

UNIT 9 ERRORS AND THEIR RECTIFICATION

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9.0 OBJECTIVES

- After studying this unit you should be able to:
- describe the types of errors which are usually committed in the process of accounting
 - explain the procedure of locating the errors
 - rectify errors before preparing the final accounts
 - explain the use and preparation of suspense account
 - rectify errors located during subsequent accounting years
 - compute the effect of rectifying errors on profits.

9.1 INTRODUCTION

You know that the Trial Balance is prepared to verify the arithmetical accuracy of accounting records. When the Trial Balance does not tally, it means there are errors in the books of account. These errors must be detected and rectified before preparing the final accounts, otherwise they will not reflect a true and fair view of the state of affairs of the business. In this unit you will learn about the types of errors which are usually committed in the process of accounting, the procedure for locating and rectifying those errors, and the effect of rectifying-entries on the profits of the business.

9.2 TYPES OF ERRORS

The errors may occur while recording transactions in the subsidiary books, or while posting them into the ledger or at the time of closing or balancing various accounts, or while preparing the Trial Balance itself. Whatever the stage at which the error is committed, it may be either an error of principle or an-error of clerical nature. All errors can therefore be broadly divided into (a) the errors of principle, and (b) the clerical errors. The clerical errors can be further divided into (i) errors of omission, (ii) errors of commission, and (iii) compensating errors. Let us now discuss these errors one by one.

1 Errors of Principle: When a transaction has not been recorded as per the rules of debit and credit, or it violates some other principle, the errors so arising are called 'errors of principle'. Examples of such errors are:

- i) A credit purchase of fixed assets recorded in the Purchases Journal instead of the Journal Proper. This results in debiting the Purchases Account instead of the concerned fixed asset account. This is an error of **principle** because it amounts to treating an expenditure of capital nature as a revenue expenditure.
- ii) An expenditure incurred on repairs of machinery debited to Machinery Account. You know repairs to machinery is a revenue expenditure **and** should have been debited to Repairs to Machinery Account. Debiting this expenditure to Machinery Account amounts to treating it as a capital expenditure. It is therefore an error of principle.
- iii) Salary paid to Ganga Ram recorded in Cash Book as a payment to **Ganga** Wam. This would result in debiting **Ganga** Ram's personal account instead of treating it as an expense and debiting it to Salaries Account.

The errors of principle do not affect the Trial Balance because they simply amount to debiting or crediting wrong accounts, the debit-credit **correspondence** is not upset.

2 Errors of Omission: When a transaction is completely or partially **omitted** to be recorded in books of account, it is called an 'error of **omission**'. If the transaction is not **recorded** in the subsidiary books or its posting is completely **omitted**, it is called an 'error of **complete omission**'. If, however, the posting is done in one account but omitted from the other, it is called an 'error of **partial omission**'. For example, if a credit purchase of goods from **Shyam** is not recorded in the Purchases Journal or a credit purchase of furniture from Ram is recorded in the Journal **Proper** but no posting is done in any of the two accounts involved, then these will be termed as errors of complete omission. If the purchase of goods from **Shyam** is recorded in the Purchases Journal but is not posted in **Shyam's** Account, it will be called an error of partial omission. Other examples of partial omission are: **Omission** in carrying forward the total from one page to the other, omission to balance an account, and so on.

The errors of complete omission do not affect the Trial Balance. But the errors of partial omission would certainly cause disagreement of the Trial Balance because they would lead to either short debit or short credit.

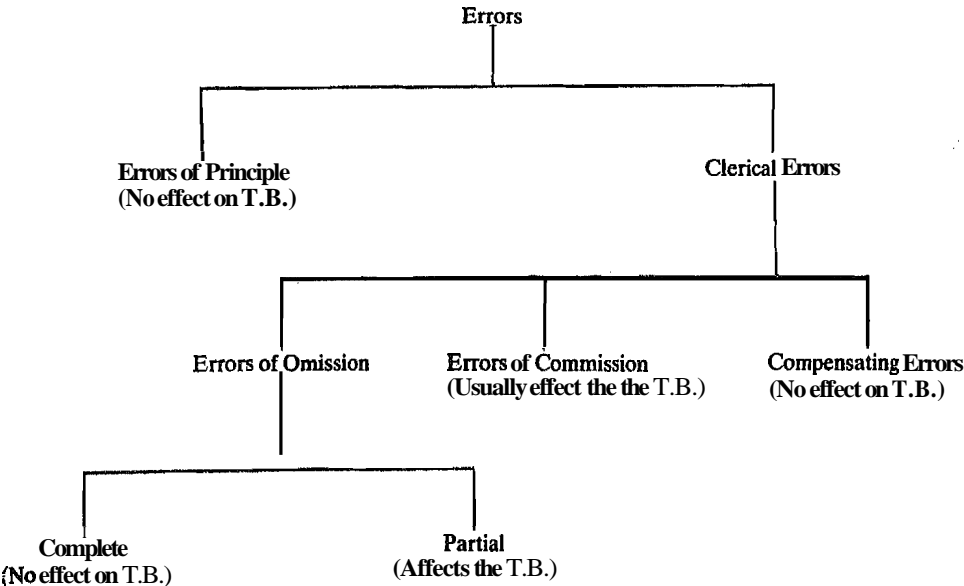
3 Errors of Commission: When an error is committed in recording a transaction with wrong amount, or posting it to a wrong account or the wrong side of an account, it is called an 'error of **commission**'. For example, a credit sale of Rs. 720 is recorded in the Sales Journal as Rs. 270, or it is **posted** to the debit of C's Account instead of B's Account or it is posted on the credit side of B's Account. Errors like double posting, wrong totalling, wrong carry forward, wrong balancing etc. are also regarded as errors of **commission**. Such errors usually cause disagreement in the Trial Balance. But, the **errors committed** while recording the transaction in subsidiary books or **posting it to a wrong account** (but with **correct amount** and on the correct side) do not affect the Trial Balance.

