CHAPTER 1

INTRODUCTION TO ACCOUNTING

Contents :

1.0 . Aims and Objectives
1.1. Introduction
1.2. Meaning of Accounting
1.3. Accounting and Book Keeping
1.4. Need for Accounting
1.5. Definition
1.6. Origin of Accounting
1.7. Development in Accounting
1.8. Steps in Accounting
1.9. Objectives of Accounting
1.10. Functions of Accounting
1.11. Classifications of Accounting
1.12. Methods of Accounting
1.13. Types of Accounting
1.14. Groups Interested in Accounting
1.15. Let Us Sum Up
1.16. Lesson End Activities
1.17. Model Answers to check your progress
1.18. References

1.0 Aims and Objectives : In the present chapter we are going to discuss in brief about

- Meaning and definition of accounting
- Meaning and nature of book keeping
- Important of accounting in the modern world
- Various objectives and functions of accounting
- Classifications, methods and types of accounting
- Various groups interested in the accounting statement.

After reading this chapter you should be able to acquire basic working knowledge about the above mentioned topics.

LESSON 1

INTRODUCTION TO ACCOUNTING

1.1 Introduction :

The word "money" is so important to survive in the human society just like as blood in the human structure. It is well said that "Nothing is impossible when money is available and nothing is possible when the money is not available". The source of money is created by way of undertaking a job, engaging in agriculture, business or profession etc. The availability of money is depend upon the manner in which money is expended. This means if a person or business concern is careless in spending money; the day may come when he or it does not have a single rupee.

In other words, the availability of money is not merely depend upon the earning of income but very much depend upon the manner in which the earned income is expended. Thus the proper management of income and expenditures is quite important to survive as well as to grow. It requires preparing and maintaining proper records and books in the systematic manner. For this purpose, a technique or tool named as "accounting" has been in the use since the ancient period.

The paper titled as "Principles of Accountancy" is aimed at educating the students to maintain, prepare and analysis various records in different situations by using universally accepted methods and rules. The present chapter deals with meaning, need, objectives and scope of accounting.

1.2. Meaning of Accounting:

The modern system of accounting is based what is known as the Double Entry principle. Accounting is a science because it has some definite objects to be fulfilled and is an art as it prescribes the process through which the object can be achieved. Non- financial transactions cannot be recorded in accounting, i.e., only transactions of financial nature is the subject –matter of accounting. To be more clear, only those transactions which are expressed in terms of money are recorded. Accounting is an art of recording transactions according to size, nature and type of business transactions – cash transactions, credit transactions, frequent transactions etc. When the recording in journal or subsidiary books is done, they are to be classified by grouping the transactions or entries of one nature at place. This is done by opening accounts in a book called ledger. Then such ledgers are summarized in order to give useful information to the management or interested parties. This is done by preparing trading and profit and loss account and balance sheet of whole accounting record. Finally, it is an art of interpreting the result of the financial transactions and communicating the result thereof. The aspect of interpretation falls under management accounting.

1.3. Accounting and Book keeping:

Book keeping may be defined as the art and science of correctly and systematically recording in the books of account the business transactions of an individual or a concern in a way to show clearly the monetary effect of each such transactions. The work of book-keeping is usually entrusted to junior employees, who maintain various books of accounts, journal, subsidiary books, ledgers etc, can be called as book

–keepers. The books of original record, by themselves, do not give an idea of the company's financial position. When one has to make a judgment regarding the financial position of the firm, the information contained in these books has to be analysed and interpreted.

1.4. Need for Accounting:

It is common experience of all of us that money must be spent carefully. A firm receives money from certain sources like sale of goods, interest on bank deposits. It has to spend money on a number of items like salary, rent, electricity, water, advertisement. The firm should manage its affairs in such a way as will enable it to receive more than it spends. Otherwise, it will have to meet expenses from the original amount invested by the owner for starting the business.

1.5. Definition:

Accounting is defined as "the art of recording, classifying and summarising in terms of money transactions and events of a financial character and interpreting the results thereof."

1.6. Origin of Accounting:

Accounting originated to meet the requirements of exchange of goods and commodities. The need for accounting grew in order to serve the transactions of the business world. The origin of accounting cannot be exactly located. The value of money or the use of currency, that now we attach to the goods to-day, was unknown to the people of ancient times when barter system existed. Later, innovation of money facilitated to ease exchange of commodities. The credit transactions necessitated to maintain accounts, and accounting is as old as business itself. Accounting was practiced in India, from ancient time, as is clear from the book Arthahastra written by Kautilya, the Minister of King Chandra Gupta. In 1494, the system of book-keeping was first conceived on scientific line in Venice by Luca Paciolia Franciscan monk.

1.7. Development in Accounting:

Accounting is as old as money itself. In India, chanakya in his, "Arthashastra" has emphasised the existence and need of proper Accounting and Auditing. The modern system of accounting owes its origin to Pacioli who lives in Italy in the 15 th century. Accounting at its initial stage, tried to meet the need of historical and stewardship functions. The conventional accounting principles and practices prove to be insufficient. The advent of Industrial Revolution has resulted in large scale production, cut- throat competition and widening market. Today there is greater need for coordination and control. Accounting day cannot be the same as it used to be about half a century ago. It has becomes a very dynamic subject. At present some of the important specialized branches of accounting which are developed are: Cost Accounting, Management Accounting, Responsibility Accounting, Social Accounting or Macro Accounting, Government Accounting, Inflation Accounting, Mechanized Accounting, Human Resources Accounting etc. Needless to mention that some of the said techniques devised are Standard Costing, Marginal Costing, Budgetary Control, Statistical and Quantitative Techniques, Ratios Accounting, Fund and Cash Flow Analysis etc.

(1.8) Steps in Accounting :

Following are the various steps involved in accounting:

i. Recording : Each and every transaction is recorded as and when it occurs in chronological order. Every entry recorded has to be supported by reliable documentary evidence. The method of recording is adjusted according to the size, and nature of business and the type of transactions.

ii. Classification : The classification takes the form of accounts in a separate book called as Ledger. Separate ledger accounts are opened for each expenses , income, property and liability. It useful for the segregation of numerous business transactions into identifiable groups.

iii. Summarising : Summarising takes place in the form of trial balance, trading account, profit & loss account and balance sheet which are discussed in detail in the following chapters.

iv. Interpretation: It is usually done through flow statements. They are useful in evaluating past performance and providing guidance for future plans and activities.

1.9. Objectives of Accounting:

Following are the objectives for which accounting is aimed at:

i. To provides the permanent record.
ii. To provides the most effective way to the management for fixing of objectives of the business.
iii. To provides the most vital information to the management to preparing budgets.
iv. To facilitates the business concern to know the profit or loss for a given period.
v. To facilitates to know the soundness of a business concern by providing balance sheet.
vi. To enables to prepare a list of customers and suppliers to ascertain amount to be received or paid.
vii. To gives opportunities to review the business policies in the light of the past records.
viii. To comply with provisions of Companies Act 1956, it is necessary to maintain accounting records.
ix. To be useful for business loss, provision of licenses, assessment of taxes etc.,

1.10. Functions of Accounting:

Accounting has the following functions:

i. Function of Book-keeping: The primary functions of accounting relates to recording, classification and summary of financial transactions – journalisation, posting and preparation of final statements. The purpose of this function is to report regularly to the interested parties by means of financial statements.

ii. Function of Language: Accounting is the language of business. Various transactions are communicated through accounting. There are many parties. Owners, Creditors, Government, Employees etc., who are interested in knowing the results of the firm and this can be communicated only through accounting. The accounting shows a real and true position of the firm on the business.

iii. Function of legality: Auditing is compulsory in case of registered firms. Auditing is not possible without accounting. Thus accounting becomes compulsory to comply with legal requirements. Accounting is a base and with its help various returns, documents, statements etc., are prepared.

iv. Function of management: Decision making programme is greatly assisted by accounting. The managerial function and decision making programmes, without accounting, may mislead. The day-today operations are compares with some pre- determined standard. The various of actual operations with pre – determined standards and their analysis is possible only with the help of accounting.

1.11. Classification of Accounting:

Accounting can be classified into the following categories :

i. Financial Accounting: The main purpose of this type of accounting is to record business transactions in the books of accounts in such a way that operating results for a particular period and financial condition on a particular date can be known for the information of the various persons.

ii. Cost Accounting : It relates to the collection, classification, ascertainment of cost and its accounting and cost control relating to the various elements of cost, that is, materials, labour and overheads.

iii. Management Accounting: It relates to the use of accounting data collected with the help of financial accounting and cost accounting for the purpose of policy formulation, planning, control and decision-making by the management. The accounting which is prepared exclusively for the use of management is called management accounting.

