ABOUT THE BOOK

This book is written in simple language making understanding easy. The questions are compiled to cover-up all problems of the concerned topics in shape of notes and intends to work as a text –book. It will help students to understand the basic concepts involved, learn & implement techniques, manage time factor with a view to learn it in the entrance examination The authors has put hard work to compile the materials relevant to the problems which students face. The book is an excellent guide for post SLC students.

Any suggestion regarding for the improvement of this book will be appreciated.

First Edition: 2003
Eighth Edition: 2014
Price: Rs. 90.00

Published By:
Cambridge Institute
GPO Box: 21159

Complied By
Keshav Pandit

Syllabus

1. Introduction
    - Concept of book keeping
    - Concept of accounting
    - Functions or importance of accounting
2. Concept of accounting terms.
3. Concept of revenue and expenditure.
    - Concept
    - Illustration
    - Problem
4. Book keeping system
    - Meaning
    - Advantages.
5. journal
    - Concept
    - Rules of journal entry
    - Illustration
    - Problem
6. Subsidiary book or books of primary entry.
    - Concept
    - Types
7. Double entry book keeping system: credit transactions.
    - Meaning
    - Cash discount
    - Trade discount.
    - Illustration
    - Problem
8. ledger
    - Meaning of Ledger
    - Rules of ledger
    - Illustration
    - problem

9. Trial balance
    - Concept
    - Rules
    - Illustration
    - Problem
10. Trading account and Profit and Loss account.
    - Concept
    - Format
    - Problem
11. Balance sheet.
    - Concept
    - Format
    - problem
12. Depreciation.
    - Concept
    - Types
    - Treatment
    - Illustration
    - Problem
13. Concept or Principles of accounting.
14. Business
15. Accruals and payments
16. Bad and doubtful debts
17. Multiple choice questions.

CHAPTER -1

Concept and Meaning of Book Keeping

Book keeping is the summation of two words: Book and keeping: In accountancy, Book means book of accounts in which business transactions are recorded. Keeping means recording of business transactions in a proper manner in the book of accounts.

Book keeping is the process of recording the financial transactions of a business in the book of accounts. These transactions are recorded in a systematic manner so that information related to the transactions can be obtained in the shortest period.

Objective or function of book keeping

1) **To identify the transactions:** It is well known that various financial and non-financial activities performed during the course of business operations. Book keeping identifies the transactions of financial character from amongst various transactions and keeps their records systematically.
2) **To measure the identified transaction:** Book keeping measures all identified financial transactions in the terms of money.
3) **To record the measured transactions:** Book keeping records the identified financial transaction in the books of primary entry systematically as and when they occur.
4) **To classify the recorded transaction:** Book keeping not only records all the identified transactions but it also classified them into personal, real and nominal accounts as per their nature.
5) **To have permanent records:** Other main objective of book keeping is to keep a permanent record of all the transactions of a business for future reference.

Concept or meaning of Accounting

Generally, it is said book keeping is the first stage of accounting. It means the term 'Accounting ' has broader meaning as compared to the term 'Book keeping '. Book keeping is mainly concerned with systematic and scientific recording of business transactions and their classification. But the term 'Accounting' goes beyond this and further it includes summarization, analysis and interpretation of the transactions recorded under book keeping. It

is the process of identifying, measuring, recording, classifying, analyzing, interpreting the financial transaction and communicating the results thereof to the persons interested in such information's.

Objective or functions of accounting

1) **Complete systematic record of all business transaction:** The first function of accounting is to keep systematic and complete record of all financial transactions for future reference.
2) **Determination of operating results:** The second objective of accounting is to ascertain operating result, is profit or loss of a business for the period.
3) **Ascertainment of financial position:** A business should know its true financial position. For this purpose, it prepares a balance sheet.
4) **Determination of tax liability:** Business has to pay different types of tax to the government. Accounting provides financial information to the tax authorities to determine tax liability.
5) **Information to the concerned parties:** Accounting provides information to the concerned parties about financial transaction. They are owners, managers, creditors and banks etc.

CHAPTER- 2

Accounting terms

Capital

The amount of money invested by an owner in the beginning or during the life of the business is known as capital. The owner may invest cash or stock or any other own properties to establish and operate the business.

