UNIT - II
INTRODUCTION TO FINANCIAL ACCOUNTING

FINANCIAL ACCOUNTING

Every trader generally starts business for the purpose of earning profit. So, he establishes business with capital, purchases machinery, raw materials, etc., buys and sells goods and incurs some expenses. So, at the end of the period he wants to know whether his business has made profit or loss. For this purpose, he prepares profit and loss account and also to know what he owns (assets) and what he owes (liabilities), he prepares Balance Sheet. Hence accounting is the Language of Business.

Book-keeping is an art of recording the business transactions in the books of original entry and the ledgers. Accountancy begins where Book-keeping ends. Accountancy means the compilation of accounts in such a way that one is in a position to know the state of affairs of the business.

Definition:

R.N. Anthony: "Accounting system is a means of collecting summarizing, analyzing and reporting in monetary terms, the information about the business.

American Institute of Certified Public Accountants (AICPA): "The art of recording, classifying and summarizing in a significant manner and in terms of money transactions and events, which are in part at least, of a financial character and interpreting the results thereof."

Objectives:

The main objectives of Accounting are:

1. To maintain the permanent records of the business transactions.
2. To ascertain the profit earned or loss suffered during accounting period.
3. To know various business Assets and liabilities apart from the above main objectives.
4. To know amount due to businessman from his customers.
5. To know amount payable to Suppliers.
6. To know various taxes and duties payable to government.
7. To detect and prevent errors and frauds committed by employees and other person.
8. To provide valuable information for taking for taking various decisions.
9. To take decision on significant business matters.
10. To compare and measure the optional efficiency of his business with other firm, companies in same type of Industry.
11. To review the progress of the business from year to year.
12. To maintain permanent record of all transactions of business for future reference.
13. To excise effective control on various expenses, incomes earned over business assets, business liabilities.
14. Other firms, Companies and within the firm compare current year with previous years. Such comparison is known as infra-firm comparison.

ACCOUNTING PRINCIPLES

The rules and conventions of accounting are commonly referred to as principles. The American institute of certified public accountants has defined the accounting principle as, "a general law or rule adopted or professed as a guide to action; a settled ground or basis of conduct or practice". It may be noted that the definition describes the accounting principle as a general law or rule that is to be used as a guide to action.

Accounting principles are judged on their general acceptability to the makers and users of financial statements and reports. They present a generally accepted and uniform view of the accounting profession in relation to good accounting practice and procedures. Therefore, it is named as "**Generally Accepted Accounting Principles**."

Accounting principles, rules of conduct and action are described by various terms such as concepts, conventions, doctrines, tenets, assumptions, axioms, postulates, etc. But for our purpose we shall use all these terms synonymously except for a little difference between the two terms – concepts and conventions. The term "concept" is used to connote accounting postulates i.e. Necessary assumptions or conditions upon which accounting is based. The term convention is used to signify customs or traditions as a guide to the preparation of accounting statements.

The classification of accounting principles is as under:

Accounting Principles

Accounting Concepts	**Accounting Conventions**
1) Business entity concept	1) Disclosure
2) Going Concern concept	2) Materiality
3) Money Measurement concept	3) Consistency
4) Cost Concept	4) Conservatism
5) Accounting period concept	
6) Dual Aspect concept	
7) Matching concept	
8) Realization concept	

ACCOUNTING CONCEPTS

Concepts mean a general idea which conveys certain meaning. Accounting concepts may be considered as basis assumption or conditions on which the science of accounting is based. Concepts are based on logical consideration. Accounts and Financial statements are always interpreted in light of concepts which govern accounting method. Different accounting concepts are discussed as follows:

1. **Business Entity Concept:** According to entity concept, business is treated as a unit of entity form separate from its Owner, Creditors and Management, etc. Accounts are kept for business entity as distinguished from a person associated with it. All business transactions are recorded in the books of Accounts from the point of view of business only. Every type of business organization is treated as separate accounting entity. The failure to recognize the business as separate accounting entity would make it extremely difficult to evaluate the performance of business alone.

2. **Going Concern Concept:** Business transactions are recorded on the assumption that the business will continue for a long time. There is neither the intention nor the necessity to liquate the particular business in near future. Therefore, it would be able to meet its contractual obligation and use its resources according to the plans and predetermined goals. Therefore, Fixed Assets are recorded at cost and depreciation is calculated on cost/written down value. Similarly, prepaid expenses are treated as Assets on the presumption that the business will continue and these expenses will be utilized in future.

3. **Money Measurement Concept:** A unit of exchange and measurement is necessary to account for business transaction in a uniform manner. Money is common denominator in terms of which the exchange ability of goods and services are measured. Only such transactions and events as can be interpreted in terms of money are recorded. Non-monetary events like public political contract, location of business; certain disputes, etc. cannot be recorded in the books of Accounts even through these have great effects. However, a unit of money measurement over period of time has its own drawbacks.