1.12. Methods of Accounting:

Following are the three methods of accounting:

i. Cash Basis of Accounting: Under this method, all incomes are considered to be earned when they are actually received in cash. Similarly, expenses are deemed to be incurred only when they are actually paid in cash. In other words, importance is attached to cash receipts and payments but non-cash items, such as outstanding, pre-paid expenses, accrued incomes or income received in advance are ignored. This method is adopted in those concerns where only cash transactions take place. Generally this system is followed by individuals like Doctors, Lawyers, Auditors, Engineers, Brokers, and Small Traders etc.

ii. Accrual Basis or Mercantile Basis of Accounting: This method is commonly adopted by business concerns. Incomes are recorded or credited to the period in which they are earned irrespective of the fact whether the same has actually been received or not. Similarly, expenses are charged to the period in which they relate irrespective of the fact that they have actually been paid or not. In other words, all items of incomes and expenditures, both cash items as well as non – cash items such as pre- paid expenses, accrued incomes or income received in advance etc, are taken into account.

iii. Hybrid or Mixed Basis of Accounting: Under this method, both cash basis and accrual basis are followed. Incomes are recorded on cash basis whereas expenses are taken on accrual basis. The net income is ascertained by matching expenses on accrual basis with income on cash basis. This is the most conservative basis of ascertaining income because all possible expenses relating to the period whether actually paid or not are considered whereas income only received in cash in taken into consideration. This system is followed by professional like Doctors, Lawyers, and Chartered Accountants etc.,

1.13. Types of Accounting:

There are two systems of accounting namely Single Entry System and Double Entry System.

1.13.1. Single Entry System: The single entry system is not a really a system because in some cases record may be one – sided; and in some other cases no record is maintained at all. It is more appropriate to call it an incomplete system of recording transactions. Double effect of every transaction is ignored and only the accounts relating to suppliers and customers an cash account are found. Thus, the system is incomplete, inaccurate and unscientific system of recording business transactions.

1.13.2. Double Entry System: The modern system of accounting is based on what is known
as double entry principle. It refers to that system of book keeping where each transaction is recorded in both of its aspects. viz.i. receiving of the benefit of the transaction and ii. giving away of the benefit of the transaction. For a complete record of transactions, it should be presented in both the accounts. Business transactions affect two aspects of the accounts in the opposite direction. If are account receives a benefit there must be another account to give the benefit. It is like the two sides of a coin. Thus, every transaction involves two accounts, one which gives the benefit of the transactions and another which receives the same.

1.14. Groups Interested in Accounting:

There are a number of parties who are interested in the accounting information relating to business. Because, accounting is the language employed to communicate financial information to the General public. The following are the groups who use the accounting statements:

i. Owners: The owners provide funds or capital for the organisation. They possess curiosity in knowing whether the business is being conducted on sound lines or not and whether the capital is being employed properly or not. Owners, being businessmen, always keep an eye on the returns from the investments. Comparing the accounts of various years helps in getting good pieces of information. Properly kept accounts are good proof in dispute. They determine the amount of goodwill and facilitate in assessing various taxes.

ii. Management: The management of the business is greatly interested in knowing the position of the firm. The accounts are the basis the management can study the merits and demerits of the business activity. Thus, the management is interested in financial accounting to find whether the business carried on is profitable or not. The financial accounting is the "eyes and ears of management and facilitates in drawing future course of action, further expansion etc.,

iii. Creditors: Creditors are the persons who supply goods on credit, or bankers or lenders of money. It is usual that these groups are interested to know the financial soundness before granting credit. The progress and prosperity of the firm, to which credits are extended, are largely watched by creditors from the point of view of security and further credit. Profit and Loss Account and Balance Sheet are nerves centers to know the soundness of the firm.

iv. Employees: Payment of bonus depends upon the size of profit earned by the firm. The more important point is that the worker expects regular income for the food. The demand for wage rise, bonus, better working conditions etc. depend upon the profitability of the firm and in turn depends upon financial position. For these reasons, this group is interested in accounting.

v. Investors: The prospective investors, who want to invest their money in a firm, of course wish to see the progress and prosperity of the firm, before investing their amount, by going through the financial statements of the firm. This is to safeguard the investments. For this, this group is eager to go through the accounting which enables them to know the safety of investments.

vi. Government: Government keeps a close watch on the firms which yield good amount of profits. The State and Central Governments interested in the financial statements to know the earnings for the purpose of taxation. To compile national accounts the accounting is essential.

vii. Consumers: These groups are interested in getting the goods at reduced price. Therefore, they wish to know the establishment of a proper accounting control, which in turn will reduce to cost of production, in turn less price to be paid by the consumers.

viii. Research Scholars: Accounting information, being a mirror of the financial performance of a business organisation, is of immense value to the research scholar who wants to make a study into the financial operations of a particular firm. To make a study into the financial operations of a particular firm, the research scholar needs detailed accounting information relating to purchase, sales, expenses, cost of materials used, current assets, current liabilities, fixed assets, long – term liabilities and share holders funds which is available in the accounting records maintained by the firm.

1.15. Let Us Sum Up : In this lesson we have discussed

- meaning and objectives of accounting
- described functions, types, classification, methods of accounting
- learnt about various persons interested in the accounting statement

1.16. Lesson End Activities :

1. What is meant by accounting ? Explain objectives and functions of accounting.
2. What are the three methods of accounting ?
3. What are the three types of accounting?
4. Who are the persons interested in the accounting statements.
5. Write short note on : i. Accounting and Book keeping ii. Cash basis and Merchantile basis iii. Single entry system and Double entry system.

1.17. Model Answers to Check your Progress :

Question No. 1. Refer para 1.2. 1.7. 1.8.
Question No. 2. Refer para 1.10.
Question No. 3. Refer para 1.12.
Question No. 4. Refer para (i) 1.2. 1.3. (ii) 1.10.1. 1.10.2. (iii) 1.11.1. 1.11.2.

1.8 References:

Financial Accounting – R.L. Gupta – Sultan chand & Sons
Advanced Accounting – S.N. Mageswari – Vikas Publishers

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LESSON 2

CONCEPTS AND CONVENTIONS OF ACCOUNTING

Contents :

2.0. Aims and Objectives

2.1. Introduction

2.2. Meaning of Accounting Concept

2.3. Meaning of Accounting Convention

2.4. Let Us Sum Up

2.5. Lesson End Activities

2.6. Model Answers to Check your Progress

2.7 References

2.0. Aims and Objectives : In this lesson we are going to learn

- The meaning and various elements of accounting concepts
- Meaning and various elements accounting conventions .

After reading this chapter you should be able to acquire basic working knowledge about the above mentioned topics.

2.1. Introduction:

Accounting is the language of business and information about business is communicated to outsiders through accounting statements. In order to make these statements easily understandable and meaningful, it is necessary that accounting should be based on certain unifrom scientifically laid down norms, which are called accounting principles. The accounting principles are rules of action or a body of doctrine universally adopted while recording the business transactions. Adopting uniform principles in recording the transactions will ensure uniformity, clarity and understanding. If accounting is to serve its purpose more effectively, it should be based on certain unifrom and scientifically laid down principles or postulates, also termed as accounting standards,. The accounting principles can be classified into two categories: 1. Accounting Concepts and 2. Accounting Conventions.

2.2. Meaning of Accounting Concepts :

There are some assumptions on which accounting is based. Accounting is the language of business. Business firms communicate their affairs and financial positions to the outsiders through the medium of accounting, which is the language of business in the form of financial statements,. To make the language convey the same meaning to all interested parties, accountants have agreed on a number of concepts which they try to follow. The meassages so communicated should easily understood by the people for whom it is intended. Accounting concepts can be described as something which signifies a general notion regarding accounting principle. The assumptions, so made, are most natural and are not forced ones. A concept is self-evident proposition i.e., something taken for granted. There is no authoritative list of these concepts.

2.2.1. Business Entity Concept :

Business is treated as separate from the proprietor. This concept is important and implies that a business is separate and distinct from the persons who supplied capital to the firm. All transactions of the business are recorded in the books of the firm. If business affairs and private affairs are mixed, the true picture of the business will not be available. The proprietor is treated as a creditor to the extent of his capital. Capital is thus a liability to the firm and the proprietor is the creditor of the business. The proprietor-sole trader, partners of a partnership firm etc.-may draw amount out of the business and this reduces the liabilty of the firm. Because of this concept, financial position of the business can be easily found out and earning capacity of the firm can be easily ascertained. It is important to note that transactions of the business affairs and private affairs are separated for recording only and in law, no such distinction is recognised except for an incorporated company.

2.2.2. Money Measurment Concept :

Only those transactions, which can be expressed in monetary terms, are recorded in accounting though their quantitative records may also be kept. All business transactions should be expressed only in money. Thus transactions, which cannot be expressed in money, will not be recorded in accounting books. Thus labour-management relations, sales pollicy, labour unrest, effectiveness of competition etc., which are of vital importance to business concept, do not find place in accounting. Another limitation of this concept makes the

assumption that the money value is constant. It is contrary to fact as there are fluctuations in the money value. For instance, a land, purchased for Rs 10,000 in 1980, may cost four or five times, in 2007. This because of fall in money value.

