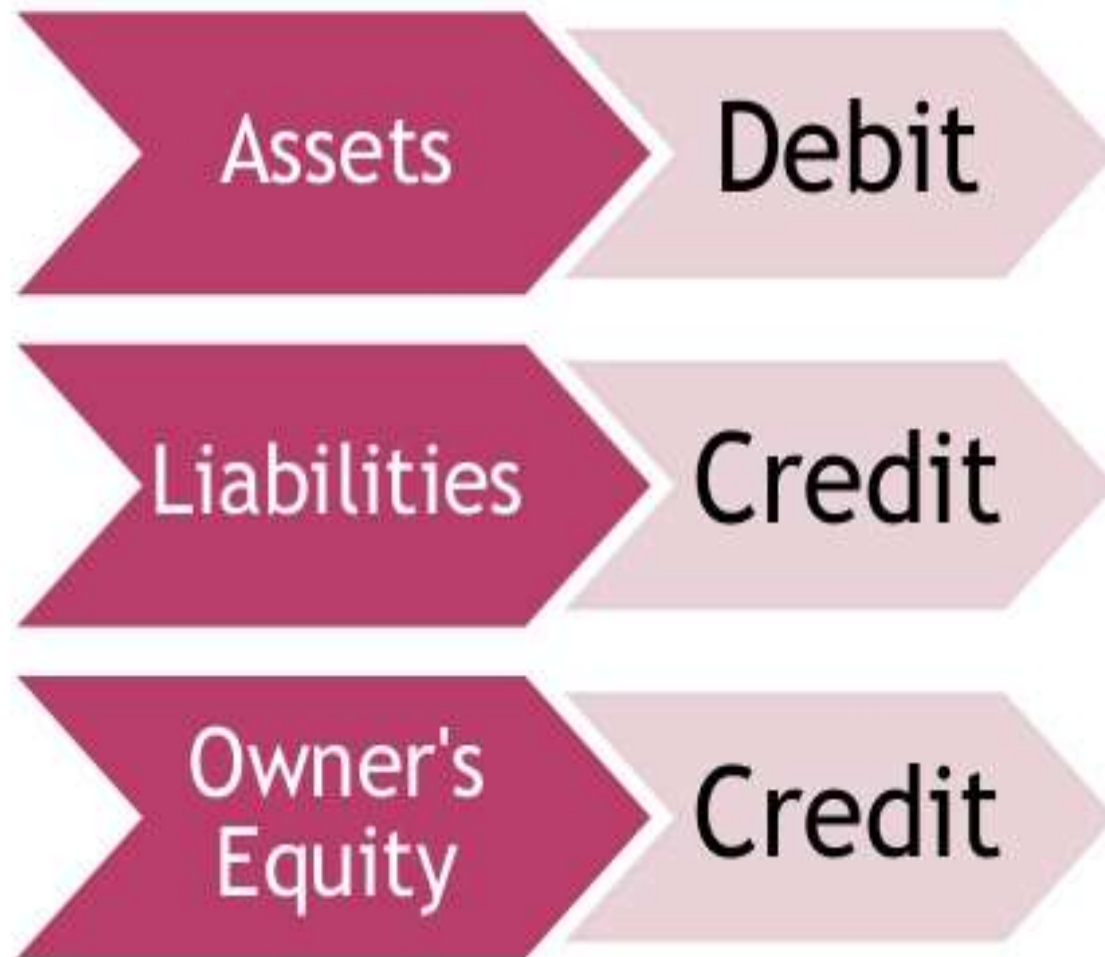
Similarly Both **Debit and Credit cannot be Nominal Accounts**

Note: Remember this important aspect and therefore You will not commit any mistake in Debit and Credit

Rules of Double Entry System

Accounts	Rules
Personal	<ul style="list-style-type: none">• Debit the receiver• Credit the giver
Real	<ul style="list-style-type: none">• Debit what comes in• Credit what goes out
Nominal	<ul style="list-style-type: none">• Debit all expenses and losses• Credit all incomes and gains

NATURE OF ACCOUNTS (BS)



NATURE OF ACCOUNTS (P&L)