4. **Cost Concept:** According to cost concept the various assets acquired by enterprise should be recorded on the basis of actual cost incurred. The cost concept does not mean that the basis for all subsequent accounting for the assets. As per cost concept Fixed Assets are shown at cost less depreciation charged from year to year. It may be noted that if nothing has been paid for acquiring something it would not be shown/recorded in the books of accounts maintain. Financial statement based on historical cost may not be much relevant for investors and other users because they are more interested in knowing what the business actually worth today rather than the original cost.

5. **Accounting Period Concept:** It is customary that the life of the business is divided into appropriate parts or segments of analyzing the results shown by the business. Each part divided is known as an accounting period. It is an internal of time at end of which the income statement and balance sheet are prepared. Normally the accounting period consists of twelve months.

6. **Matching Concept:** This concept is based on accounting period concept for determining accurate profit/income has to compare the revenues of the business with the cost that is incurred to earn that revenue. The term “Matching” means appropriate association of related revenues and expenses. According to this concept adjustments should be made for all outstanding expenses, income receivable, prepaid expenses, Income received in advance, depreciation, etc. While preparing final accounts at the end of accounting period.

7. **Realization Concept:** This accounting concept explains that sell is supposed to be completed only when ownership of goods is passed on from the seller to the buyer. Income is considered to be earned on the date when sales take place. No profit is supposed to accrue on the acquisition of anything, however, income earned / realized will be earn only when goods are sold at a profit. Therefore, closing stock is valued at cost or market price whichever is less. It prevents business Firms from inflecting their profits by recording income that is expected in future.

8. **Dual Aspect Concept:** This concept based on double entry book-keeping which means that accounting system is set up in such a way that a record is made of the two aspects of each transaction that affects the record. The recognition of the two aspects of every transaction is known as duel aspects concept. Modern Financial Accounting considers both aspects of every transaction. One entry consists of debit to one or more accounts and another effect consist of credit to some other one or more accounts. However, the total amount debited is always equal to the total amount credited. Therefore, at any point of time total assets of a business are equal to its total liabilities. Liabilities to outsider are known as liabilities, liabilities to the owner are referred to as capital.

Assets = Liabilities + Capital

Therefore, Capital = Assets – Liabilities

ACCOUNTING CONVENTIONS

The term 'Convention' denotes customs or traditions or practice based on general agreement between the accounting bodies which guide the accountant while preparing the financial statements.

1. **Disclosure:** According to convention of full disclosure, accounting must disclose all the material facts and information so that interested parties after reading such accounting report can get a clear view of the state of affairs of the business. All information which is of material interest to proprietors, creditors and investors should be disclosed in accounting statement. The Companies Act makes various provisions for disclosure of essential information that there is no chance of any material information being left out.

2. **Materiality:** The term material means "relative importance", Accounting to the convention of materiality; account should report only what is material and ignore insignificant details while the preparing the final accounts. Materiality will differ or changed with nature, size and tradition of the business. What is material for one enterprise may be immaterial for another enterprise. This is because otherwise accounting will unnecessarily be overburdened with minute details. It is not possible to lay down any fixed standard by which Materiality can be judged. The decision is to be made by the accountant or the Auditor based on their professional experience.

3. **Consistency:** This accounting convention state that one's a particular accounting practice, method or policy is adopted to prepare accounts, statements and Reports. It should be continued for years together and should not charge unless it is forced to change it. Accounting practices should remain the same from one year to another. The results of different years will be comparable only when accounting rules are continuously adhered to from years to years i.e. Valuation of stock in trade, method of depreciation, treatment of approval sale etc. Since methods of accounting consistence, the financial statements are reliable to the people who use it.

4. **Conservatism:** Financial Statements are usually drawn up on a conservative basis. There are two principles which stem directly from conservatism.
   - The accountant should not anticipate income and should provide all possible losses, and
   - Faced with the choice between two methods of valuing an asset the accountant should choose a method which leads to the lesser value.

Accounting convention must be followed continuously. If not followed continuously it would result into understatement of incomes, assets and overstatement of liabilities and provisions and expenses.

DOUBLE ENTRY SYSTEM

It was in 1494 that Luca Pacioli the Italian mathematician, first published his comprehensive treatise on the principles of Double Entry System. The use of principles of double entry system made it possible to record not only cash but also all sorts of Mercantile transactions. It had created a profound impact on auditing too, because it enhanced the duties of an auditor to a considerable extent.

The Double entry system is based on scientific principle and is used universally by most of business organisations. This system recognises the fact that every transaction has two aspects and records both aspects of each and every transaction. Thus, every transaction has two aspects i.e. receiving and giving. The receiving aspect is also known as the incoming aspect (Debit) and going aspect is known as the outgoing aspect (credit). For every transaction there will be a debit and credit entry. These debits and credits will be equal and opposite. If a debit increases assets, then a credit counter item has to increase liabilities or owner's equity. Thus, increases and decreases in assets and liabilities (or owner‘s equity) must be recorded opposite to each other.