4 Compensating Errors: Those errors which **nullify** the effect of each other are called 'compensating **errors**'. In other words, compensating errors refer to such a group of errors wherein the effect of one error is **compensated by** the effect of other error or errors. For example, while posting an entry of Rs. 200 to the debit of Ram's Account we wrongly wrote Rs. 400. Then, while posting an entry of Rs. 500 to the debit of some other account we wrote Rs. 300. The first error led to a higher debit of Rs. 200 whereas the second error resulted in a lower debit of Rs. 200. Thus, the effect of the first error is nullified by the effect of the second error. Take another example. The Purchases Journal is overcast in excess by Rs. 1,000 which means the Purchases Account will be debited in excess by Rs. 1,000. The Sales Journal also, by mistake, is overcast by Rs. 1,000 which means the Sales Account will be credited in excess by Rs. 1,000. These two mistakes, together, result in an excess debit of Rs. 1,000 as well as an excess credit of Rs. 1,000. Thus, they cancel out of the effect of each other. Such errors do not affect the Trial Balance.

Look at Figure 9.1. It shows various types of errors and indicates whether a particular type of error affects the Trial Balance or not.

Figure 9.1

Types of Errors and their Effect on Trial Balance



Check Your Progress A

1 Give two examples of errors of principle.

.....

.....

2 What do you mean by compensating errors?

.....

.....

.....

3 A few errors committed in Rao's books are given below. State in each case the type of **error** involved and whether it would affect the Trial Balance or not.

- i) Sales of Rs. 950 to **Ram** completely omitted from books of account.
- ii) Purchases of Rs. 720 **from Shyam** entered in the Purchases Journal as Rs. 700.
- iii) Purchases Journal is overcast by Rs. 1,000.
- iv) Sales Returns Journal is undercast by Rs. 200.
- v) Amount paid **to Agarwal** wrongly posted **to** the debit of **Mittal's** Account.
- vi) Bank overdraft is shown under the debit balances column in the Trial Balance.
- vii) Sales of Rs. 500 to Sadiq entered in Sales Journal as sales to Mushtaq.
- viii) Wages paid for installation of machinery debited to Wages Account.

S. No.	Type of Error	Whether it affects the Trial Balance
i)	Yes/No
ii)	Yes/No
iii)	Yes/No
iv)	Yes/No
v)	Yes/No
vi)	Yes/No
vii)	Yes/No
viii)	Yes/No

9.3 LOCATION OF ERRORS

You have learnt the types of errors which are usually committed in the **process** of accounting. These errors must be located and rectified before preparing the final **accounts**. You know that some of the errors affect the agreement of the Trial Balance while some do **not**. The errors such as errors of principle, errors of complete omission and errors of compensating nature which do not affect the Trial Balance are difficult to locate. They are usually found out during the course of audit **or** when the statement of accounts is received by the business or sent to customers for confirmation. However, the **location** of errors of omission and **commission** which affect the Trial Balance is not so difficult. The following routine procedure is usually adopted for locating such errors.

- a) Check the totals of both the debit and the credit columns of the Trial Balance.
- b) If the difference still persists, ascertain the exact amount of difference; and then
 - i) see whether an account having that balance has **been** omitted from the Trial Balance. Suppose the debit **column** in Trial Balance is short by Rs. 630, it is just possible that an account with a debit balance of Rs. 630 has not **been** entered in the Trial Balance.
 - ii) **check** whether an account with a balance equal to that difference has been entered twice in the Trial Balance.
 - iii) take half the amount of difference, see whether there is any account with such balance in the Trial Balance, and if so, check whether it is entered in the correct column or not. If an account with a debit balance of **Rs. 315** has been entered in the credit column, the debit column **becomes** short by Rs. 630.
- c) Verify whether (i) the balances of all the accounts are included in the Trial Balance (ii) they are entered in the correct column, and (iii) their amounts have been correctly written.
If no errors are found **upto** this stage, or the errors located **have** been duly corrected, but still the Trial Balance does not tally, there is need to take **further** action. **You** may take the following steps:
 - d) Check the totals of the lists of sundry debtors and sundry creditors.
 - e) Check the **totals** and balances of all accounts in the ledger.
 - f) Check **the** totals and the postings of all subsidiary books.
 - g) Check the postings of all amounts equal to **the** difference in the trial **balance**. It is possible that a posting has been omitted. Similarly, check the postings of all amounts equal to half the difference. It is possible that the amount has been posted on the wrong side of the concerned account.
 - h) See that correct amounts have been brought forward from the previous pages.
 - i) Verify that all opening balances have been correctly entered in various accounts.
 - j) **Compare** the current year's Trial Balance with that of the previous year. Any **variation** noticed should be carefully checked.

The procedure outlined above, if carefully **followed**, should normally reveal **all** this errors. The errors are then rectified and a revised Trial Balance is prepared. If no other errors exist, the revised Trial Balance is likely to tally.

9.4 RECTIFICATION OF ERRORS

Any error when located must be rectified. The **rectification** should **not be made** by overwriting or by **striking off the wrong entry**. This would destroy the authenticity of the books of account. Hence, the errors should always be corrected by making suitable entries called rectifying entries. For purposes of rectification the errors are divided into two categories: (i) one-sided errors, and (ii) two-sided errors.