2.2.3.. Going Concern Concept:

This concept relates with the long life of the business. A business is intended to continue for an indefinitely long period. For all practical purposes, a business firm comes under going concern concept, when there is no evidence to the contrary. All firms that continue to operate on a profitable footing are treated as going concerns. Accordingly, continuity of activity is assumed, thus accounting reports are fashioned as a going concern, just as against liquidation. The current disposal value is irrelevant for a continuing business. Thus under this assumption fixed assets are recorded at original cost and are depreciated in a proper manner, In Balance Sheet market price of fixed assets not considered. While preparing final accounts, recored is made for outstanding expenses and pre-paid expenses with the assumption that the business will continue.

2.2.4. Accounting Period Concept:

Accounting is a continuous process in any business undertaking. Every businessman wants to know the result of his investment and efforts at frequent intervals. Accountants choose some shorter period to measure the result. Therefore, one year has been, generally, accepted as the accounting period. It may be 3 months or 2 years also. This period is called accounting period. Financial period chosen, in this regard, should be neither too long nor too short. Closing day of the accounting period is known as accounting date. At this date, accountant prepares income and position statements, shows the business operations, brings the changes of positions since the construction of last statements. The financial reports prepared facilitate to make good decison, corrective measures, expansion etc. One the basis of income and position statement, financial position and earning capacity of one year can be compared with another. Their comparison helps the business for expansion. The outsiders too draw various conclusions. One year accounting period is recognised by law and the taxation is assessed annually. Reports to the outsiders are provided on this accounting period.

2.2.5. Accrual Concept:

According to this concept the revenue is recognised on its realisation and not on its actual receipt. Similary, the costs are recognised when they are incurred and not when payment is made. This assumption makes it necessary to give certain adjustments in the preparation of income statement regarding revenues and costs. But under cash accounting system, the revenues and costs are recognised only when they are actually received or paid. Hence, the combination of both cash and accural system is preferable to get rid of the limitaions of each system.

2.2.6. Cost Concept:

Under this concept, fixed assets are recorded in the account books at the price at which they are acquired. This price paid to acquire the assets is termed as cost and this cost is the basis for all the subsequent accounting for the asset. When an asset is acquired for Rs 5,000, it is recorded in the account books at Rs 5,000 even though the market value may be different. But the asset is shown in balance sheet year after year, at cost price minus depreciation. This value is called book value. It the business pays nothing for an item it acquired, then this will not appear in the accounting records as an asset. Thus, all such events

are ignored which affect the business but have no cost, for example, a facourable location, a good reputation with its customers, market standing etc.

2.2.7. Reliasation Concept :

This concept revolves around the determination of the point of time when revcenues are earned. A business firm invests money to purchase or manufacture goods for sale. To earn profit, sales have to be made. There can be no profit without realisation of sale proceeds. According to realisation concept, which is also known as the “revenue recognition concept”, revenue is considered as being earned on the date on which is realised i.e., the date on which goods and services are transferred to customers either for cash or for credit. Credit transactions create debtors and the promise of debtors to make payment is sufficient for the purpose of realising revenue. The realisation concept is important in ascertaining the exact profit earned during a period in business concern. This concept is very important as it prevents firms from inflating profits by recording sales and incomes that are likely to accrue.

2.2.8. Dual Aspect Concept :

This concept signifies that every business transaction involves a two-fold aspect a. the yielding of beneift and b. the giving of the beneift. For an exchange of value, two parties are required-a giver and a receiver. Thus, a firm sells goods worth Rs 100, the two simultaneous implications on the seller are i. forgoing goods worth Rs 100 and ii. receipt of cash Rs 100. And those on the purchaser would be i. receipt of goods worth Rs 100 ii. forgoing of cash Rs 100. Every transaction affects two accounts and entials two-fold simultaneous effect on each transaction affects receiving account and giving account equally. Technically speaking, "for every debit, there is a credit". Therefore, we can say that every debit must have a corresponding credit and vice versa. This is the only system of modern account keeping. The underlying principle of Double Entry is very simple but wonderfully effective. "Double Entry book-keeping is a system of accounting by which receiving and giving aspects of each transaction are recorded at a time". As such transaction affects giving account and receiving account equally, the assets of a business entity will always be equal to its liabilities i.e.,

Total Assets	=	Total Liabilities
Total Assets	=	Capital + Outsiders' liabilities
Capital	=	Total Assets - Outsiders'liabilities.

2.2.9. Matching Concept :

According to this concept, it is necessary to match the expenses incurred during the accounting period with the revenues recognised during the same period. Since profit is an excess of revenue over expenses, it becomes necessary to bring together all revenues and expenses pertaining to a particular period. In other words, expenses incurred in an acounting year should be matched with the revenues recognised in that year. Again, only such expenses as incurred in generating revenues during the period should be deducted from those revenues for deriving the amount of income or profit during the period. The object of accounting is that accounting record the made in such a manner that cost may be compared with revenue. If the accounting method does not facilitae the comparison, then accounting method is considered unsatisfactory. Neither receipt of cash for revenue nor payment of cash for expenses is necessary. What is necessary is that they must accrue in the current year so that the incurred expenses are mathched against the realised revenue. American Institute of Certified Public

Accountants' Committee on Accounting Procedue states that "it is plainly desirable to provide, by charging in the current income statement, properly classified, for the foreseeable costs and losses applicable against current revenues, to the extent they can be measured and allocated to fiscal preiod with reasonable approxiamation". All costs incurred during the period are taken. Similarly, expenses paid in advance are exculded from the total costs incurred to arrive at the expired costs. By application of this concept, proprietor can easily know about the profit or loss and he can make effort to increase earning capacity.

2.2.10. Objectivity Concept:

This concept implies that all accounting transactions should be evidenced and supported by business documents i.e., invoices, vochers etc. The evidence substantiating the business transactions should be objective free from the is of the accountant or others. These supporting documents form the basis for record of entries and of audit. Accounting record is based on documentary evidence is readily and objectively verifiable and therefore universally acceptable.

2.3. Meaning of Accounting Convention:

An accounting convention is a common practice which is universally followed in recording and presenting accounting informations of business. They are like customs that are followed in a society. As a society develops its own customs for its day to day work, conventions are devloped by business to facilitate its recording of business transactions in the books of accounts.Conventions help in comparison of accounting data of different business units or of the same unit for different periods. The object is to make accounting data more useful. Following are the accounting conventions in the use:

2.3.1. Convention of Disclosure:

The convention requries that accounting statements should be honesty prepared and all significant information should be disclosed therein. That is, while making accountancy records, care should be taken to disclose all material information. Here the emphasis is only on material information and not on immaterial information. This conention assumes greater importance in respect of corporate organisations, where the management is divorced from ownership. That is why forms of Balance sheet and Profit and Loss accounts are prescribed in Schedule VI of the Companies Act, 1956; so that significant information may not be left out to be disclosed. The purpose of this convention is to communicate all material and relevant facts of the financial position and the results of operations, which have material interests to properietor, creditors and investors. Sometimes, there may be time gap between the prearation of Balance Sheet and its publication and if there are material events- bad debts, destruction of plant or machinery etc., which occured in the time gap, may also be known to users- proprietors, creditors etc. In short, full disclosure of all relevent facts in accounts is a necessity in order to make accounting record useful. Therefore, full disclosure is a very healthy convention, and is important.

2.3.2. Convention of Conservatism :

"Anticipate no profit and provide for all possible lossess" is the essence of this convention. Future is uncertain. Fluctuations and uncertainties are not uncommon. Conversatism refers to the policy of choosing the procedure the leads to under-statement as against overstatement of resources and income. The consequences of an error of

understatement are likely to be less serious that of an error of overstatement. For example, closing stock is valued at cost or market price whichever is lower. This is a convention of caution or playing safe and is adhered to while preparing financial statements. Showing a position better than what it is, is not permitted. More ever, it is not proper to show a position substantialy worse than what it is. Following are the examples:

(a) The value of an asset should not be overestimated.

(b) The value of a liability should not be underestimated.

(c) The profit should not be overestimated.

(d) The loss should not be underestimated.

2.3.3. Convention of Materiality :

American Accounting Association defines the term materiality as "an item should be regarded as material if there is reason to believe that knowledge of it would influence the decision of informed investor." It refers to the relative importance of an item or event.