Revenue

Credit

Expenses

Debit

DEBIT AND CREDIT

Assets

Increase

Debit

Liabilities

Increase

Credit

Owner's
Equity

Increase

Credit

DEBIT AND CREDIT

Revenue

Increase

Credit

Expense

Increase

Debit

Accounting cycle

Recording monetary transactions in a systematic manner

Journal entries

Ledger

Trial balance

Trading and Profit & Loss Account

Balance Sheet

Journal

- The word journal is derived from the Latin word '**Journ**' which means **a day**.
- Journal means a day book where in day-to-day business transactions are recorded in a chronological order.
- The process of recording a transaction in the journal is called **Journalisation**.
- The entries made in the book are called **journal entries**.

The ruling of the journal is as follows:-

Journal

Date	Particular	LF	Debit Rs [Dr]	Credit Rs [Cr]
Year Month Date	Name of account to be debited. To, Name of account to be credited. [Narration]			

Items in Journal

- **Date:** The first column deals with the date of transaction.
- **Particulars :** In the first line write about debit aspect and in the second line write about credit aspect. In the third line write regarding brief explanation of the entry (narration).
- **Ledger Folio (L.F.):** It denotes page number on which its journal entry is found.
- **Debit:** Fourth column deals with the amount to be debited.
- ***Credit:*** Fifth column deals with the amount to be credited.

1. Examine the following transactions and determine the two accounts affected according to the double entry book keeping.

(a) Bought goods for cash	Rs. 2000
(b) Sold goods for cash	Rs. 1000
(c) Received cash from Kulkarni	Rs. 500
(d) Received interest on loan	Rs. 180
(e) Paid salary to Manager	Rs. 5000
(f) Paid rent	Rs. 1500
(g) Purchased goods from Desai & Co.	Rs. 1500
(h) Goods sold on credit to Lalit	Rs. 1000
(i) Purchased motor car equipment from Mumbai Motor Agency and paid	Rs. 8900
(j) Purchased machinery from India Tools Limited	Rs. 7000
(k) Withdrew cash for household expenses	Rs. 300

- Solution : The two account involved in the transactions are :
- (a) Purchases a/c and cash a/c
- (b) Sales a/c and cash a/c
- (c) Kulkarni's a/c and cash a/c
- (d) Interest a/c and cash a/c
- (e) Salary a/c and cash a/c
- (f) Rent a/c and cash a/c
- (g) Purchases a/c and Desai & Co. a/c
- (h) Sales a/c and Lalit's a/c
- (i) Motor car equipment a/c and cash a/c
- (j) Machinery a/c and India Tools Ltd. a/c
- (k) Drawings a/c and cash a/

EX : Identify the debit and credit aspects of the following transactions under Mriet co. giving reasons for the same.

1. Mr. Soumya Gupta started business with a capital Rs.5,00,000
2. He purchased machinery on credit from Ram Rs.40,000
3. He purchases goods for cash Rs.1,00,000
4. He sold goods to Satish for Rs.50,000
5. He paid rent for the month Rs.5,000
6. He received commission Rs.10,000
7. He received cash from Satish Rs.20,000
8. He withdrew for personal use Rs.5,000
9. He purchased goods from Ratan Rs.40,000
10. He returned goods to Ratan Rs.6,000

<i>S. No.</i>	<i>Aspects</i>	<i>Debit or Credit</i>	<i>Reason</i>
1.	Cash Capital	Debit Credit	Increase in asset Increase in capital
2.	Machinery Ram	Debit Credit	Increase in asset Increase in liability
3.	Goods (Tangible asset) Cash	Debit Credit	Increase in asset Decrease in asset
4.	Satish Goods (Tangible asset)	Debit Credit	Increase in asset Decrease in asset
5.	Rent Cash	Debit Credit	Increase in expense Decrease in asset
6.	Cash Commission	Debit Credit	Increase in asset Increase in income
7.	Cash Satish	Debit Credit	Increase in asset Increase in liability
8.	Capital (Drawings) Cash	Debit Credit	Decrease in capital Decrease in asset
9.	Goods (Asset) Ratan	Debit Credit	Increase in asset Increase in liability
10.	Ratan Goods (Asset)	Debit Credit	Decrease in liability Decrease in asset.