One-sided Errors: Certain errors affect only one side of **an** account, either the debt side or the credit side. Such errors are called 'one-sided errors'. Examples of one-sided errors are:

i) Rs. 100 received from Deshmukh was posted to his account as Rs. 10. It means Deshmukh's Account has been credited with Rs. 10 instead of Rs. 100 and there is no mistake in the Cash Book. Thus, this error has affected only one-side of an account.

ii) The **Purchases** Book is overcast by Rs. 1,000. This will affect **the** debit side of Purchases Account where the total of the Purchases Book is posted, and no **other** account is affected.

Two-sided Errors: Certain errors may affect two or more accounts. Such errors are **called** 'two-sided errors'. Examples of two-sided errors are:

- i) A credit sale of **Rs. 1,080** to **Anand** was wrongly recorded in the Sales **Book** as Rs. **1,800**. This error will affect two accounts. **viz., Anand's** Account and Sales Account. **Anand's** Account has been debited by Rs. 1,800 instead of Rs. 1,080. The Sales Account **has** also been credited by an additional amount of Rs. 720 (Rs. 1,800—1,080) because the Sales Book will show a higher total.
- ii) A sale of Rs. 500 made to Kamal has been posted on the debit side of **Kishore's** Account. This error will affect two accbunts viz., Kamal's Account and Kiskore's Account. An entry of Rs. 500 does not appear on the debit side of **Kamal's** Account **whereas** Kishore's Account has been wrongly debited with that amount.

9.4.1 Rectification of one-sided Errors

Generally errors are corrected by passing suitable journal entries. You know passing a journal **entry** means debiting one account and crediting another. But in the case of one-sided error **only** one account is involved. So it cannot be corrected by passing the journal entry. It is rectified simply by noting the correction on the appropriate side. Take the first **example** of one-sided error. **Deshmukh's** account was credited short by Rs. 90. This will be corrected by an additional entry for Rs. 90 on the credit side of his account as follows:

Deshmukh's Account			
Dr.			Cr.
		By Difference in amount received from him posted on...	Rs. 90

In the second example of one-sided error, the Purchases Account is debited in **excess** by Rs. 1,000. This will be corrected by crediting the Purchases Account with Rs. 1,000 as follows:

Purchases Account			
Dr.			Cr.
		By Overcasting of Purchases Book for the month of...	Rs. 1,000

The wrong total in the Purchases **Book** will be circled with red ink and the correct total entered above or below the circle. The person doing the rectification will also put his initials.

9.4.2 Rectification of Two-sided Errors

You have **learnt** that one-sided errors are corrected simply by noting the correction on the appropriate side of the account affected by the error. They cannot **be rectified** by suitable **journal** entries **because only** one account is involved. But, the two-sided **errors** are mostly rectified by journal entries. It is because such errors affect two or **more** accounts and in most cases **the** debit **and** credit are **equally** affected. Take the **case** of first example of two-sided error given earlier. A credit sale of **Rs. 1,080 to**

Anand was wrongly recorded in the Sales Book as Rs. 1,800. The two accounts affected are: (i) **Anand's** Account which shows an excess debit of Rs. 720 and (ii) Sales Account which stands credited in excess by Rs. 720. To rectify this error we must credit **Anand's** Account with Rs. 720 and debit the Sales Account with Rs. 720. So, a **journal entry** can be passed as follows:

		Rs.	Rs.
Sales Account	Dr.	720	
To Anand			720
(Being sales of Rs. 1,030 to Anand wrongly recorded in the Sales Book as Rs. 1,800 now rectified)			

Take the second example of two-sided errors given earlier. A sale of Rs. 500 made to Kamal was posted to the debit side of Kishore's Account. The two accounts affected are: (i) **Kamals** Account which has not been debited by Rs. 500, and (ii) Kishore's **Account which has** been wrongly debited with Rs. 500. To rectify this **error** we have to debit **Kamal's Account** with Rs. 500 and credit Kishore's Account with Rs. 500. So journal entry for the rectification of this error will be as follows:

		Rs.	Rs.
Kamal	Dr.	500	
To Kishore			500
(Being rectification of wrong debit to Kishore for sales made to Kamal)			

Look at illustrations 1 and 2 and study **how** various errors have been corrected.

Illustration 1

- How would you rectify the following errors in the books of **Kiran & Co**?
- 1 The Sales Return **Book** has been undercast by Rs. 500.
 - 2 The total of the Bills Receivable **Book amounting** Rs. 4,500 has been posted to the credit of Bills Receivable Account.
 - 3 While posting Purchases Book to the ledger the personal account of **Kumar** has been credited with Rs. 221 instead of Rs. 212.
 - 4 Rs. 60,000 paid for the purchase of a TV set for the proprietor is debited **to** General Expenses Account.
 - 5 An amount of **Rs. 1,000** paid **by** Pran has been credited to the account of Praneet.
 - 6 Goods sold to Inder for Rs. 1,200 have been entered in the Purchases Book.

Solution:

- 1 This error will be rectified by entering **Rs. 500** on the debit side of Sales Returns Account by writing "To **Undercasting** of Sales Returns Book for the Month of **Rs. 500**".
- 2 **This** error will be rectified by entering an amount of Rs. 9,000 on the debit side of Bills Receivable Account by **writing** "To Wrong posting of the total of Bills Receivable **Book** on the opposite side., Rs. 9000".
- 3 Kumar's Account **has** been credited with an excess amount of Rs. 9 (Rs. 221 - Rs. 212). This error will be rectified by debiting his account with Rs. 9 by writing "**To Difference** in amount posted from the Purchases **Book** on... .., Rs. 9".
- 4 The following journal entry is required for rectification.