Materiality of an item depends on its amount and its nature. Theoretically, all items, large or small, should be treated alike. Materiality convention implies that the economic significance of an item will to some extent affect its accounting treatment. Materiality in its essence is of relative significance. In the sense that some of the unimportant items are either left out or included with other items. For instance, acquisition of items like fountain pen, stapler, pin cushion, punching machine ect, can be treated as part of assets, when considering their durability and span of life. But, it is not necesary to maintain seperate ledgers. Such low cost items can be treated as expense for the period. Therefore, unimportant items are either left out or merged with other items. The reason for this different treatment lies in the magnitude of their amount. The dividing line between material and immaterial varies accroding to the company, the circumstances of the transaction and economic significance. It should also noted that an item considered to be material in a year may not be material in the subsequent years. Similarly, most of the companies publish their financial statements in whole ruees-round figures, by ignoring paise. Omission of paise is immaterial i.e., in significant when figures appear in lakhs. In short, all material information should be disclosed that it is necessary to make the financial statements clear and understandable.

2.3.4. Convention of Consistency :

Rules and practices of accouting should be continuously observed and applied. In order to enable the management to draw conclusions about the operation of a company over a number of years, it is essential that the practices and methods of accounting remain unchanged from one period to another. Comparisons are possible only if a consistent policy of accounting is followed. Comparison of accounting period with that in the past is possible only when the convention of consistency is adhered to. According to Anthony, " The consistency requires that once a company had decided on one method, it will treat all subsequent events of the same character in the same fashion unless it has a sound reason to do otherwise." This convention plays its role particularly when alternative accounting practice is equally acceptable. More ever, consistency serves to eliminate personal bias. But if a change becomes desirable, the change and its effect should be clearly stated in the financial statements. Accounts should lend themselves easily to comparisons and contrasts. This convention increases accuracy and comparability of accounting information for prediction or decision making. This convention does not prohibit changes. If there is any change, its effect should be clearly stated in the financial statements.

2.4. Let Us Sum Up : In this lesson we have learnt meaning of accounting concept various elements of accounting concepts, meaning of accounting convention various elements of accounting convention.

2.5. Lesson End Activities :

1. What do you mean by accounting concepts ? Explain any four accounting concepts.

2. Briefly explain various accounting concepts which form the backbone of accounting.

3. What are accounting conventions ? Name and explain them in detail.

4. Write short note on

   i. Business entity concept.

   ii. Going concern concept

5. Write short note on

i. Convention of conservatism.

ii. Convention of Consistency

2.6. Model Answers to Check your Progress :

Question No. 1. Refer para 2.2.

Question No. 2. Refer para 2.2.1. to 2.2.10.

Question No. 3. Refer para 2.3.1. to 2.3.4.

Question No. 4. Refer para (i) 2.2.1. (ii) 2.2.3.

Question No. 5. Refer para (i) 2.3.2. (ii) 2.3.4.

2.7 References:

Financial Accounting – R.L. Gupta – Sultan chand & Sons
Advanced Accounting – S.N. Mageswari – Vikas Publishers

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LESSON 3

ACCOUNTING PROCEDURE

Contents :

3.0. Aims and Objectives

3.1. Introduction

3.2. Journal

3.3. Ledger

3.4. Subsidiary Books

3.5. Trial Balance

3.6. Fundamental Journal Entries

3.7. Illustrations

3.8. Let Us Sum Up

3.9. Lesson End Activities

3.10. Model Answers to Check your Progress

3.11 References

3.0. Aims and Objectives : In this lesson we are going to discuss

- meaning, rules and steps of journal
- meaning and process of ledger
- relationship between journal and ledger
- meaning, elements and advantages of subsidiary books
- meaning and rules of trial balance
- practical Illustrations of journal entries
- practical Illustrations of ledger accounts
- practical Illustrations for trial balance.

After reading this chapter you should be able to acquire basic working knowledge about the above mentioned topics.

3.1. Introduction :

In the previous two chapters we have discussed basic elements, concepts and conventions of accounting . In the present chapter we are going to discuss the various procedures involved in the process of accounting starting with journal and ending with trial balance .

3.2. Journal :

3.2.1. Meaning : Journal is the day-by-day of the business, wherein both the aspects of all business transaction are recorded in chronological order i.e. date – wise. The journal is, thus , a Book of Prime Entry. It is otherwise known as the Book of Original Entry. These entries are then posted from the journal into the ledger. As such, the ledger is known as the Principal Book or the Main Book. The journal merely helps the posting of entries from the journal into the ledger. Hence, journal is known as Sunsidiary Record or Subsidiary Book. Journalising is an act of recording the debit and credit aspects of a business transaction in journal together with an explanation of the transaction, known as Narration.

3.2.2. Rules of Journals :

The act of recording the transaction in journal is called journalising. This recording is made according to certain rules and these rules, are called rules of journalising. The business must enter into transactions with a number of persons or firms, possess some property, for example , cash, furniture, machinery etc., to carry on the business, pay certain expenses for example, rent salaries, wages etc., and receice certain incomes , for example, interest, commission etc. The following accounts are required to be maintained. Rules for Debit and Credit are

i. Personal Accounts
   Debit the Receiver
   Credit the Giver
ii. Real Accounts
   Debit what comes in
   Credit what goes out
iii. Nominal Accounts
   Debit all losses and expenses
   Credit all gains and incomes.

3.2.3. Compound Journal :

When many transactions of the same nature occur on a particular day, such transactions can be entered in the journal by means of combined Composite. journal entries, known as Compound Journal Entry. Make sure that the amount in the debit column equals to the amount in the credit column, based on the double entry system of book- keeping. One amount in the debit column must be equal to two or more amounts in the credit column or one amount in the credit column equals to two or more amounts in the debit column or under compound entry, a few debits it will be equal to a few credits. The rule for jounalising is the same as that of simple journal.

3.2.4. Steps in Journalising: The following are the steps in journalising:

i) Determine the two accounts which are involved in the transactions.
ii) Clasify the above two accounts under Persaonal, Real or Nominal.
iii) Find out the rules of debit and credit for the above two accounts.
iv) Identify which accounts are to be debited and which account is to be credited.
v) Record the date of transaction in the date column. The years and month are written once, till they change, the sequence of the dates and months should be strictly maintained.
vi) Enter the name of the account to be debited in the particulars column very close to the left hand side of the particulars column followed by the abbreviation Dr. in the same line against this, the amount to be debited is written in the debit amount, column in the same line.
vii) Write the name of the account to be credited in the second line starts with the word 'To' a few space away from the margin in the partculars column. Against this, the amount to be credited is written in the credit amount column in the same line.
viii) Write the narration within brackets in the next line in the particulars column.
ix). Draw a line across the entire particular column to seperate one journal entry from the other.

3.2.5.Advantages: The main advantages of the journal are: i. It reduces the possibility of errors ii. It provides an explanation of the transactions iii. It provides a chronological record of all transactions.

3.2.6. Limitations: The limitations of the journal are:i. It will be too long if all transactions re recorded here ii. It is difficult to ascertain the balance of each account.

3.3. Ledger

3.3.1..Meaning: As we know that first, all business transactions are recorded in the journal, separately and date-wise. The transactions relating to person, assets, expenses and income are journalized chronologically, i.e. date- wise. But one cannot find similar transactions at one place in the journal. Therefore, to have a consolidated view, we have to prepare different accounts in the ledger. No transaction gets into the ledger unless it appears first in the journal. The source of information for the ledger is the journal. Thus, journal is subsidiary to the ledger and the ledger is the principal or main book of account. The method of writing from journal to the ledger is called posting or ledger posting. It contains accounts related to business transactions. Ledger is a register, having a number of pages, which are numbered consecutively. One page in the ledger is usually allotted to one account. An index to various accounts in the ledger is given at the beginning of the ledger for easy reference.

An account is a summary of business transactions affecting a person or property or an income or an expense. An account is a brief history of financial dealings of a particular man or particular item. An account has two sides- Debit and Credit. The left side is known as Debit and the right side is known as Credit. Double entry book-keeping, means recording of both the receiving and giving aspects of every transaction. When an account receives a benefit, the account is debited. When an account gives a benefit, the account is credited. These two aspects are denoted by the symbols Debtor Dr. and Creditor Cr. respectively.

3.3.2. Relationship between Journal and ledger:

i. Transactions are entered first in the journal and then these entries are posted to appropriate accounts in the ledger.
ii. The journal is subsidiary book, while the ledger is the main book of accounts.

iii. The journal shows the transactions in chronological order, that is, journal is a daily record. Posting from the journal is done periodically, may be weekly or fortnightly etc.,
iv. Entering the transactions in the journal is called journalising and the act of recording in the ledger is called posting.
v. Journal is the book of prime entry, while ledger is the book of final entry.