Liabilities

The amount of money payable by the business to outsiders on a specific point of time is known as liabilities. These are the financial obligations of business. The liabilities are classified into two types:

1) **Long term liabilities:** The amount of money payable by the business to the outsiders normally after a period of one year is called long term liabilities. For example, debenture, mortgage loans, long term loans, loan taken from bank and financial institution etc.
2) **Short term liabilities:** The amount of money payable by the business to the outsiders normally within a period of one year is called short term liabilities. For examples, bills payable , creditors, bank overdraft, outstanding expenses, advance income etc.

Assets

The office resources which are used by the business for the purpose of generating revenue are called assets. Such assets are classified into two types:

1) **Fixed assets:** The assets which are purchased for generating income for a long period of time are called fixed assets. For example, land and building, plant and machinery, vehicle etc.
2) **Current assets:** The assets which can be used or converted into cash within a period of one year is known as current assets. For example, cash at bank, cash in hand, debtors, closing stock etc.

Closing stock

The materials or goods which remain unsold at the end of accounting year are known as closing stock. It may stock of raw material, work in progress and finished goods.

Debtors

Debtors are the customers. The amount receivable from the customers against the goods sold on credit is called debtors.

Creditors:

Creditors are the suppliers of goods. The amount payable to the suppliers against the goods purchased on credit is called creditors.

Outstanding expenses

Expenses incurred but not yet paid are called outstanding expenses.

Expenses

The amount which is paid for goods or services are called expenses. For examples, Salary, rent, commission, wages, purchases etc.

Income

The amount which is earned by selling goods or providing services are known as income. For example, rent received, commission received, discount received etc.

Bank overdraft

If the bank gives permission to withdraw more amounts of cash up to certain limit than the bank balance, it is called bank overdraft. For example, if the businessman has a bank balance amounting to 50000 and the bank has given permission to withdraw 60000, the excess amount of withdrawal 10000 is considered as bank overdraft.

Advance incomes

The incomes, which are not earned but received in advance, are called advance incomes. Advance incomes are current liabilities.

Prepaid expenses

Expenses paid in advance are called prepaid expenses. Prepaid expenses are current assets of the business.

Accrued incomes:

Incomes earned but not yet received are called accrued incomes. Accrued incomes are current assets of the business.

Interest:

Interest is an extra amount paid to a money lender against the use of his money for a given period. It is expenses of business.

Financial transactions

Financial transactions refer to those business dealings which are related to money or equivalent to money.

Profit the excess amount of incomes over expenditures is known as profit.

Loss:

The excess amount of expenditures over incomes is known as loss.

Exercise -1

1) Copy and complete this table, ticking the boxes which correctly describe the given accounts in the books for a bakery:

Account	Fixed assets	Current assets	Revenue or income	expenses
Rent				
Salary				
Commission				
Wages				
Commission received				
Advertising				
Purchases				
Plant and machinery				
Vehicle				
Computer				
Rent received				
Dividend received				
Discount allowed				
Discount received				
Debtors				
Creditors				
Expenses due				
Income due				
Prepaid expenses				

CHAPTER-3

Capital Expenditure and Revenue Expenditure Concept

Capital expenditure

Expenditure for the purchase or expansion of fixed assets, the benefit of which is not fully consumed in one period but spread over several period is called capital expenditure. It includes the purchase of assets for use in a business not for resale. It is non-repetitive kinds of expenditure. It is used for generating revenue. For example, purchase of fixed assets.

Revenue expenditure

The expenditure, which is incurred for performing day to day activities of a business on regular basis, is called revenue expenditure. It is recurring in nature. It includes purchasing assets for resale at a profits, maintaining assets in good working order, cost of fixed assets like rent, rates, taxes etc. For example, Salary, rent, repair etc.

Exercise -1

1) Copy and complete this table, ticking the boxes which correctly describe the given accounts in the books for a bakery:

Account	**Capital expenditure**	**Revenue expenditure**
Purchased furniture		
Repair of machinery		
Installlation of machine		
Salary		
Rent		
Construction of building		
Vehicle purchasd		
Replacement cost		

Purchase of computer		
Purchase of printer		
Insurance of building		
Rent of machince		
Insurance of machince		
Advertisement		
Tax		
Factory rent		
Wages		
Stationery		
Postage and telegram		
Purchase of stock		
Fixture and fitting		
Part exchange		
Purchase of patent right		
Sample distribution		

CHAPTER-4

Book Keeping System

There are two system of book keeping.