		Rs.	Rs.
Drawings A/c	Dr.	10,000	
To General Expenses A/c			10,000
(Being rectification of purchase of TV for the proprietor wrongly debited to General Expenses A/c)			

Journal entry is required for rectification:

Errors and their Rectification

Prancet	Dr.	Rs. 1,000	Rs. 1,000
To Pran			

(Being rectification of wrong credit to **Praneet** for the amount paid by Pran)

6 The following journal entry is required for rectification:

Inder	Dr.	Rs. 2,400	Rs. 1,200
To Purchases A/c			1,200
To Sales A/c			1,200

(Being rectifying entry for sale to **Inder** wrongly entered in the Purchases **Book**)

Illustration 2

How would you rectify the following errors:

- Rs. 3,000 received for the sale of old machinery has been wrongly posted to Sales Account.
- Rs. 600, the cost of repairing the machinery has been wrongly charged to Machinery Account.
- Goods purchased for **Rs. 500** ~~from Sanjay~~ has been wrongly debited to **Furniture** Account,
- A sale of Rs. 600 has been wrongly credited to the customer's account.
- A payment of Rs. 400 on account of rent has been posted twice to the Rent Account.
- An item of Rs. **197** has been debited to a personal account as **Rs. 179**.

Solution:

1 The following journal entry is required for rectification:

Sales A/c	Dr.	Rs. 3,000	Rs. 3,000
Machinery A/c			

(Being rectifying entry for sale of machinery credited to Sales Nc)

2 The following **journal** entry is required for **rectification**:

Repairs A/c	Dr.	Rs. 600	Rs. 600
To Machinery A/c			

(Being rectification of wrong debit to **Machinery A/c** instead of Repairs **A/c**)

3 The following journal entry required for **rectification**:

Purchases A/c	Dr.	Rs. 500	Rs. 500
To Furniture A/c			

(Being rectifying entry for purchase wrongly debited to Furniture N c)

4 **This** error will be rectified by debiting the customer's account with Rs. 1,200 (double of Rs. 600) by writing "To-Wrong posting ~~from~~ Sales Book on the credit side on Rs. 1,200."

5 This error will be rectified by entering Rs. 400 on the credit side of the Rent Account by writing "By Double **posting from** Cash Book ~~on~~.....**Rs. 400**".

6 The personal **A/c** has been debited Rs. 18 short (Rs. 197–179. **To** rectify this error, the personal **A/c** will be debited with difference by **writing "To** Difference in **amount** posted on, Rs. 18."

Check **Your Progress** **B**

Following errors have been detected:

- a) A credit purchase of goods ~~from~~ **Chetan** amounting to Rs. 15,000 has been **wrongly passed** through the Sales Book.
- b) A sale of an old typewriter for Rs. 800 was passed through the Sales Book.
- c) Rs. 700 withdrawn for personal use has been debited to General Expenses Account.
- d) A credit sale of Rs. 2,300 to Jatin was omitted ~~from~~ Sales Book.
- e) Purchase of a wooden cupboard for Rs. 3,000 has been passed through the Purchases Day Book.

You are required to **answer** the following questions.

1. In case of each error name the accounts **affected**.

- a) i)
ii)
iii)
- b) i)
ii)
- c) i)
ii)
- d) i)
ii)
- e) i)
ii)

2. In case of each error, write the effect on each account **involved**.

- a) i)
ii)
iii)
- b) i)
ii)
- c) i)
ii)
- d) i)
ii)
- e) i)
ii)

9.5 SUSPENSE ACCOUNT AND RECTIFICATION

You have learnt the **method** of rectifying the **errors**. This method is **used** for rectifying the errors located before preparing the final accounts. After the corrections have **been** made, a **revised Trial Balance** is prepared which should **normally tally**. But, if it **does not tally**, it means there are **still some** errors **which** have not been detected. As **considerable** time and effort have already been **spent in locating and rectifying the** errors, it **may** not be possible to wait any longer **because** it **will** delay the **preparation** of final accounts. **Hence, in such a** situation the usual **practice is** to place the difference to **Suspense Account** and **tally the** Trial Balance for the **time** being. If **the** total of the debit **column** in the **Trial Balance is more than** the total of its credit

column total, the difference is **placed** to the credit of Suspense Account and the Trial Balance will **tally**. Similarly, if the credit column total is **more** than the debit column total the difference is placed to the debit of **Suspense Account**. The Suspense Account thus created is shown in the Balance Sheet and is **carried** forward to the next year. Note that the Suspense Account is not the **result** of any transaction, It merely **represents** the net effect of errors which still remain undetected. Therefore, during the next accounting year, after the errors are located and rectified, the Suspense Account will get closed. Let us now understand how errors will be corrected in the following year. As for the two-sided errors, there is **no** change in the **method** of rectification. These errors do not affect the agreement of Trial Balance and hence do not involve the Suspense Account. They are rectified by **means** of the journal entries as usual. This is not the case in respect of one-sided errors. When one-sided errors were to be corrected before preparing the Trial Balance we did it by writing an appropriate note in the concerned account. But, when they are to be corrected during the next year i.e., after Suspense Account has been created, the rectification will be through an appropriate journal entry. The one-sided error usually affects only one account. So to pass a journal entry for rectification of such error, we **shall** now take Suspense Account as the **other account** involved. For example, Rs. 580 received from **Shyam** were posted to his **account** as Rs. 850. It means **Shyam's** Account is to be debited with Rs. 270. You can now pass the following **journal** entry to rectify this error.

		Rs.	Rs.
Shyam	Dr.	270	
To Suspense Account			270
(Being rectification entry)			

Thus **all** errors, whether they are two-sided or one-sided will **now** be rectified by means of journal **entries**.