3.3.3. Posting Process: The following procedure are followed for posting :

i) Left hand side of the Account :

a. Locate in the ledger , the first Account named in the journal.
b. Write the date of the transaction, in the date column, in debit- side of that account.
c. Enter in the debit – side of the ledger, in particulars column, the name of the Account credited with prefix ' To'
d. Write in folio column on the debit-side of the account, the page number of journal from which the entry is being posted.
e. Enter the amount, on the debit column of the ledger as per journal.
f. Similarly, write the ledger page number inthe folio column of the journal.

ii) Right hand side of the Account :

a. Locate in the ledger, the second Accounta named inthejournal.
b. Write the date of the transaction, in the date column on credit side of that Account.
c. Enter in the credit-side of the ledger, in particulars column, the name of the Account debited with prefix "By".
d. Write inthe folio column of the ledger, the page number of the journal from which the entry is being posted.
e. Enter the amount on the credit side of the ledger as per the journal.
f. Similarly, write the ledger page number in the folio column of the journal.

3.3.4. Balancing of an Account :

Debit side of the journal entry is posted to the debit side of the account and credit side of the journal entry is posted to the credit side of the account. After the ledger posting, accounts are closed and their balances are found out. There are three possibilities while striking the balance in an account i. the two sides of the account are equal ii. the debit total is greater than the credit total iii. The credit total is greater than the debit total.

If the two sides of an account are equal, it indicates the equality of benefitds received and given by that account. The account can be closed as there is no balance in that account. If debit side total of an account is greater than the credit total, then that account indicates a "Credit Balance". The proceedure to balance an account is:

(a) Total both the sides of the account , on rough sheet of paper.
b. Find out the difference between the total i.e. credit side and debit side. The difference is called balance.
c. Enter write. the differences balance. in the lesser side as Balnce c/d carried down. as the last item, and on the last date of the month.
d. Now, bith the sides are equal in total. Write the totals which are equal and close the account. The balance is afterwards taken to the opposite side and entered as balance b/d brought down. on the first day of the next month.

3.4. Subsidiary Books :

3.4.1. Meaning : Maintaining a single ‘ journal book’ in which journal entries are written for each transaction and posting them to ledger is practicable in small business where a single accountant can maintain accounts or the owner himself can do the accounts work. In bigger business, transactions are so numerous and varied that a single journal book is absolutely inadequate and cumbersome. Several accounts assistants may have to do accounts work as a team and share the burden. It may be necessary to group similar transactions even at journal stage in the shape of ‘ Special journals’ to minimise and facilitate ledger work. Thus, the system of Subsidiary Books as an alternative for single journal was developed.

3.4.2. Purchase Book : Purchase book is also known as ‘ bought book’ ‘Purchase day book’, invoice book’; and ‘purchase journal’. All credit purchase of goods are recorded in this book. Periodical total of this book provided total credit purchase of goods made by the firm.

3.4.3. Purchase Return Book : It is also called ‘Returns outward book’ and ‘ Purchase returns journal’. Goods returned to suppliers which were originally purchased on credit are recorded in this book. Periodically totals of this book provide data on purchase returns by the firm.

3.4.4. Sales Book : Sales book is also known as ‘Day book’, Sales day book’, ‘ Sold book’, Sales journal’, etc.All credit sales of goods are recorded in this book. Periodical totals of this book provide the total credit sales of goods by the firm.

3.4.5. Sales Returns Book : This book is also called ‘ Returns Inward Book’ and Sales Returns Journal’.Goods returned by customers which were originally sold on credit are recorded in this book. Monthly totals of this book provide data on sales returns. Credit notes sent to the customers after receiving the goods returned by them form the basis for entries in this book.

3.4.6. Debit Note: When goods are retuned to suppliers, a statement is sent to them information about the debit given to their account. This statement is called Debit Note. It is so called Debit Note., because of the Debit given to the concerned Party’s account.

3.4.7. Credit Note : Our customers may return goods to us. On receipt of the goods returned by the customers, a credit note is sent to them, by us, intimating the credit given to their account.This statement is called Credit Note.

3.4.8. Cash Book : One of the most important books maintained in any business concern is the cash book. The cash book records transactions connected with cash. The object of cash book is to keep a daily record of transactions relating to receipts and payments of cash. When the business is large, the number of transactions relating to cash are also usually large. Since, cash transaction form the major portion of the transactions of a business, it is necessary to keep a seperate book for cash transactions. If every transaction is entered in the jouranl, it will be tremendous job. Thus, it becomes necessary to have a cash book to record only the cash transactions.The following are the different types of cash book maintained in business firms :

i. Simple Cash Book
ii. Cash Book with Discount and Cash Columns.
iii.Cash Book with Discount, Cash and Bank Columns.
iv. Analytical Petty Cash Book.

3.4.9. Journal Proper : There are certain transactions, which cannot be entered in through any subsidiary books and such transactions are entered in the form of journal, called Journal Proper. From this journal proper, further their postings are made as usual. Examples of such transactions are: i. Opening entries ii. Transfer entries iii. Adjusting entries iv. Closing entries v. Rectification journal entries.vi. Credit Purchase or Sales of assets. vii. Bad debts.viii. Other entries not made in any other subsidiary books

3.4.10. Advantages of Subsidiary Books :

The advantages of maintaining sunsidiary books are as follows :

i. Division of labour : The division of journal resulting in division of work, ensures more clerks working independently in recording original entries in the subsidiary books.

ii. Efficiency : the division of labour also helps the reduction in work laod, saving in time and stationery. It alsogives advantages of sopecialisation leading to efficiency.

iii.Prevents Errors and Frauds : The accounting work can be divided in such a manner that the work of one person is automatically checked by another person. With the use of internal check, the possibility of occurance of errors and frauds may be avoided.

iv.Easy References : It facilitates easy references to any particular item. For instance total credit sales for a month can be easily obtained from the sale book.

v. Easy Postings : Postings from the subsidiary books are made at convienient intervals depending upon the nature of the business.

3.5. Trial Balance :

3.5.1. Meaning : Books of accounts of a firm are closed at the end of the year, but they may be closed at any time according to the requirements of the proprietor. When ever books are closed, balances are found out in various accounts and then , these balances are recorded in a statement which has four columns. viz Particulars, L.F, Debit Balances and Credit Balances and this statement is called Trial Balance. Thus, Trial Balance is a statement in which the debit and credit balances of all accounts are recorded with a view two ascertain the arithmetical accuracy of the books of accounts. The only condition is the accounts must be balance in order to draw a Trial Balance. Trial Balance is not a part of journal or ledger. It is only a list or statement. No posting can ever be made to a Trial Balance. Although it’s agreement always signals the presence of an error, this does not assured a conculsive proof as to the obsolute accuracy of the books in some cases.

3.5.2. Objectives : The objects of the preparation of the Trial Balance are as follows :

i. A Trial Balance provides a good check on the accuracy of the work done in preparing ledger accounts. When the total of the debit balances agree with total of credit balances, it is quite a good proof that the ledger acounts have been correctly written up. If the Trial balance totals do not agree, then it shows that there are some errors which must be detected and rectified, before final accounts are prepared.

ii. It brings together the balances of all the accounts at one place and thus facilitates the preparing the trading accounts and profit and loos acccounts, which is the results of the business; and the balance sheet to ascertain the financial position of the firm. In short, Trial Balance is the basic to prepare the final accounts.

iii. The balance of any accounts can be easily and convinently known by the trail balance.

iv. It serves as a summary of what is contained in the ledger.

3.5.3. Rules for Preparation of Trial Balance :

From the available balances of various ledger accounts, the trial balance shall be prepared on the basis of following rules.

Debit All Expenses and Assets .
Credit All Incomes and Liabilities.

3.6. Fundamental Journal Entries:

Following are the Journal entries for the important transactions usually take place in a business. The students are advised to use these entries to familiar with passing of journal entries.

1 For Capital Introduced
Cash A/c Dr
To Capital A/c

2 For Drawings Made
Drawings A/c Dr
To Cash A/c

3 For Deposit into Bank
Bank A/c Dr
To Cash A/c

4 For Withdrawl from the Bank
Cash A/c Dr
To Bank A/c

5 For Income Received
Cash A/c Dr
To Income

6 For Expenses paid
Expenses A/c Dr
To Cash A/c

7 For Purchases of Asset for Cash
Asset A/c Dr
To Cash A/c

8 For Purchases of Asset on Credit
Asset A/c Dr
To Seller A/c

9 For Purchases of Goods for Cash
Purchases A/c Dr
To Cash A/c

10 Purchases of Goods on Credit
Purchases A/c Dr
To Creditor A/c

11 For Sale of Asset for Cash
Cash A/c Dr
To Asset A/c

12 For Sale of Asset on Credit
Buyer A/c Dr
To Asset A/c

13 For Sale of Goods for Cash
Cash A/c Dr
To Sales

14 For Sale of Goods on Credit
Debtors A/c Dr
To Sales A/c

15 For Collection from Debtors
Cash A/c Dr
To Debtors A/c

16 For Payment to Creditors
CreditorsA/c Dr
To Cash A/c

17 For Purchase Returns
Creditors A/c Dr
To Purchase ReturnsA/c

18 For Sales Returns
Sales Returns A/c Dr
To Debtors

3.7. ILLUSTRATIONS

3.7.1. Passing of Journal Entries

Illustration: 1. Jouranlis the following transactions in the books of Miss Amudha.