1) **Single entry system:** it is an old system. Under this system, only an account or effect of each transaction relating to a supplier or a customer or cash is recorded.it ignores two aspect of a transaction, i.e. debit & credit.
2) **Double entry system:** it is modern and scientific system of recording the financial transaction.it is propounded by Luca D Pacioli in 1494. This system recognizes that every financial transaction has two aspects. Both of these aspects, i.e. one is debit and another is credit must be recorded in the system of book keeping. The rule of double entry system is that there are two parties in every transaction, one is giver and another is receiver.

Feature of double entry system

1) **Double effect:** it follows the principle of double aspect by debiting and crediting the transaction. Every transaction must have two equal effect debit and credit.
2) **Equal effects:** it assumes that debit must be equal to credit amount i.e. it considers the effect of equal amount on both sides of accounts.
3) **Debit and credit:** it has two sides I.e. debit and credit.
4) **Classification of accounts:** it maintains the records of transactions classifying them into personal, real and nominal accounts.
5) **Arithmetical accuracy:** another feature of bauble entry system of book keeping is to be check arithmetical accuracy of records of financial transactions by preparing tray balance.

Importance or advantage of double entry book keeping system

1) **Complete records of each transaction:** double entry system of accounting presents a complete record of transaction. It records all the aspects of every transaction.

2) **Checking of arithmetical accuracy:** under the double entry system every transaction has the equal effects on two parties and such effects will be shown on debit and credit side of accounts. The arithmetical accuracy of the records cane checked by preparing trial balance.

3) **Profit and loss accounts:** under the double entry system, profit and loss account can be easily be prepared. It helps to find out profit and loss.

4) **Scientific and systematic:** Double entry system of book keeping is scientific and systematic records of financial transaction.

5) **Prevention of frauds and errors:** It prevents frauds and errors and makes possible their detection easier as soon as possible.

CHAPTER-5

Journal Entry

The books of accounts in which business transactions are recorded for the first time is called 'books of Original Entry' Journal is one of them. Journal is derived from the French word 'which means a day'. Journal is a daily record of business transactions. It is the 'day by day' book of the business wherein both the aspects of business transactions are recorded in the chronological order i.e. Date wise. Journal is a book of Original Entry because transaction is first written in the journal. It is also known as a Book of Prime Entry. These entries are them posted into the ledger. The act of recording the dual aspects of each transaction i.e. debit and credit into the journal is known as journalizing.

Advantage of Journal

Followings are the advantages of Journal

1) It provides systematic and date wise records of all business transaction.

2) It ensures the application of double entry book keeping system in recording the transaction.

3) It avails the records with details of accounts debited and credited and amount of transactions.

4) It simplifies the preparation of ledgers.

5) It can be reliable evidence in eyes of law.

Rule for debit and credit

There are two alternative rule of journalizing. They are as follows:

1) On the basis of types of account

2) On the basis of accounting equation

1) On the basis of types of account

Under double entry system, accounts are classified into three types.

a. **Personal account:** It is the account of a person or organization or debtor or creditor. It is the record of an individual or organization.

According to personal account, the rule of debit and credit is as follows:

i. Debit the receiver
ii. Credit the giver

b. **Real account:** It is an impersonal account. It is the account of a real thing or property. It is the record of an asset of the business. According to real account, the rule of debit and credit is as follows:

i. Debit what comes in
ii. Credit what goes out

c. **Nominal account:** It is another impersonal account. It is the account of expenses, loss, income and profit. It has no any physical shape. It does not exist in the business in real form. It appears only in the books. According to nominal account, the rule of debit and credit is as follows:

i. Debit all expenses and losses
ii. Credit all incomes and profit

2) On the basis of accounting equation.

Assets = Liabilities + Capital
Increases in assets and expenses are debited.
Decrease in assets and expenses are credited.
Decrease in capital, liabilities and incomes are debited.
Increase in capital, liabilities and incomes are credited.

Illustration.

- Purchased furniture of $ 20000 by cheque.