Basic accounting equation:

Assets = Liabilities + Equity + Profit (Income-Expenses)

Assets + Expenses = Liabilities + Equity+ Income

Features of Double Entry System:

1. Every transaction has two-fold aspects, i.e., one party giving the benefit and the other receiving the benefit.
2. Every transaction is divided into two aspects, Debit and Credit. One account is to be debited and the other account is to be credited.
3. Every debit must have its corresponding and equal credit.

Advantages of Double Entry System:

1. Since personal and impersonal accounts are maintained under the double entry system, both the effects of the transactions are recorded.
2. It ensures arithmetical accuracy of the books of accounts, for every debit, there is a corresponding and equal credit. This is ascertained by preparing a trial balance periodically or at the end of the financial year.
3. It prevents and minimizes frauds. Moreover, frauds can be detected early.
4. Errors can be checked and rectified easily.
5. The balances of receivables and payables are determined easily, since the personal accounts are maintained.
6. The businessman can compare the financial position of the current year with that of the past year/s.
7. The businessman can justify the standing of his business in comparison with the previous year's purchase, sales, and stocks, incomes and expenses with that of the current year figures.
8. Helps in decision making.

9. The net operating results can be calculated by preparing the Trading and Profit and Loss A/c for the year ended and the financial position can be ascertained by the preparation of the Balance Sheet.
10. It becomes easy for the Government to decide the tax.
11. It helps the Government to decide sickness of business units and extend help accordingly.
12. The other stakeholders like suppliers, banks, etc., take a proper decision regarding grant of credit or loans.

Limitations of Double Entry System:

1. The system does not disclose all the errors committed in the books accounts.
2. The trial balance prepared under this system does not disclose certain types of errors.
3. It is costly as it involves maintenance of numbers of books of accounts.

ACCOUNTING TERMINOLOGIES

1. **Transactions:** Any sale or purchase of goods or services is called the transaction. Transactions are two types.
   a) **Cash transaction**: cash transaction is one where cash receipt or payment is involved in the exchange.
   b) **Credit transaction:** Credit transaction will not have cash, either received or paid, for something given or received respectively.

2. **Goods:** Those things which a firm purchase for resale are called goods.
   a) **Purchases:** It means purchase of goods, unless it is stated otherwise it also represents the goods purchased.
   b) **Sales:** It means sale of goods, unless it is stated otherwise it also represents these goods sold.

3. **Expenses:** Payments for the purchase of goods as services are known as expenses.
   a) **Revenue Expenditure:** It refers to expenses incurred for running the business. Ex: wages, salaries, rent, etc.
   b) **Capital Expenditure:** It refers to expenses incurred to acquire fixed assets.

4. **Revenue:** It is the amount realized or receivable from the sale of goods or services.
   a) **Revenue Receipts:** It refers to those receipts from customers for goods supplied or fees received. Ex: rent, commission, discount received, etc.
   b) **Capital Receipts:** It refers to receipts from sale of fixed assets.

5. **Assets:** The valuable things owned by the business are known as assets. These are the properties owned by the business. It is of two types:
   a) **Fixed Assets:** It is of two types:
      i. **Tangible Assets:** The assets which can be seen, touch or felt and which are fixed and permanent in nature. Ex: land, buildings, machinery, furniture, etc.
      ii. **In-tangible Assets:** The assets which cannot be felt or touched. Ex: goodwill, patents, copyrights, etc.
   b) **Current Assets:** These are expected to be realized in cash or consumed during business operations. Ex: debtors, stock, bills receivable, etc.

6. **Liabilities:** Liabilities are the obligations or debts payable by the enterprise in future in the term of money or goods. It refers to what the firm owes to outsiders. Liabilities are categorized as capital & reserves, long term debts, and current liabilities.

7. **Debtors:** A debtor is a person who owes money to the business.

8. **Creditors:** A creditor is a person to whom something is owned by the business.

9. **Drawings:** Cash or goods withdrawn by the proprietor from the business for his personal or household is termed to as drawing.

10. **Capital:** The amount invested by the owners or investors in the business is called capital.

11. **Reserve:** An amount set aside out of profits or other surplus to meet contingencies.

12. **Discount:** There are two types of discounts:
    a) **Cash discount:** An allowable made to encourage frame payment or before the expiration of the period allowed for credit.
    b) **Trade discount:** A deduction from the gross or catalogue price allowed to traders who buys them for resale.

BASIS OF ACCOUNTING

Under double entry system books of accounts can be maintained by either cash basis or accrual basis.

Cash System of Accounting

Under cash system of accounting entries are made only when cash is received or paid. No entry is made when amount is due for receipts or payments. Income is received is accounted irrespective of period for which relates. Similarly, expenses are restricted to the actual payments made in cash, during the current period is immaterial whether the payments have been made for previous year or subsequent year. The financial statement prepares under this system do not present a true and fair view of Income, operating results of enterprise. In cash system financial statements are prepared on the basis of Receipts and payments accounts. However, it is suitable in following cases:

- For very small business organisation.
- For individual to record his own transactions.
- For professionals like Doctors, Lawyers, Chartered Accountant, etc.