		Rs.
01.01.2007	Amudha commenced business with cash	50,000
02.01.2007	Purchased goods for cash	10,000
05.01.2007	Purchased goods from Mohan on credit	6,000
07.01.2007	Paid into Bank	5,000
10.01.2007	Purchased furniture	2,000
20.01.2007	Sold goods to Suresh on credit	5,000
25.01.2007	Cash sales	3,500
26.01.2007	Paid to Mohan on account	3,000
31.01.2007	Paid salaries	2,800

Solution : Journal Entries in the books of Amudha

Date	Particulars		Debit Rs.	Credit Rs.
Jan 1	Cash A/c	Dr	50,000	
	To Amudha's Capital A/c			50,000
	Started business with capital.			
Jan 2	Purchase A/c	Dr	10,000	
	To Cash A/c			10,000
	Cash purchases.			
Jan 5	Purchase A/c	Dr	6,000	
	To Mohan A/c			6,000
	Credit purchase.			
Jan 7	Bank A/c	Dr	5,000	
	To Cash A/c			5,000
	Cash paid into bank.			
Jan 10	Furniture A/c	Dr	2,000	
	To Cash A/c			2,000
	Furniture purchased.			
Jan 20	Suresh A/c	Dr	5,000	
	To Sales A/c			5,000
	Credit sales.			
Jan 25	Cash A/c	Dr	3,500	
	To Sales A/c			3,500
	Cash sales.			
Jan 26	Mohan A/c	Dr	3,000	
	To Cash A/c			3,000
	Cash paid to Mohan.			
Jan 31	Salaries A/c	Dr	2,800	
	To Cash A/c			2,800
	Salaries paid.			

Illustration:2. Journalise the following transactions of Miss. Banu for the year 2007.

		Rs.
Jan 1	Banu commenced business with cash	30,000
Jan 2	Paid into bank	21,000
Jan 3	Purchased goods by cheque	15,000
Jan 7	Drew cash from bank for office use	3,000
Jan 15	Purchased goods from Siva	15,000
Jan 20	Cash sales	30,000
Jan 25	Paid to Siva	14,000
”	Discount Received	250
Jan 31	Paid rent	500
”	Paid Salaries	2,000

Solution:

Date	Particulars		Debit Rs.	Credit Rs.
2007 Jan 1	Cash A/c	Dr	30,000	
	To Banu Capital A/c			30,000
	Banu started business with cash.			
2	Bank A/c	Dr	21,000	
	To Cash A/c			21,000
	Cash paid into bank.			
3	Purchase A/c	Dr	15,000	
	To Bank A/c			15,000
	Purchase through cheque.			
7	Cash A/c	Dr	3,000	
	To Bank A/c			3,000
	Cash withdrawn from bank.			
15	Purchase A/c	Dr	15,000	
	To Siva A/c			15,000
	Credit purchases.			
20	Cash A/c	Dr	30,000	
	To Sales A/c			
	Cash sales.			30,000

25	Siva A/c	Dr	15,000	
	To Cash A/c			14,750
	To Discount A/c			250
	Cash paid to siva and discount received.			
31	Rent A/c	Dr	500	
	Salaries A/c	Dr	2,000	
	To Cash A/c			2,500
	Rent, Salaries etc paid.			

3.7.2. Preparation of Ledger Accounts :

Illustration :3. Journalise the folllowing transactions of Miss. Chitra and post them in the ledger and balance the same relating to June 2007.

1 Chitra invested Rs. 5,00,00 cash in the business.

3 Paid into Bank Rs. 80,000

5 Purchased building for Rs. 3,00,000

7 Purchased goods for Rs. 70,000

10 Sold goods for Rs. 80,000

15 Withdrew cash from bank Rs. 10,000

25 Electricity Charges Rs. 3,000

31 Salaries Rs. 15,000

Solution :

Journal Entries in the Books of Miss Chitra

Date	Particulars		Debit Rs.	Credit Rs.
Jun 1	Cash A/c	Dr	5,00,000	
	To Chitra capital A/c			5,00,000
	Started business with cash.			
3	Bank A/c	Dr	80,000	
	To Cash A/c			80,000
	Cash paid into bank.			
5	Building A/c	Dr	3,00,000	
	To Cash A/c			3,00,000
	Building purchased.			

7	Purchase A/c To Cash Cash purchase.	Dr	70,000	70,000
10	Cash A/c To Sales A/c Cash sales.	Dr	80,000	80,000
15	Cash A/c To Bank A/c Cash withdrawn from Bank.	Dr	10,000	10,000
25	Electric Charges A/c To Sales A/c Electri charge paid.	Dr	3,000	3,000
30	Salary A/c To Cash A/c Salary paid.	Dr	15,000	15,000

Ledger Accounts in the books of Miss.Chitra

Capital Account

Date	Particulars	Rs.	Date	Particulars	Rs.
30.6.07	To Balance c/d	**5,00,000**	1.6.07	By Cash A/c	5,00,000
		5,00,000			5,00,000
			1.7.07	By Balance b/d	**5,00,000**

Cash Account

Date	Particulars	Rs.	Date	Particulars	Rs.
Jun 1	To Chitra capital A/c	5,00,000	June 3	By Bank A/c	80,000
10	To Salaries A/c	80,000	5	By Building A/c	3,00,000
15	To Bank A/c	10,000	7	By Purchase A/c	70,000
			25	By Electricity A/c	3,000
			30	By Salary A/c	15,000
				By Balance c/d	**1,22,000**
		5,90,000			5,90,000
	To Balance b/d	**1,22,000**			

Bank Account

Date	Particulars	Rs.	Date	Particulars	Rs.
03.6.07	To Cash	80,000	15.6.07	By Cash A/c	10,000
			30.6.07	By Balance c/d	**70,000**
		80,000			80,000
01.7.07	To Balance b/d	**70,000**			

Building Account

Date	Particulars	Rs.	Date	Particulars	Rs.
5.6.07	To Cash A/c	3,00,000	30.6.07	By Balance c/d	**3,00,000**
		3,00,000			3,00,000
1.7.07	To Balance b/d	**3,00,000**			

Purchases Account

Date	Particulars	Rs.	Date	Particulars	Rs.
1.6.07	To Cash A/c	70,000	30.6.07	By Balance c/d	**70,000**
		70,000			70,000
1.7.07	To Balance b/d	**70,000**			

Sales Account

Date	Particulars	Rs.	Date	Particulars	Rs.
30.6.07	To Balance c/d	**80,000**	10.6.07	By Cash A/c	80,000
		80,000			80,000
			1.7.07	By Balance b/d	**80,000**

Electricity charges Account

Date	Particulars	Rs.	Date	Particulars	Rs.
25.6.07	To Cash A/c	3,000	30.6.07	By Balance c/d	**3,000**
		3,000			3,000
1.7.07	To Balance b/d	**3,000**			

Salary Account

Date	Particulars	Rs.	Date	Particulars	Rs.
30.6.07	To Cash A/c	15,000	30.6.07	By Balance c/d	**15,000**
		15,000			15,000
1.7.07	To Balance b/d	**15,000**			

3.7.3. PreparationTrial Balance:

Illustration :4. The following balances are extracted from the books of Miss.Dhivya. Prepare trial balance as on 30.12.2007.

Particulars	Rs.
Capital	4,70,000
Cash in hand	6,000
Building	3,20,000
Stock	33,000
Sundry creditors	26,000
Commission paid	750
Rent & Taxes	6,300
Purchases	1,65,000
Salaries	70,600
Discount allowed	650
Drawings	5,000
Bad debts	1,350
Machinery	1,58,800
Sundry Debtors	48,000
Repairs	5,400
Insurance premium	3,300
Sales	2,90,000

Telephone charge	6,450
Furniture	11,000
Discount earned	1,100
Loan from Mohammed	51,000
Reserve fund	5,900
Bills receivable	8,600
Bills payable	6,000

Solution :

Trial Balance of Miss. Divya as on 31.12.2007

Particulars	Dr.	Cr.
Capital		4, 70,200
Cash in hand	6,000	
Building	3,20,000	
Stock	33,000	
Sundry creditors		26,000
Commission paid	750	
Rent & Taxes	6,300	
Machinery	1,58,800	
Sundry Debtors	48,000	
Rapairs	5,400	
Insurance premium	3,300	
Sales		2,90,000
Telephone charges	6,450	
Furniture	11,000	
Discount allowed	650	
Purchases	1,65,000	
Salaries	70,000	
Drawings	5,000	
Bad debts	1,350	51,000
Loan from Mohammed		1,100
Discount earned		5,900
Reserve fund		
Bills receivable	8,600	
Bills payable		6,000
Total	**8,50,200**	**8,50,200**

Illustration :5. Miss. Eswari provides the following particulars as on 31.12.2007, prepare Trial Balance as on the above date.