Journal

	$	$
Furniture A/C Dr	20000	
Bank A/C Cr		20000

(Being furniture purchased through cheque)

Exercise -1

	Debit account	Credit account
Neol paid a cheque into his business bank account as capital	Bank	Capital
Purchase some stock and pays by cheque		
Sells some stockand banks the taking		
Paid rent by cheque		
Furniture purchsased and pays by cheque		
Cashes cheque for personal uses		
Pays wages by cheque		
Return stock to supplier and banks refund		
Receives rent from tenant and banks cheque		
Refunds money to customers by cheque for goods returned		
Motor vehicle purchased and paid by cheque		

Exercise -2

1) Journalese the following

a. June 1, Forsook commenced business by paying $15000 into his business bank account.

i. Amna lent the business $5000.
ii. Farook then haed the following business transaction:

b. June 2, Purchased premises and paid $8000.
c. June 3, Bought office furniture for $2000 and paid by cheque.
d. June 4, Paid $5000 by cheque for goods for re-sale.
e. June 5, Sold some goods for $1500 and banked the proceeds.
f. June 6, Paid insurance premium by cheque, $600.

g. June 7, Bought motor van and paid $3000 by cheque.
h. June 8, Drew cheque for $50 to pay for petrol for motor van.
i. June 9, Bought some goods costing $2000 for re-sale and paid by cheque.
j. June 10, Sold goods for $2400 and banked the proceeds.
k. June11, Repaid $1200 by cheque to customers for goods returned.
l. June 12, Received a refund of $900 from suppliers for goods returned.
m. June 13, Received a refund of insurance of $100.

Exercise-3

1) Journal the following

a. Started busines by $90000.
b. Purchase office furniture from Julee $4000.
c. Sold goods to Natase for $30000
d. Paid to Mukesh $10000.
e. Goods taken for personal use $3000
f. Paid telephone bill $4000
g. Rent due but not paid $4000.
h. Paid insurane in advance $3000
i. A furniture costing $1500 sold for $1000.
j. A machine costing $2000 sold for $2500.
k. $ 2000 due from Natase became due to his insolvency.

CHAPTER 6

Subsidiary Book or Primary Entry

In the business where the size of transaction is small, financial statements can be prepared and other relevant information can be obtained with the help of journal and ledger. But if the size of transactions are numerous and number of ledgers to be maintained are very large, it becomes very difficult to the company to prepare journal of each transaction and post them into separate ledgers. Also, Journal compiles all types of transactions in a single sheet of paper which may create inconvenience to find out the amount of debit and credit on a particular account.

To overcome the problems of journalizing a new practical accounting system evolved under which transaction of common nature are recorded in related books (called subsidiary book). The subsidiary books, also called as sub journals, are prepared to record the transactions of similar nature and avoid the needs of journal entries. A separate subsidiary book is prepared for the transaction, which is of particular class and recurring in nature.

Importance of subsidiary book

Following are the advantages of subsidiary book

a. Division of labor
b. Promptness in work
c. Increases in efficiency
d. Saving in time
e. Reduction in errors.

Types of subsidiary book

1) **Purchase book or purchase journal:** Purchase book may be defined as the subsidiary book which is a prepared to record the goods purchased on credit for selling. Purchase book shows the information of supplier, quantity and price of goods purchased, availability of discount and other terms and condition etc. It is also known as' purchase journal'.

2) **Sales book or sales journal:** Sales book may be defined as the subsidiary book which is prepared to record the goods sold on credit.

Sales book shows information about customers, quantity and price, discount allowed and other terms and conditions etc.

3) **Purchase return book or return outward book:** Purchase return book is prepared to record all the goods returned to the suppliers. It gives information about the price and quantity of goods returned to the suppliers and particular causes.

4) **Sales return book or return inward book:** Sales return book is prepared to record all the goods returned from the customers. It gives information about the price and quantity of goods returned from the customers.

5) **Cash book:** The book in which all cash transactions are recorded is known as cash book. There are three types of cash book

a. Single column cash book

b. Double column cash book

   i. With cash and bank

   ii. With cash and discount

   iii. With bank and discount

c. Triple column cash book

CHAPTER -7

Double Entry Bookkeeping: Credit Transactions

Many transactions take place without any money being paid or received at the certain time. For example, Lai sells goods to Chin for $500 on 31 May and gives Chin until 30 June to pay. The transaction is 'on credit'. The sale has taken place on 31 May and must be recorded in the books fo both Lai and Chin at that date. No entry to record payment is made in their books until Chin pays Lai.