Let us assume that a businessman could not tally his **Trial** Balance. The **difference** of Re. 1 between the **totals** of the two **columns** was put against the Suspense Account on its debit side and the **Trial** Balance was made to **tally** temporarily. The Suspense Account was carried **forward** to the next accounting year. The **following** errors were then located:

- 1 An **amount** of Rs. 99 was omitted to be posted to the credit of a customer's account from the Cash Book.
- 2 The Sales **Book** was overcast by **Rs.** 100.

The first error involved the omission of **posting** to the credit of customers **account**. So, to rectify **this error** you will **have** to credit customer's account with Rs. 99. As the **Suspense Account** is in existence, the corresponding **debit would be given** to the Suspense **Account**. Thus, the journal entry will be:

		Rs.	Rs.
Suspense A/c	Dr.	99	
To Customer's A/c			99
(Being the rectification of omission in posting)			

The **second** error refers to Sales **Book** being **overcast** by Rs. 100. It means that the Sales **Account** has been credited with Rs. 100 **in excess**. To **rectify this** error, the Sales **Account** will have to be **debited** with Rs. 100. The **corresponding** credit would be given to **Suspense Account**. The rectifying entry will be:

		Rs.	Rs.
Sales A/c	Dr.	100	
To Suspense A/c			100
(Being the rectification of Overcasting in Sales Book)			

The **Suspense Account**, after **posting** the **two** rectification entries, would appear as follows:

Suspense Account			
Dr.		Cr.	
To Balance b/d (dif. in T.B.) To Customer's A/c	Rs. 1 99	By Sales A/c	Rs. 100
	100		100

With the posting of the two rectification entries the Suspense Account is closed. Note that the opening balance in Suspense Account simply shows the net effect of these errors. Sometimes, the balance of **Suspense** Account is **not given**. In that **case it can be** worked out after completing the posting of the **rectification** entries.

Suppose in the above example the amount with which the Suspense Account was opened was not given. Leave the first line blank on both the debit and credit sides of the Suspense Account and post the rectification entries. The difference between the totals of the two sides will be considered as the balance with which the Suspense Account was opened. This is based on the assumption that there are no more errors remaining undetected.

Look at illustrations 3 and 4 and study how **errors** are rectified when Suspense Account is in existence.

Illustration 3

The Trial Balance of Siva did not tally. The credit side exceeded by **Rs. 1,455**. This amount was entered in the debit **column** against Suspense Account and the Trial Balance was made to tally.

Later, the following errors were discovered.

- 1 Goods worth **Rs. 1,250** were sold to Mahesh on credit. This was entered in the Sales **Book** but was not posted.
- 2 **Goods worth Rs. 313** were returned by **Ahmed**. The amount was credited to **his** account but was not recorded in the Returns Inwards **Book**.
- 3 **Manoj** paid Rs. 670 but his account was wrongly credited with **Rs. 607**.
- 4 An amount of Rs. 375 owed by **Dinesh** was omitted from the schedule of sundry debtors.
- 5 The Sales **Book was undercast** by Rs. 420.

Rectify the errors and show the Suspense Account

Solution:

Journal			
		Rs.	Rs.
1	Mahesh To Suspense A/c (Being sales to Mahesh not posted)Dr.	1,250	1,250
2	Returns Inward A/c To Suspense A/c (Being goods returned not recorded in Returns Inwards Book though credited to personal account)Dr.	313	313
3	Suspense A/c To Manoj (Being Cash paid by Manoj underposted)Dr.	63	63
4	Sundry Debtors A/c To Suspense A/c (Being Dinesh's debit omitted from the list of sundry debtors)Dr.	375	375

5	Suspense A/c To Sales A/c (Being rectification of overcasting in Sales Book)	Dr.	420
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Errors and their Rectification

Suspense Account			
Dr.		Cr.	
To Difference in Trial Balance	Rs. 1,455	By Mahesh	Rs. 1,250
To Manoj	63	By Returns Inwards A/c	313
To Sales A/c	420	By Sundry Debtors A/c	375
	1,938		1,938

Illustration 4

Rectify the following errors assuming that a Suspense Account was opened.

- 1 A purchase made from Anthony & Co. for Rs. 8,000 was not entered in the Purchases Book.
- 2 An amount of Rs. 500 received from Mr. Roy was credited to Ray's A/c.
- 3 A sale of Rs. 600 to Gopal was debited to his account as Rs. 6,000.
- 4 Salaries paid amounting to Rs. 1,000 was wrongly debited to Wages Account.
- 5 Rs. 450 received on account of interest stands wrongly credited to Commission Account.
- 6 The total of Returns Outwards Book amounting to Rs. 560 was not posted in the ledger.
- 7 A credit sale of Rs. 250 to Rakesh was wrongly credited to his account.
- 8 A credit sale of Rs. 520 to Madhu debited to him as Rs. 250.
- 9 A credit purchases from Kailash of Rs. 400 was debited to him,
- 10 In Cash Book the total of discount allowed column of Rs. 304 has been carried forward as Rs. 403.

Solution:

Journal			
1	Purchases A/c To Anthony & Co.'s A/c (Being the omission of credit purchases, now rectified)	Dr.	Rs. 8,000 8,000
2	Ray To Roy (Being credit given to Ray's A/c instead of Roy's A/c now rectified)	Dr.	500 500
3	Suspense A/c To Gopal (Being excess debit given to Gopal's A/c, now rectified)	Dr.	5,400 5,400
4	Salaries A/c To Wages A/c (Being debit to Wages A/c instead of Salaries A/c now rectified)	Dr.	1,000 1,000
5	Commission A/c To Interest A/c (Being credit given to Commission A/c instead of interest A/c now rectified)	Dr.	450 450
	Suspense A/c To Returns Outwards A/c (Being the omission of posting total of Returns Outwards Book, now rectified)	Dr.	560 560