	Rs.
Commenced business capital	5,00,000
Purchases Furniture for	20,000
Purchases goods	1,00,000
Purchases goods on credit form Guna	2,00,000
Cash sales	1,50,000
Credit sales	2,00,000
Salarise paid	10,000
Interest Received	5,000

Solution :

Journals Entries in the Books of Miss. Eswari for the year ended 31.12.2007

Particulars		Dr.	Cr.
Cash A/c	Dr	5,00,000	
To Capital A/c			5,00,000
Being Capital Introduced.			
Furniture A/c	Dr	20,000	
To Cash A/c			20,000
Being Furniture Purchasesed.			
Purchases A/c	Dr	1,00,000	
To Cash A/c			1,00,000
Being goods Purchases for cash.			
Purchases A/c	Dr	2,00,000	
To Guna A/c			2,00,000
Being goods Purchases an credit.			
Cash A/c	Dr	1,50,000	
To Sales A/c			1,50,000
Being cash sales.			
Debtors A/c	Dr	2,00,000	
To Sales A/c			2,00,000
Being credit sales.			
Salaries A/c	Dr	10,000	
To Cash A/c			10,000
Being Salaries paid.			
Cash A/c	Dr	5,000	
To Interest A/c			5,000
Being interest received.			

Ledger Accounts in the books of Miss. Eswari for the year ended 31.12.2007.

Cash A/c

Particualrs	Rs	Particulars	Rs
To Capital	5,00,000	By Furniture	20,000
To Cash	1,50,000	By Purchases	1,00,000
To Interest	5,000	By Salaries	10,000
		By Balance c/d	**5,25,000**
	6,55,000		6,55,000
To Balance b/d	**5,25,000**		

Capital A/c

Particualrs	Rs	Particulars	Rs
To Balance c/d	**5,00,000**	By Cash	5,00,000
	5,00,000		5,00,000
		By Balance b/d	**5,00,000**

Furniture A/c

Particualrs	Rs	Particulars	Rs
To Cash	20,000	By Balance c/d	**20,000**
	20,000		20,000
To Balance b/d	**20,000**		

Purchases A/c

Particualrs	Rs	Particulars	Rs
To Cash	1,00,000	By Balance c/d	**3,00,000**
To Credit	2,00,000		
	3,00,000		3,00,000
To Balance b/d	**3,00,000**		

Sales A/c

Particualrs	Rs	Particulars	Rs
To Balance c/d	**3,50,000**	By Cash	1,50,000
		By Credit	2,00,000
	3,50,000		3,50,000
		By Balance b/d	**3,50,000**

Creditors A/c

Particualrs	Rs	Particulars	Rs
To Balance c/d	**2,00,000**	By Purchases	2,00,000

	2,00,000		2,00,000
		By Balance b/d	**2,00,000**

Debtors A/c

Particualrs	Rs	Particulars	Rs
To Salas	2,00,000	By Balance c/d	**2,00,000**
	2,00,000		2,00,000
To Balance b/d	**2,00,000**		

Salary A/c

Particualrs	Rs	Particulars	Rs
To Cash	10,000	By Balance c/d	**10,000**
	10,000		10,000
To Balance b/d	**10,000**		

Interest A/c

Particualrs	Rs	Particulars	Rs
To Balance c/d	**5,000**	By Cash	5,000
	5,000		5,000
		By Balance b/d	**5,000**

Trial Balance of Miss. Eswari as on 31.12.2007

Particulars	Debit	Credit
Capital		5,00,000
Furniure	20,000	
Purchases	3,00,000	
Sales		3,50,000
Debtors	2,00,000	
Creditors		2,00,000
Salaries	10,000	
Interest		5,000
Cash	5,25,000	
Total	**10,55,000**	**10,55,000**

3.8. EXCERCISES

3.8.1. Passing of Journal Entries :

Exercise: 1. Journalise the following transactions of Mr.Arun for the Month of January 2007.

			Rs.
Jan	3	Received cash from Ramkumar	60,000
	4	Purchased goods for cash	15,000
	11	Sold goods to Damodaran	22,000
	13	Paid to Ramkumar	40,000
	17	Received from Damodaran	20,000
	20	Bought furniture from Jagadeesan	5,000
	27	Paid rent	1,200
	30	Paid salary	2,500

Excercise :2 Journalise the following transactions of Mr.Balaji for the Month of January 2007

			Rs.
Jan	1	Received cash form Siva	75,000
	7	Paid cash to Sayeed	45,000
	10	Bought goods for cash	27,000
	12	Bought goods on credit form David	48,000
	15	Sold goods for cash	70,000

Excercise:3. Journalise the following transactions of Mr.Cheran for the Month of January 2007

			Rs
Jan	3	Bought goods for Cash	84,500
	7	Sold goods to Dhanalakshmi on credit	55,000
	9	Received Commission	3,000
	10	Cash Sales	1,09,000
	12	Bought goods from Mahalashmi	60,000
	15	Recieved five chairs from Revathi & Co at Rs. 400 each	
	20	Paid Revathi & Co, cash for five chairs	
	28	Paid Salaries	10,000
		Paid Rent	5,000

Excercise:4. Journalise the following transactions of Mr.Dhayalan for the Month of January 2007**.**

		Rs.
Jan 1	Sold goods on credit to Mohanasundaram	75,000
12	Purchased goods on credit from Bashyam	70,000
15	Sold goods for cash form David	50,000
20	Received from Mohanasundaram	70,000
25	Paid to Bashyam	50,000

Excercise: 5 Journalise the following transactions of Mr.Arun for the Month of January 2007

		Rs.
Jan.1	Started business with cash	1,25,000
3	Purchased goods	20,000
5	Cash sales	37,000
6	Cash sales	18,000
7	Purchasesd from Mr. Velusamy	50,000
8	Crdit sales to Mr. Palani	60,000
12	Bought furniture	7,000
18	Sales to Mr. Selvendran	18,000
24	Purchased goods	1,30.000
28	Cash sales	55,000
30	Cash received from Palani	60,000
30	Paid to Mr. Velusamy	50,000

Excercise:6 Journalise the following transactions of Mr.Favourable for the Month of Jan 2007.

		Rs.
Jan 1	Started business with cash	2,50,000
6	Bought furniture	15,000
7	Cash purchase	90,000
9	Cash sales	40,000

10	Cash purchase	25,000
14	Credit sales to Moorthy	15,000
15	Credit purchase from Mr. Venkat	15,000
16	Cash sales	44,000
17	Received from Moorthy	14,500
17	Allowed discount	500
21	Paid to Venkat	14,700
21	Discount allowed by him	300
26	Advertisement	4,000
27	Electricity	2,700
30	Sales	72,000
31	Rent	4,000
31	Salaries	15,000
31	Telephone Charges	6,700

Excercise :7 Journalise the following transactions of Mr.Gokul for the Month of Jan 2007.

		Rs.
Jan 1	Introduced cash as capital	45,000
3	Paid into Bank	25,000
4	Sales	18,000
5	Purchases	15,000
18	Cash collected from Chezhian	23,700
21	Withdrawn for office use	5,000
25	Telephone charges	1,400
26	Cash sales	7,000
27	Credit purchases from Muthu	7,500
28	Credit sales to Kumar	12,000
29	Paid to Muthu	7,500
30	Cash received from Kumar	11,500
	Allowed discount	500

Excercise:8. Journalise the following transactions of Mr.Happy for the Month of Jan 2007.

		Rs.
Jan1.	Purchased goods for cash	10,000
2.	Purchased stationery for cash	500
3.	Purchased furniture for cash	3,000

4.	Sold goods for cash	8,000
5.	Sold goods to Jagan for cash	3,000
6.	Sold goods to James	2,000
7.	Paid Rent to Krishnan, the landlord	800
8.	Paid salary	8,000
9.	Paid salary to the manager Mr. Lokesh	3,000
10.	Paid freight on goods purchased	300
11.	Paid freight on machine purchased	400
12.	Paid wages	500
13.	Paid Wages to erect a machine	1,000

Excercise:9. Journalise the following transactions of Mr.Indian for the Month of Jan 2007

Jan	1	Business started with Rs. 2,50,00 and cash	Rs.
		Deposited with Bank	1,50,000
	3	Purchased machinery on credit from Rangan	50,000
	6	Bought furniture from Ramesh for cash	25,000
	12	Goods sold to Yesodha	22,500
	13	Goods Returned by Yesodha	2,500
	15	Goods sold for cash	50,000
	17	Bought goods for cash	25,000
	20	Cash received from Yesodha	10,000
	21	Cash paid to Raman	20,000
	25	Cash withdrawn from bank	50,000
	29	Paid advertisement expenses	12,500
	30	Bought office stationery for cash	5,000
	31	Cash withdrawn from bank for personal use of the proprietor	6,250
	31	Paid salaries	15,000
	31	Paid rent	2,500

Excercise:10. Journalise the following transactions of Mr.Jaggu for the Month of Jan 2007.