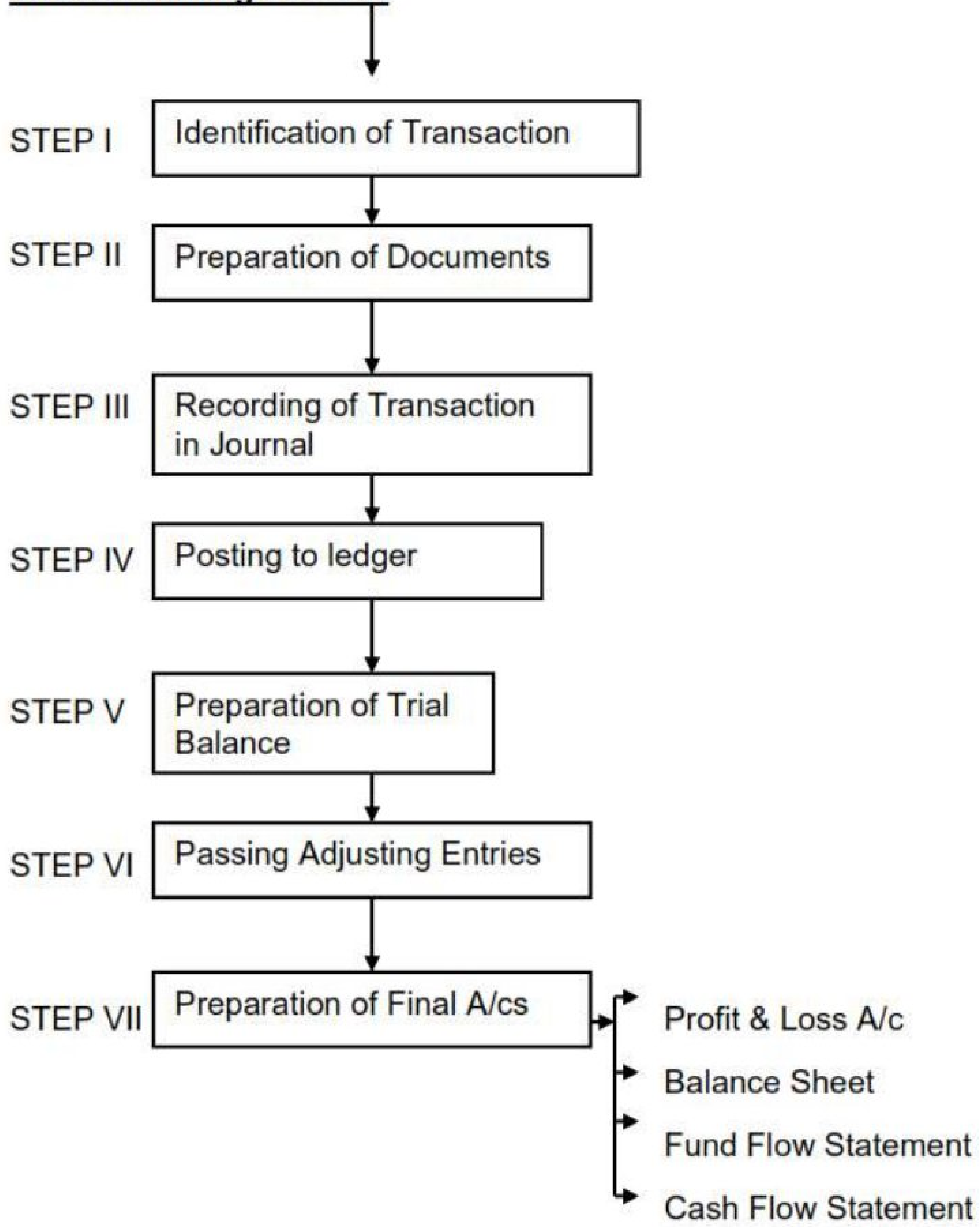
Accrual System of Accounting

This is also known as mercantile system of accounts. Under this system business transactions are recorded as and when it takes place irrespective of amount / cash received or paid. Income earned as well as expenses incurred are recorded related to the particular period. The following are the essential features of accrual basis.

- Revenue is recognized on it is earned irrespective of whether cash is received or not.
- Costs are matched against revenues on the basis of relevant time period to determined periodic income.
- Costs which are not charged to income are carried forward.
- Any cost that lost its utility is written off as a loss.