Final Accounts

		Rs.	Rs.
7	Rakesh To Suspense A/c (Being wrong credit given to Rakesh, now rectified)	Dr. 500	500
8	Madhu To Suspense A/c (Being short amount debited to Madhu's A/c, now rectified)	Dr. 270	270
9	Suspence A/c To Kailash (Being debit given to Kailash instead of credit. now rectified)	Dr. 800	800
10	Suspense A/c To Discount Allowed A/c (Being excess amount carried forward in Cash Book, now rectified)	Dr. 99	99

Suspense Account

Dr.		Cr.	
	Rs.		Rs.
To Gopal	5,400	By Balance b/d	6,089
To Returns Outwards A/c	560	(balancing figure)	
To Kailash	800	By Rakesh	500
To Discount Allowed A/c	99	By Madhu	270
	<u>6,859</u>		<u>6,859</u>

9.6 EFFECT OF RECTIFYING ENTRIES ON PROFITS

You have seen that the creation of **Suspense** Account helps in **tallying** the Trial Balance and avoiding delay in the **preparation** of final **accounts**. The errors **still** remain to be detected and rectified so, **the Profit** and Loss Account prepared from such Trial Balance is subject to the **undetected** errors. The profit thus arrived at may be more or **less** than the actual profits. **Similarly**, when the errors are detected and rectified during the next year, the rectifying entries will have their effect on the profit of the next year.

The profit is affected only if the errors involve accounts which usually appear in the Trading and Profit and Loss **Account** (nominal **accounts**) and not **those** which appear in the Balance Sheet (real and personal accounts).

Let us understand it with the help of an example. Suppose Rs. 24,000 paid for salaries during 1986 was posted to the Salaries Account as Rs. **20,400**. This error has resulted in short debit of **Rs. 3,600** to Salaries Account and so the salaries charged to Profit and Loss Account are **short** by Rs. 3,600. This would overstate the profits of 1986. When this **error will be detected** in 1987 and the rectifying entry passed, Rs. **3,600** will be added to salaries of 1987 **and** so the profit of 1987 will be decreased by Rs. 3,600. Thus, the **errors as well as** the rectifying entries affect the profit. Of course, the effect of **rectifying entries** will be **almost** the reverse of the effect of errors.

Look at **illustration 5**. It shows rectifying entries and their effect on profits.

Illustration 5

A **businessman** finds that he could tally his Trial Balance of 1986 only by opening a Suspense Account. During 1987, he **discovered the following** errors.'

- 1 The Discount Allowed column of the Cash **Book** was overcast by Rs. 25.
- 2 Sale of old machinery amounting to Rs. 550 had been credited to Sales Nc .
- 3 A sale of Rs. 780 to Ahmed had been debited to his account as Rs. 870.
- 4 The total of Bills Payable Book Amounting to Rs. 4,000 for the month of June was not posted into the ledger.

Rectify the above errors and prepare **the** Suspense Nc. Also explain the effect of rectifying the errors on the profits of 1987.

Solution:

Journal			
		Rs.	Rs.
1.	Suspense A/c To Discount Allowed A/c (Being the rectifying entry for wrong casting of discount allowed column)	Dr. 25	25
2.	Sales A/c To Machinery A/c (Being the rectifying for sale of machinery wrongly credited to Sales Account)	Dr. 550	550
3.	Suspense A/c To Ahmed (Being rectifying entry for excess amount debited)	Dr. 90	90
4.	Suspense A/c To Bills Payable A/c (Being the rectifying entry for omission of posting the total of B/P Book)	Dr. 4000	4000

Dr.			Cr.
	Rs.		Rs.
To Discount Allowed A/c	25	By Balance bld	4,115
To Ahmed	90	(balancing figure)	
To Bills Payable A/c	4,000		
	4,115		4,115

Effect on Net Profit of 1987

Rectifying Entry	Increase	Decrease
	Rs.	Rs.
1 Credit to Discount Allowed A/c	25	
2 Debit to Sales A/c	—	550
3 No nominal account is involved	—	—
4 No nominal account is involved	—	—
	25	550
Net decrease in Profits		525

Profit and Loss Adjustment Account: In the above illustration you observed that errors were committed during 1986 and the rectifying entries were passed in the books of 1987. This unnecessarily affected the profits of 1987. In order that the profits of the year in which rectifying entries are passed is not affected, a new account called Profit and Loss Adjustment Account is opened. Then, all amounts which are to be debited or credited to nominal account in the rectifying entries may be debited or credited to the Profit and Loss Adjustment Account. The balance of the Profit and Loss Adjustment Account is directly adjusted in the capital. Thus, the profit of the year in which the rectifying entries are made remains unaffected. The rectifying entries 1 and 2 of Illustration 5 which involve debit and credit to nominal account can now be shown as follows:

Journal

1	Suspense A/C To Profit and Loss Adjustment A/c (Being the rectification of overcasting the discount allowed column)	Dr.	Rs. 25	Rs. 25
2	Profit & Loss Adjustment A/c To Machinery A/c (Being the rectification for wrong credit given to Sales Account)	Dr.	550	550

The Profit and Loss Adjustment Account will be as follows:

Dr.		Cr.	
To Machinery A/c	Rs. 550	By Suspense A/c By Capital A/c (Transfer)	Rs. 25 525
	550		550

9.7 LET US SUM UP

When the Trial **Balance** does not tally, it **means** there are errors in books of **account**. These may be the errors of principle, errors **of omission**, errors of **commission** or compensating errors. Some of these errors affect the agreement **of Trial Balance** **while** some do not. **The** errors which do not **affect** the Trial Balance are **difficult to locate** **but those** which affect it are easily **located** by **following** a series of steps. **The** errors thus **located** **must** be rectified **before** preparing the final accounts.