			Rs
Jan	1	Arul commenced business with	21,000
	2	Bought goods for Cash	9,200

4	Sold goods to Kannan on Credit	5,600
5	Purchased goods form Mani	3,300
9	Received Cash from Kannan	3,600
11	Paid Mani on account	2,100
16	Sold goods to Manohar	3,500
21	Cash Sales	7,500
26	Paid Mani	1,200
29	Received Cash from Manohar	3,500
30	Paid Rent	450
30	Paid Salaries to Office Staff	700

3.8.2. Preparation of Ledger Accounts

Excercise :11 Journalise the following transactions of Mr.Karuna and post them to proper ledger accounts relating to the month of January 2007.

		Rs.
Jan. 1	He started business with a capital of	10,000
4	Bought goods from Velan	6,750
7	Cash Purchases	3,000
10	Cash Sales	4,000
13	Bought goods from Velan	2,000
16	Sold goods to Gurunath	5,000
18	Paid Cash to. Velan	2,850
19	Sold goods to Gurunath	500
24	Paid Velan on account	2,400
26	Reecived cash from Gurunath	1,650
27	Paid Salaries	1,250

Excercise:12 . Journalise the following transactions of Mr.Lallu and post them to proper ledger accounts relating to the month of January 2007.

		Rs
Jan 1	Started business with	4,50,000
3	Goods purchased	70,000
5	Doods sold	15,000
10	Goods purchased from Rangasamy	2,00,000
16	Goods returned to Rangasamy	5,000
23	Drew from bank	30,000

26	Furniture purchased	10,000
26	Settled Rangasamy's account	
31	Salaries paid.	12,000

Excercise:13 Journalise the following transactions of Mr.Murugan and post them to proper ledger accounts relating to the month of January 2007.

			Rs.
Jan	1	He started business with	3,00,000
	3	Opened a current account with Indian Overseas Bank	50,000
	12	Bought goods from Tmt. Sumathi	90,000
	18	Paid to Tmt. Sumathi	90,000
	20	Sold goods to Tmt. Chitra	1,26,000
	26	Tmt. Chitra settled her account	

Excercise:14. Journalise the following transactions of Mr. Naresh and post them to proper ledger accounts relating to the month of January 2007.

			Rs.
Jan	5	Sold goods to Arumugam on Credit	17,500
	9	Bought goods for cash from Chellappan	22,500
	12	Met Travelling expenses	2,500
	15	Sivakumar Received from as loan	80,000
	21	Paid wages to workers	3,000

Excercise:15. Journalise the following transactions of Mr.Original and post them to proper ledger accounts relating to the month of January 2007.

			Rs
Jan	1	He commenced business with the following assets and liabilities.	
		Plant and Machinery	2,50,000
		Stock	90,000
		Furniture	7,000
		Cash	50,000
		Sundry creditors	1,50,000
	2	Sold goods to Sundar	1,50,000
	3	Bought goods from Natarajan	56,000
	4	Sundar Paid cash	1,25,000
	5	Returned damaged goods to Natarajan	2,000
	9	Paid to Natarajan	28,000
	31	Paid Rent	5,000
		Paid Salaries	9,000

Excercise:16. Journalise the following transactions of Mr.Purushothaman and post them to proper ledger accounts relating to the month of January 2007.

		Rs
Jan 1	Received cash from Ramesh	1,60,000
5	Bought goods for cash	60,000
7	Sold to Suresh	30,000
15	Bought from Dayalan	40,000
18	Sold to Ganesan	50,000
20	Withdrew cash for personal use	18,000
25	Received commission	20,000
30	Paid Rent	5,000
30	Paid Salary	10,000

3.8.3. Preparation of Trial Balance:

Excercise:17. Prepare Trial Balance as on 31.3.2004 from the books of Miss Quick.

	Rs.
Capital	2,49,000
General expenses	97,000
Machinery	1,18,000
Wages	14,000
Bad debts	1,100
Sales	3,30,000
Commission	5,500
Bills payable	7,700
Bank overdraft	28,600
Discount	1,210
Drawings	24,000
Building	78,000
Stock	1,32,400
Insurance	2,610
Creditors	5,000
Loan Cr..	75,000
Purchases	2,10,800
Reserve Fund	15,000
Cash in hand	25, 320

Excercise :18. Prepare trial balance as on 31.12.2002 from the following balances of Mr. Raghul.

	Rs.
Drawings	74,800
Stock 1.1.2007.	30,000
Capital	2,50,000
Furniture	33,000
Sundry creditors	75,000
Printing charges	1,500
Bank loan	1,20,000
Freight	3,500
Income tax	9,500
Machinery	2,15,400
Purchases	2,95,700
Discount received	1,000
Discount allowed	950
Sales	3,35,350
Rent	72,500
Sundry expenses	21,000
Bills receivable	52,500
Carriage outwards	1,500
Insurance	1,200
Bills payable	31,700

Excercise:19. Prepare trial balance as on 31.3.2007 from thefollowing balance of Mr. Sathish..

	Rs.
Drawings	43,000
Capital	2,12,000
Sundry creditors	61,500
Bills Payable	22,000
Sundry Debtors	55,000
Bills Receivable	72,600
Loan from Shyam	2,50,000

Furniture & Fittings	12,250
Opening stock	2,23,500
Cash at bank	86,250
Purchases	2,98,000
Sales	3,64,000
Salaries	44,950
Sales return	500
Purchases return	2,550
Travelling expenses	12,300
Commission Paid	250
Discount earned	2,000
Cash in hand	65,450

Excercise: 20. Prepare trial balance as on 31.3.2007 from the following balance of Mr.Tamil Mani.

	Rs.
Capital	4,20,000
Building	1,15,000
Machinery	60,000
Furniture	11,000
Car	68,000
Opening stock	86,000
Purchases	94,000
Sales	1,96,000
Sundry debtors	16,200
Reserve for	7,300
Cash in hand	25,000
Cash at bank	84,700
Salaries	94,000
Rent	48,000
Commission	1,400
Rates and Taxes	2,600
Bad debts	3,200

Insurance	2,400
Geneal Expense	800
Sundry Creditors	68,000

3.9. Let Us Sum Up : In this lesson we have discussed a theoretical procedure of accounting equation and practical applications of journal, ledger and trial balance.

3.10. Lesson End Activities :

1. What is meant by journal ? Mention the rules for journalizing .
2. What is meant by ledger ? Explain the rules regarding posting and balancing of ledger accounts .
3. What is meant by subsidiary books ? What are its various contents ?

3.11. Model Answers to Check your Progress :

Ex : 17.
Debit : 97,000 +78,000 + 24,000 + 1,32,400 + 2,610 + 1,100 + 5,500
+ 25,320 + 1,18,680 + 14,400 + 1,210 + 2,10,800 = **7,11,020**
Credit : 2,49,000 + 3,30,720 + 7,700 + 28,60 + 5,000 + 75,000+ 15,000 = **7,11,020**

Ex : 18.
Debit : 30,000 + 74,800 + 33,000 + 2,95,700 + 950 + 1500 + 3,500 +
` 9500 + 2,15,400 + 72,500 + 21,000 + 52,500 + 1,500 + 1,200 = **8,13,050**
Credit : 2,50,000 + 1,000 + 3,35,350 + 75,000 + 1,20,000 + 31,700 = **8,13,050**

Ex : 19.
Debit : 43,000 + 72,600 +55,000 + 2,98,000 + 86,250 + 250 + 44,950
+ 500 + 12,300 + 12,250 + 2,23,500 + 65,450 = **9,14,050**
Credit : 2,12,000 + 61,500 + 22,000 + 3,64,000+2,550 + 2,50,000+ 2,000 = **9,14,050**

Ex : 20
Debit : 1,15,000 + 60,000 + 11,000 + 68,000 + 86,000 + 94,000
+ 16,200 + 25,000 + 84,700 + 94,000 + 48,000 + 1,400 + 2,600
+ 3,200 + 2,400 + 800 = **7,12,300**
Credit : 4,20,000 + 1,96,000 + 7,300 + 68,000 + 21,000 = **7,12,300**

3.12 References :

Financial Accounting – R.L. Gupta – Sultan chand & Sons
Advanced Accounting – S.N. Mageswari – Vikas Publishers

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