ACCOUNTING PROCESS

The Accounting Process

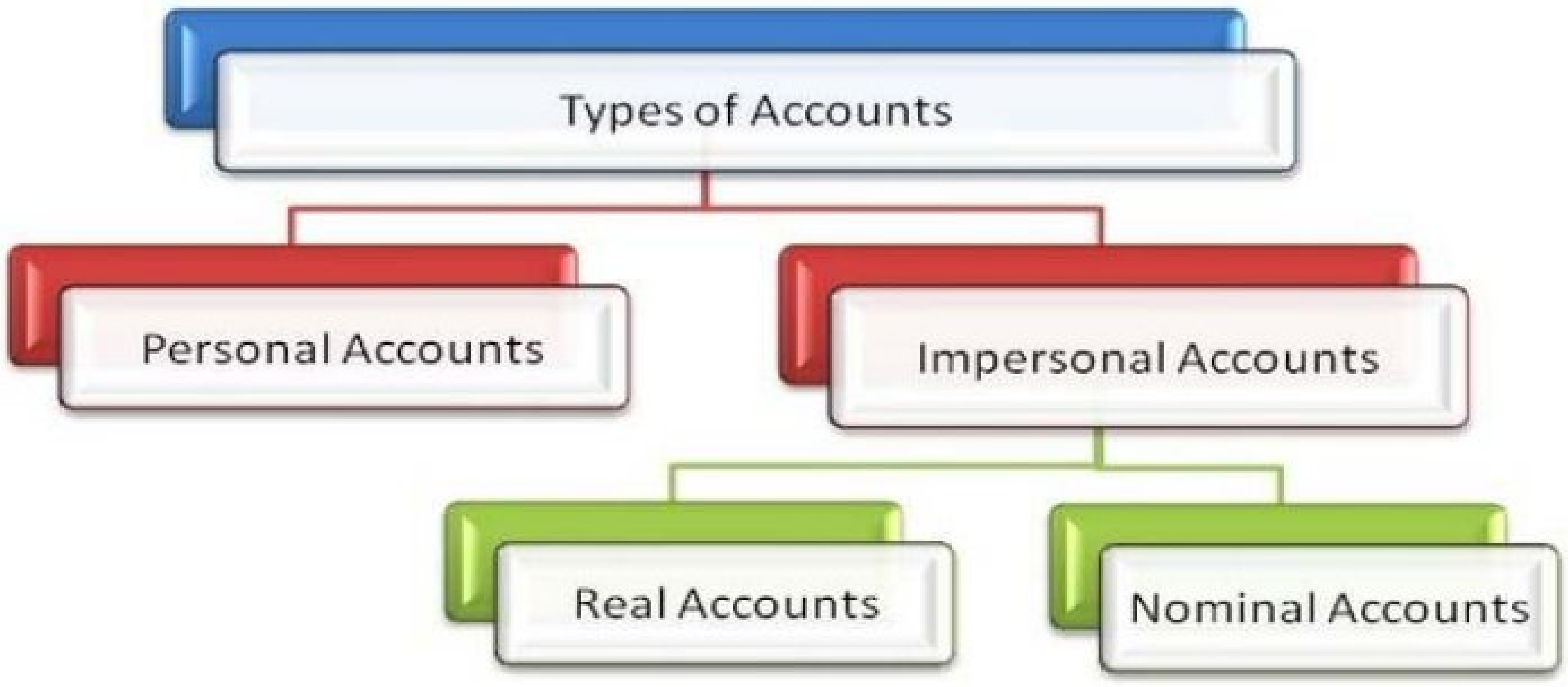


TYPES OF ACCOUNTS AND RULES

An account is defined as a summarized record of transactions related to a person or a thing e.g. when the business deals with customers and suppliers, each of the customers and supplier will be a separate account. The account is also related to things – both tangible and intangible. e.g. land, building, equipment, brand value, trademarks etc. are some of the things. When a business transaction happens, one has to identify the 'account' that will be affected by it and then apply the rules to decide the accounting treatment. An account is capable of receiving and giving values. When an account receives a value / benefit. It is debited and when it gives a value / benefit it is credited. In order to keep full record of all the transactions the business has to keep:

- ✓ An account of each head of expenses or income earned by the business and
- ✓ An account of each property which belongs to the business and
- ✓ An account of each party with whom business deals.

The accounts are maintained for recording all business transactions. They are divided in to 3 types:



1. **Personal Accounts:** Accounts which shows transactions related to persons are called Personal Accounts. A separate account is kept on the name of each person for recording the benefits received from or given to the person. The persons could also be artificial persons like companies, bodies corporate or association of persons or partnerships etc.
   Example: Gopal's A/C, SBI A/C, Nagarjuna Finanace Ltd. A/C, Capital A/C Ali and Sons trading A/c, ABC Bank A/c, Infosys Technologies A/c, etc.

   Rule: The account of the person receiving benefit (receiver) is to be debited and the account of the person giving the benefit (given) is to be credited.

   Debit----The Receiver
   Credit---The Giver

2. **Real Accounts:** The accounts relating to properties or assets are known as Real Accounts. Every business need asset such as machinery, furniture, etc. for running its activities. A separate account is maintained for each asset owned by the business.
   - ✓ **Tangible real Accounts:** These are accounts of such things which are tangible i.e. which can be seen touched or felt physically. Ex: Land, Building, Furniture, Cash etc.
   - ✓ **Intangible real Accounts:** These accounts represent such things which cannot be touched, seen or felt physically. Ex: Goodwill, Trademarks, Patent right etc.

   Example: Cash A/C, furniture A/C, building A/C, machinery A/C etc.