EX:3.Show how the following transactions appear in the Journals of Ram and Rahim.

1. Ram bought goods from Rahim Rs. 1,000.
2. Rahim bought goods for cash Rs. 8,000 from Ram.
3. Rahim received from Ram Rs. 5,000 and allowed him discount Rs. 250.
4. Ram sold goods to Rahim Rs. 7,000
5. Rahim supplied goods worth Rs. 2500 for Ram's domestic use.
6. Ram received Rs. 5,000 from Rahim for repairing the private car of Rahim.

<i>Date</i>	<i>Particulars</i>	<i>LF</i>	<i>Debit</i>	<i>Credit</i>
1	PURCHASE a/c <div>Dr</div> TO RAHIM'S a/c (Being goods purchased from Rahim)		1,000	1,000
2	Cash a/c Dr. To Sales a/c (Being cash sales to Rahim)		8,000	8,000
3	Rahim's a/c Dr. To Cash To Discount (Being payment made and discount received)		5,250	5,000 250

4	Rahim's a/c Dr. To Sales a/c (Being goods sold)		7,000	7,000
5	Drawings a/c Dr. To Rahim's a/c (Being goods bought from him for domestic use)		2,500	2,500
6	Repairs a/c Dr. To Cash (Being repair charged of car paid to Ram)		5,000	5,000

Ledger

- It is a book which contains various accounts. It is in 'T' form.
- It is a summary statement of all the transactions relating to a person, asset, expense or income which have taken place during a given period of time and shows their net effect.
- It is designed to accommodate the various accounts maintained by a trader.
- The process of transferring the entries from the journal into the ledger is called *posting*.

Ledger Format

Dr	Name of Account
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Cr

Date	Particular	F	Amount	Date	Particular	F	Amount
	To, Name of credit A/c		Rs		By, Name of debit A/c		Rs

EX: Rama, a businessman, entered into the following transactions with Krishna on the following dates. Draft the ledger account of Krishna and balance the same.

January 2020,

Date 1. Opening debt of Krishna to Rama Rs. 100

3. Sold goods to Krishna subject to 10% trade discount Rs. 1000

8. Krishna returned goods Rs. 100

9. Sold goods to Krishna and received a bill accepted by him Rs. 200

10. Krishna became insolvent and Rama realized from his assets Rs. 850

In the books of RAMAKRISHNA'S A/C

<i>Date</i>	<i>Particulars</i>	<i>Amt.</i>	<i>Date</i>	<i>Particulars</i>	<i>Amt.</i>
2020 Jan 1.	To Balance b/d	100	Jan 2020		100
3.	To Sales a/c (1000-100)	900	8.	By sales returns	
				By cash	850
			10.	By P & L a/c —loss amounts not realisable	250
9.	To Bills Receivable	200			
		1200			1200

Trial Balance

- A list of balances of the ledger accounts at a point of time is called trail balance.
- The balances of all the ledger accounts are extracted and are written up in a statement known as Trial Balance and finally totaled up to see if the total of debit balances is equal to the total of credit balances. It
- is a list of ledger account titles and their respective balances.
- As per double entry system, every debit equals to corresponding equal credit. To prove this, statements of debits and credits will be prepared by accountant. This statement is called trail balance.

Trial Balance

Trial Balance is a list of balances extracted from the ledger accounts at the end of an accounting period. Since the balances in ledger accounts are effects of double entries, the total of debit balances should be equal to total of credit balances.

Uses of Trial Balances

- 1) It is the basis of preparation of Final Accounts.
- 2) It helps in verifying the arithmetical accuracy of ledger accounts.

The two sides of the trial balance will not tally if a mistakes has taken place in the following.

- a) Posting
- b) Totaling
- c) Balancing.

Nature of Balances:

In the normal circumstances,

- i) All assets accounts & also dues from persons will show debit balances.
- ii) All liabilities accounts will show credit balances.
- iii) All expenses account will show debit balances.
- iv) All income accounts will show credit balances.

Trial Balance Format

Sl No	Particulars	LF	Debit Balance Rs	Credit Balance Rs