One-sided **errors** which affect only **one account** **are** rectified by means **of** a **suitable** note on **the** relevant side in the concerned **account**. Two-sided **errors** involving **two or more accounts** are rectified by **means** of journal entries. If the **Trial** Balance does not tally even after the detected errors have been rectified, it **means** that there are still **some** errors which **have** not **been detected**. In **such a** situation, **the** difference in **Trial** Balance is put **against** a Suspense Account to avoid delay **in preparing** the final accounts. Later, **when** these errors **are discovered**, they can be rectified through **journal** entries and the Suspense **Account** may be closed.

When errors are rectified during the next accounting **year**, the **rectification** entries involving nominal **accounts** affect the profits of the next year. To **avoid** such **effect**, a **Profit and Loss** Adjustment Account **can** be opened and its balance **directly** adjusted in **capital**.

9.8 KEY WORDS

- Audit:** **Checking** the books of account by auditors for **detection** and prevention of **errors** and frauds.
- Compensating Errors:** A group of errors **wherein** the effect of **one** error is counter-balanced (**compensated**) by the effect of the other **errors**.
- Errors of Commission:** A clerical **error** committed while **recording or posting the** transactions or while totalling, **balancing**, etc.
- Error of Complete Omission:** An **error** committed by **completely** omitting to record a transaction in books.
- Error of Partial Omission:** An error committed in omitting to post one aspect of an entry in the ledger.
- Error of Principle:** An **error** committed by ignoring or **misapplying** some principles of accounting while recording a **transaction** in books.
- One-sided Error:** An error which affects **the** debit **or** credit side of **one** account only.
- Profit and Loss Adjustment Account:** An account opened for avoiding the effect of **rectifying** entries in respect of the previous year's errors on the profits of the current year.

Rectifying Entries: Entries made in books of account for correction of errors.

Suspense Account: An account opened to tally the Trial Balance temporarily. It represents the net effect of undetected one-sided errors.

Two-sided errors: An error which involves two or more accounts and effect both the debit and credit aspects.

8.9 SOME USEFUL BOOKS

Maheshwari, S.N. 1986. *Introduction to Accounting*, Vikas Publishing House: New Delhi. (Chapter 11)

Patil, V.A. and J.S. Korlahalli, 1986. *Principles and Practice of Accounting*, R. Chand & Co. New Delhi. (Chapter 16)

William Pickles. 1982. *Accountancy*, E.L.B.S. and Pitman: London. (Chapter 14)

Gupta, R.L. and M. Radhaswamy. 1986. *Advanced Accountancy*, Sultan Chand & Sons: New Delhi. (Chapter 9)

9.10 ANSWERS TO CHECK YOUR PROGRESS

A 3 i)	Error of Complete Omission	No effect on Trial Balance
ii)	Error of Commission	No effect on Trial Balance
iii)	Error of Commission	Affects the Trial Balance
iv)	Error of Commission	Affects the Trial Balance
v)	Error of Commission	No effect on Trial Balance
vi)	Error of Commission	Affects the Trial Balance
vii)	Error of Commission	No effect on Trial Balance
viii)	Error of Principle	No effect on Trial Balance

- B 1** a) i) **Chetan's** Account ii) **Purchases** Account iii) Sales Account
 b) i) Typewriter Account ii) Sales Account
 c) i) Drawings Account ii) General Expenses **Account**
 d) i) Jatin's Account ii) Sales Account
 e) i) **Furniture** Account ii) Purchases Account

- 2** a) i) Chetan's Account debited **with** Rs. 15,000 instead of being credited
 ii) **Purchases Account** not debited with Rs. **15,000**
 iii) Sales Account credited in excess by Rs. 15,000
 b) i) Typewriter Account not credited with Rs. 800.
 ii) Sales **Account** credited in **excess** by Rs. 800.
 c) i) Drawings Account not debited
 ii) **General** Expenses Account debited in excess
 d) i) Jatin's Account not debited
 ii) Sales Account not credited
 e) i) Furniture Account not debited
 ii) Purchases Account debited in excess

- C 1** i) Debit Sales Returns Account and Credit Suspense Account
 ii) Debit Suspense Account and Credit **Purchase** Account.
 iii) Debit Suspense Account and **Credit Kant's** Account (With Rs. 1,500).
 iv) Debit Nagesh's Account and Credit Suspense Account.
 v) Debit Interest Account and Credit Rent Account.

- 2** Difference in Trial Balance Rs. **1,506** placed to the credit of Suspense Account.

9.11 TERMINAL QUESTIONS/EXERCISES

Questions

- 1 What are its various types of errors which are usually committed in the process of accounting? Explain them with examples.
- 2 Is **Trial** Balance a conclusive proof of the accuracy of the books of account? If not, discuss the errors which are **not** disclosed by the Trial Balance.
- 3 Describe briefly the procedure for locating the errors.
- 4 What is Suspense Account? State its advantages.
- 5 Does rectification of errors in the subsequent accounting periods always affect the trading result of those years? Give examples of errors which affect it and which do **not**.