   Rule: When an asset is coming into the business is to be debited. When an asset is going out of the business the account is to be credited.

   Debit----What comes in
   Credit---What goes out

3. **Nominal Accounts:** Accounts relating to expenses, losses, incomes and gains are known as Nominal Account". A separate account is maintained for each item of expenses, losses, income or gain.
   Example: Salaries A/C, stationery A/C, wages A/C, postage A/C, rent received A/C, etc.

   Rule: When an expense is incurred or loss encountered, the account is to be debited. When any income is earned or gain made, the account is to be credited.

   Debit----All expenses and losses
   Credit---All incomes and gains

JOURNAL

The first step in accounting is recording of all the transactions in the books of original entry viz., Journal and then posting into ledgers. The word Journal is derived from the Latin word 'journ' which means "a day". Journal is the first book in which transactions are recorded in chronological order (date wise), the moment they take place in the business. It is also called Day Book, Book of original entry, First entry and Prime Entry book. The process of recording a transaction in the journal is called "Journalising". The entries made in the book are called "Journal Entries".

The Performa of Journal:

Journal Entries in the Books of ………

Date	Particulars	L.F. No	Debit (Rs.)	Credit (Rs.)

1. **Date:** To write the date of the transaction.
2. **Particulars:** To write the names of the accounts and its description. Every entry has two aspects i.e. Debit and Credit.
   - ✓ The name of the account to be debited is written on left side followed by "Dr." (indicates Debit).
   - ✓ The name of the account to be credited is written in next line using "To" before the account name.
   - ✓ In next line the description of the transaction is written within brackets, starting with the word "Being".
3. **Ledger Folio (L.F. No.):** To write the page number of the account in ledger.
4. **Debit (Rs.):** To write the amount to be debited.
5. **Credit (Rs.)**: To write the amount to be credited.

Example: Jan-10th Purchased furniture for cash Rs.5,000

Journal Entries in the Books of ABC Co. Ltd.

Date	Particulars	L.F. No	Debit (Rs.)	Credit (Rs.)
Jan-10th	Furniture A/c Dr. To Cash A/c (Being furniture purchased for cash)		5,000	 5,000

Advantages of Journal

The following are the advantages of a journal:

1. **Chronological record:** Journal records transactions as and when it takes place in the business. So, it is possible to get a detailed day-to-day information.
2. **Narration:** It refers to the explanation of the recorded transactions.
3. **Minimising the possibility of errors:** The nature of transaction and its effect on the financial position of the business is determined by recording and analyzing into debit and credit aspect.
4. **Helps to finalise the accounts:** Journal is the basis of ledger posting and the ultimate trial balance. The trial balance helps to prepare the final accounts.

LEDGER

All the transactions in a journal are recorded in a chronological order. After a certain period, if we want to know whether a particular account is showing a debit or credit balance it becomes very difficult. So, the ledger is designed to accommodate the various accounts maintained the trader. It contains the final or permanent record of all the transactions in duly classified form.

"A ledger is a book which contains various accounts." The process of transferring entries from journal to ledger is called "Posting". Posting into ledger is done periodically, may be weekly or fortnightly as per the convenience of the business. The format of ledger A/c is "T" shape. The left-hand side is debit side (Dr.) and right-hand side is credit side (Cr.).

The Performa of a ledger:

Dr. Name of the Account Cr.

Date	Particulars	JF. No	Amount Rs.	Date	Particulars	JF. No	Amount Rs.

1. **Date:** Write here the date of the transaction as noted in Journal.

2. **Particulars:** Every entry on the debit side of this column must begin with the word 'To' and on credit side with the word 'By'.
   a) On the debit side of the account after the word 'To' write "Name of the Credit Part of the Journal entry.
   b) On the credit side of the account, after the word' By' write 'Name of the Debit Part of the Journal entry'.

3. **Journal Folio:** Write the page number of Journal from where the entry is posted.

4. **Amount:** Write here the amounts of the transaction. The amount in the debit column of the Journal is entered on the debit side. The amount in the credit column of the Journal is entered on the credit side.

Balancing an Account:

Accounts are balanced with a view to prepare the final accounts. Take the totals of the two sides of account and enter the higher balance on both the sides. Enter the difference amount and write "To/By balance c/d" against the balance. The balance is brought forward at the beginning of next period written as "To/By balance b/d". If the debit and credit balance are equal it implies nil balance.

SUBSIDARY BOOKS

As Business transactions are numerous and large in size, the Journal may be split up into number of separate Journals to record particular type of transaction. These journals are known as the subsidiary books. Some of the subsidiary books are:

1. Purchase Book
2. Purchase Return / Return Outward Book
3. Sales Book
4. Sales Return / Return Inward Book
5. Bills Receivable Book
6. Bills Payable Book
7. Journal Proper

1. **Purchase Book:** The purchase day book records the transactions related to credit purchase of goods only. It follows that any cash purchase or purchase of things other than goods is not recorded in the purchase day book. Periodically, the totals of Purchase day book are posted to Purchase account in the ledger. The specimen Purchase day book is given below:

Purchases Book

Date	Name of the Supplier	Inward Invoice No.	L.F. No	Amount (Rs.)

2. **Purchase Return / Return Outward Book:** This book contains the transactions relating to goods that are returned by the business to creditors. For example, goods broken in transit, not according to the sample etc. The specimen Purchase returns day book is given below:

Purchase Returns Book

Date	Name of the Supplier	Debit Note No.	L.F. No	Amount (Rs.)

3. **Sales Book:** The sales day book records transaction of credit sale of goods to customers. Sale of other things, even on credit, will not be entered in the sales day book but will be entered in Journal Proper. If goods are sold for cash, it will be entered in cash book. Total of sales day book is periodically posted to sales account in the ledger. The specimen of a sales day book is given below:

Sales Book

Date	Name of the Supplier	Outward Invoice No.	L.F. No	Amount (Rs.)

4. **Sales Returns/Return Inward Book:** The transactions relating to goods which are returned by the customers for various reasons, such as not according to sample, or not up to the mark etc. contain in this book. Generally, when a customer returns good to suppliers, he issues a Debit Note for the value of the goods returned by him. Similarly, the supplier who receives those goods issues a Credit Note. The specimen of a sales returns book is given below:

Sales Returns Book

Date	Name of the Supplier	Credit Note No.	L.F. No	Amount (Rs.)

5. **Bills Receivable Book:** It is such a book where all bills received are recorded and therefrom posted directly to the credit of the respective customer's account. The total amounts of the bills so received during the period (either at the end of the week or month) is to be posted in one sum to the debit of Bills Receivable A/c. The specimen of a Bills receivable book is given below:

Bills Receivables Book

Date	Received From	Term	Due Date	L.F. No.	Amount (Rs.)

6. **Bills Payable Book:** Here all the particulars relating to bills accepted are recorded and therefrom posted directly to the debit of the respective creditor's account. The total amounts of the bills so accepted during the period (either at the end of the week or month) is to be posted in one sum to the credit of Bills Payable Account. The specimen of a Bills payable book is given below:

Bills Payable Book

Date	To Whom Given	Term	Due Date	L.F. No.	Amount (Rs.)

7. **Journal Proper:** Credit transactions that cannot be entered in any other subsidiary book are entered in journal proper. It will cover purchase or sale of assets, expense accruals, rectification entries, adjusting entries, opening entries and closing entries.

Journal Proper

Date	Particulars	L.F. No	Debit (Rs.)	Credit (Rs.)

Advantages of Subsidiary Books

The following are the advantages of having a number of subsidiary books:

1. **Classification of transactions becomes automatic:** As there is a separate book for each type of transactions, the transactions of same nature are automatically brought at one place. For example, all credit purchases of goods are recorded in the Purchases Book.
2. **Reference becomes easy:** If any reference is required, it can be traced easily by referring to the appropriate subsidiary book. You do not have to go through all the transactions recorded in the journal.
3. **Facilitates division of work:** The division of journal into various subsidiary books facilitates division of work among many persons. This, in turn, facilitates prompt recording of transactions and saves a lot of time.
4. **More particulars:** More details about the transactions can be given-in subsidiary books than would be possible in one book.
5. **Responsibility can be fixed:** The work of maintaining a particular book can be entrusted to a particular person. He will be responsible for keeping it up-to-date and in order.
6. **Facilitates checking:** When the Trial Balance does not agree, the location of errors will be relatively easy.

CASH BOOK

In any business there would be numerous cash transactions which involve either receipts or payments of cash. Cash sales, receipt of cash from debtors, cash purchases, payments to creditors, payment of various expenses such as salaries, wages, rent, taxes, etc., are some examples of transactions involving cash. These are recorded in cash book, receipts on one side and payments on the other. Every business unit, small or big, maintains a cash book. It enables the businessman to know and verify the amount of cash in hand from time to time. As a matter of fact, cash book plays a dual role. It is a book of prime entry and also serves the purpose of a Cash Account. It is designed in the form of a ledger account and records cash receipts on the debit side and payments on credit side. It is also balanced in the same way. Hence, when cash book is maintained, there is no need to have a Cash Account in the ledger. There are different types of cash books maintained by the business. They are:

1. Simple or Single Column Cash Book
2. Two or Double Column Cash Book
3. Three or Triple Column Cash Book
4. Petty Cash Book

Simple or Single Column Cash Book: A Single Column Cash Book is nothing but a Cash Account. It is used for recording all cash receipts and cash payments and serves the purpose of Cash Account as well. There is no need to open separate cash account in the ledger. It is called Single Column Cash Book just because it has only one amount column on each side.

Dr. Cash Book Cr.

Date	Particulars	JF. No	Amount Rs.	Date	Particulars	JF. No	Amount Rs.

Two/Double Column Cash Book: The Double Column Cash Book having two amounts. Columns on each side as under:

(a) Cash and discount columns
(b) Cash and bank columns
(c) Bank and discount columns

Dr. Cash Book Cr.