Exercises

- 1 Rectify **the** following errors.
 - a) Rs. 690, the amount of rent paid to the landlord, was debited to his personal account.
 - b) Goods taken away by the proprietor for personal use costing Rs.600, **was** debited to the Purchases Account.
 - c) **Rs.** 1,080 paid as wages for construction of a room was debited to the Wages Account.
 - d) Total of **purchases** Book of one page was carried forward to the next page as Rs. 876 instead of Rs. 786.
 - e) Discount **allowed** amounting to Rs. 25 had been credited to Discount Received Account.
 - f) Total of Sales Book of one page was carried forward to the next pages as Rs. 872 **instead** of 782.
- 2 **Rectify** the following errors.
 - a) Rs. **700** recovered on account of bad debts written off earlier, credited to the customer's personal account.
 - b) **Goods** returned by Murari amounting to Rs. 250 has been entered in the Returns Outwards Book.
 - c) An amount of Rs. 800 withdrawn by the proprietor for his personal use has been debited to General Expenses **Account**.
 - d) Discount allowed to **Kurien** amounting **to** Rs. **47** has not been entered in the **discount** column of the Cash Book, but it has been posted to the customer's personal account.
 - e) A cash sale to **Ashok** for Rs. **690** was recorded in the Cash Book and also in the **Salés** Book. Postings were **made** from both the books.
 - f) **The Bank** Column on the credit side of the Cash Book was overcast by **Rs.** 50.
- 3 On **taking** out a **Trial** Balance a book-keeper finds an excess credit of Rs. 2,460. Being desirous of closing the books, he places the difference in a Suspense Account, which is carried forward. In the next period, he discovers the following errors. Pass **the rectifying** entries and **prepare** the **Suspense Account**.
 - a) The total of Returns **Inwards** Book has been found to be **Rs.** 400 short.
 - b) **A sum** of Rs. 4,800 **written** off as depreciation on machinery, has not been posted to the Depreciation Account,
 - c) A discount of Rs. 1,000 allowed to a customer has been posted to his account as Rs. **100**.
 - d) **The** Sales Book was **undercast** by Rs. 4,000.
 - e) Purchase of Ws 480 was posted as Rs. **840** in the supplier's account.(**Answer:** Suspense **Account** still show a debit balance of Rs. 1,800.)
- 4 A book-keeper failed to balance **his** Trial **Balance**. He places the difference to a newly opened Suspense Account which is carried forward. The following **errors** were subsequently discovered. Give journal entries to rectify **these** errors and show the Suspense Account.
 - a) The total of Purchases Day Book had been undercast by Rs. 200.
 - b) Purchase of a typewriter on credit from **Harnath** for Rs. 9,600 was entered in the Purchases Book.

- c) Goods returned by Hari amounting to Rs. 2,000 has been entered in the **Returns Outwards Book**, however, the posting was done correctly to **Hari's Account**.
 - d) A cash sale of Rs. 2,500 to **Somnath**, correctly entered in the Cash Book, was posted to the credit of his personal account.
 - e) A cheque received from **Mahinder** for Rs. 8,160 had been debited in the Cash Book, but the double entry had not been completed.
- (Answer: Suspense Account was started with a credit balance of Rs. 3,960)

5 The **Trial Balance** prepared by **Dhanraj** did not tally and the difference was transferred to a Suspense Account. Subsequently, the following errors were found. Rectify the errors and show the Suspense Account. Also explain the effect of rectifying entries on the profits.

- a) A sale of Rs. 1,600 to **Kamalnath** was posted to **Karunanath**.
- b) Insurance amounting to Rs. 250 paid was posted twice.
- c) A sale of Rs. 1,500 for old machinery was passed through the **Sales Book**.
- d) A Purchase worth Rs. 600 from **Kamesh** was not passed through the books.
- e) The debit balance on **Commission Account** amounting to Rs. 80 was omitted from the Trial Balance.
- f) The Purchases Returns Book was undercast by Rs. 700.

(Answer: Suspense Account was started with a credit balance of Rs. 870. Profit will decrease by Rs. 1,230).

6 An accountant could not tally the Trial Balance. He placed the difference of Rs. 2,380 to the credit of **Suspense** Account and prepared the final accounts. The following errors were discovered in the next year.

- i) The Sales Book was undercast by Rs. 500.
- ii) Entertainment expenses of Rs. 950, though entered in the Cash Book, were omitted to be posted in the ledger.
- iii) Commission of Rs. 250 paid was posted twice to **Commission** Account.
- iv) Discount column of the receipt side of the **Cash Book** was wrongly added as Rs. 1,400 instead of Rs. 1,200.
- v) A sale of Rs. 1,390 to **Kamesh**, though correctly entered in the Sales Book, was wrongly posted to his personal account as Rs. 1,930.
- vi) A purchase from **Nahar** worth Rs. 920, though correctly entered in the Purchases Book, was wrongly debited to his personal account.

Pass the necessary rectifying entries, prepare Suspense Account and state the effect of rectifying the entries on the profits.

(Answer: Suspense Account was closed. Effect on Profit: nil).

Note: These questions will help you to understand the unit better. Try to write answers for them. But do not submit your answers to the University for assessment. These are for your practice only.

ECO-02 ACCOUNTANCY-I

Course Components

BLOCK	UNIT NO.	PRINT MATERIAL
I		Accounting Fundamentals
	1	Basic Concepts of Accounting
	2	The Accounting Process
	3	Cash Book and Bank Reconciliation
	4	Other Subsidiary Books
	5	Bills of Exchange
2		Final Accounts
	6	Concepts Relating to Final Accounts
	7	Final Accounts-I
	8	Final Accounts-II
	9	Errors and their Rectification
3		Consignments and Joint Ventures
	10	Consignment Accounts-I
	11	Consignment Accounts-II
	12	Consignment Accounts-III
	13	Joint Venture Accounts
4		Accounts from Incomplete Records
	14	Self Balancing System
	15	Accounting from Incomplete Records-I
	16	Accounting from Incomplete Records-II
	17	Accounting from Incomplete Records-III
5		Accounts of Non-trading Concerns, Depreciation, Provisions and Reserves
	18	Accounts of Non-trading Concerns-I
	19	Accounts of Non-trading Concerns-II
	20	Depreciation-I
	21	Depreciation-II
	22	Provisions and Reserves