Date	Particulars	JF. No	Amount Rs.	Amount Rs.	Date	Particulars	JF. No	Amount Rs.	Amount Rs.

Triple Column Cash Book: Triple Column Cash Book has three amount columns, one for cash, one for Bank and one for discount, on each side. All cash receipts, deposits into book and discount allowed are recorded on debit side and all cash payments, withdrawals from bank and discount received are recorded on the credit side. In fact, a triple-column cash book serves the purpose of Cash Account and Bank Account both. Thus, there is no need to create these two accounts in the ledger.

Dr. Cash Book Cr.

Date	Particulars	JF. No	Cash	Bank	Discount	Date	Particulars	JF. No	Cash	Bank	Discount

Petty Cash Book: When the petty cash fund is operated as an imprest fund, the recording of the petty expenses paid will be made in the petty cash book. This would also avoid recording too many small value transactions in the main cash book. The petty cash book would contain a number of analytical columns for grouping the various expenses under a few classifications which would facilitate subsequent posting into the General Ledger.
A specimen petty cash book is given below:

Petty Cash Book

Amount Received	Date	Particulars	Total Amount Paid	Expenses	Postage	Stationery	Carriage	Travelling

TRAIL BALANCE

The fundamental principle of double entry book keeping is that debit must be equal to credit. In other words, debit aspect of any transaction is always equal to its credit aspect. All ledger accounts are balances. A debit balance in a general ledger account indicates an excess of debit side over credit side of the account. A credit balance in a ledger account indicates the excess of credit side over debit side of the account.

A trial balance is a summary of all the ledger balances outstanding as on particular date. List of debit balances and credit balances should be equal. It said that Trial balance is tallied. When trial balance tallies are establishes the arithmetical accuracy of record. It is a statement prepared before preparing the final accounts. It is a link between books of account and final accounts i.e. the Trading & Profit & Loss A/c and Balance Sheet.

Trial balances are of two types:

1. **Gross Trial Balance:** Gross Trial Balance is prepared by taking all ledger account debit total and credit total, instead of considering ledger balances, as on a particular date.
2. **Net Trial balance:** Net trial balance is list of debit & credit balance, taken from ledger accounts on particular date. Normally, net trial balance is prepare, since it is transferred to final accounts and personal and real accounts balance are carried forward from current year to subsequent year.

Trail balance of ………………… as on …………

Name of account (Particulars)	Debit Amount (Rs.)	Credit Amount (Rs.)

Preparation of Trial Balance:

1. It may be prepared on a loose sheet of paper.
2. The ledger accounts are balanced at first. They will have either "debit-balance" or "credit balance" or "nil-balance".
3. The accounts having debit-balance is written on the debit column and those having credit-balance are written on the credit column.
4. The sum total of both the balances must be equal, for "Every debit has its corresponding and equal credit".

Features of a Trial Balance:

1. It is a list of debit and credit balances which are extracted from various ledger accounts.
2. It is a statement of debit and credit balances.
3. The purpose is to establish arithmetical accuracy of the transactions recorded in the books of accounts.
4. It does not prove arithmetical accuracy which can be determined by audit.
5. It is not an account. It is only a statement of account.
6. It is not a part of the final statements.
7. It is usually prepared at the end of the accounting year but it can also be prepared anytime as and when required like weekly, monthly, quarterly or half-yearly. It is a link between books of accounts and the Profit and Loss Account and Balance sheet.

Purpose of a Trial Balance:

1. To check the arithmetical accuracy of the recorded transactions.
2. To ascertain the balance of any ledger Account.
3. To serve as an evidence of fact that the double entry has been completed in respect of every transaction.
4. To facilitate the preparation of final accounts promptly.

ILLUSTRATIONS

1. Journalize the following transactions in the books of ABC Ltd. Company.
   May 1st Paid salaries Rs. 5000
   May 4th Sold goods to Venkat Rs. 10000
   May 10th Sold machinery Rs. 30000
   May 13th Commission received Rs. 2000
   May 18th Allowed discount Rs. 1000
   May 22nd Brought goods from Raghava Rs. 4000
   May 31st Sold goods to Abhi for cash Rs. 6000

Solution:

Journal Entries in the books of ABC Ltd. Company

Date	Particulars	L.F. No	Debit (Rs.)	Credit (Rs.)
May 1st	Salaries A/c Dr. To Cash A/c (Being Paid salaries)		5000	5000
May 4th	Venkat A/c Dr. To Sales A/c (Being Sold goods to Venkat)		10000	10000
May 10th	Cash A/c Dr. To Machinery A/c (Being machinery sold)		30000	30000
May 13th	Cash A/c Dr. To Commission A/c (Being Commission received)		2000	2000
May 18th	Discount A/c Dr. To Cash A/c (Being discount allowed)		1000	1000
May 22nd	Purchase A/c Dr. To Raghava A/c (Being brought goods from Raghava)		4000	4000
May 31st	Cash A/c Dr. To Sales A/c (Being Sold goods to Abhi for cash)		6000	6000