In the seller's books: A sale on credit is credited to sales account and debited to an account opened for the customer. When the customer pays his or her account is credited and the Bank account debited.

In a customer's books: A purchase on credit is debited purchases account and credited to an account opened for the supplier. When the supplier is paid , his or her account is debited, and the bank account credited.

Trade discount: Trade discount is an allowance made by one trader to another at the time of purchase. It is never recorded in ledger accounts.

Cash discount (or settlement) discount: Lai has given Chin one month to pay for the goods. To encourage Chin to pay by 30 June, Lai may allow Chin to pay less than the amount due. This allowance is a cash discount.

Exercise: 1

a. May 1, Purchased goods from Debit. The goods cost $1000 less 10% trade discount.

b. May 2, Purchased goods from Rodeny for $1600 less trade discount 15%.

c. May 3, sold goods to View for $20000 less trade discount 10% and cash discout 5%.

d. May 5, sold goods to Uriah for $10000 less trade discount 5%.

e. May 10, Cash paid to Jony $ 9000 after deducting $1000 discount.

CHAPTER-8

Ledger

The ledger is second step of accounting. It is the principle book of accounts. It contains all the accounts appeared in the journal books. It classified record of all the transaction in summarized form. It is the final destination of all the account created in the primary books. It is the final source of all accounting information.

Ledger account

A ledger account simply an account is a statement of information on a particular head. It is the summary records of all the transactions relating to a particular person or property or income or expense. The ledger account contains two sides which are debit and credit. Its left hand side is called debit side and right hand side is called credit side.

Procedures of preparing ledger account.

The process of transferring the account from journal to ledger is called posting. While posting the account from journal to ledger, the rules of journalizing should be followed. Account debited in journal should also be debited in ledger and account credited in journal should also be credited in ledger.

Exercise -1

1) Posting in ledger accounts from following transaction.

a. June 1, Farook commenced business by paying $15000 into his business bank account.

i. Amna lent the business $5000.

ii. Farook then haed the following business transaction:

b. June 2, Purchased premises and paid $8000.

c. June 3, Bought office furniture for $2000 and paid by cheque.

d. June 4, Paid $5000 by cheque for goods for re-sale.

e. June 5, Sold some goods for $1500 and banked the proceeds.

f. June 6, Paid insurance premium by cheque, $600.

g. June 7, Bought motor van and paid $3000 by cheque.

h. June 8, Drew cheque for $50 to pay for petrol for motor van.

i. June 9, Bought some goods costing $2000 for re-sale and paid by cheque.

j. June 10, Sold goods for $2400 and banked the proceeds.

k. June11, Repaid $1200 by cheque to customers for goods returned.

l. June 12, Received a refund of $900 from suppliers for goods returned.

m. June 13, Received a refund of insurance of $100.

CHAPTER-9

Trial balance

A trial balance is a list of all the balances extracted from the ledgers at a particular date. And its purpose is to check that the total of the debit balances equals the total of the credit balances. The principle of double entry ensures that the two sides total should agree. If the totals do not agree there must be an error somewhere in the bookkeeping.

Importance of the Trial balance

Followings are the importance of the Trial balance

1) It helps to check the arithmetical accuracy of accounting.
2) It helps to locate the errors and to rectify them.
3) It helps to prepare financial statement for profitability and financial position.

Rules of trial balance

Debit – the expenses, losses and assets.
Credit- the incomes, profit , capital and liabilities.

Example

1) The following trial balance has been extracted from the books of Zabine at 31 March 2003.

Account	**debit ($)**	**credit($)**
Premises	70000	
Machinery		10000
Office furniture		5000
Sales		100000
Sales returns		700
Purchases		6900
Purchases returns		1000
Trade debtors	1100	
Trade creditor		1575
Rent payable	1600	
Wages and salary		4080

Heating and lighting	960	
Sundry expenses	1430	
Cash	500	
Bank	12600	
Loan		2000
Capital		13000
Drawings	2705	
	117575	117575

Exercise-1

1) Prepare a trial balance from the following balances that have been extracted from the books of Sine Ltd at 31st Dec.

Account	**$**
Premises	50000
Motor Vans	8000
Office furniture	2000
Computer	3000
Sales	60000
Sales returns	700
Purchases	4000
Purchase return	500
Motor Vehicle running expenses	4200
Wages	1800
Rent	2000
Bank	1650
Capital	20000
Drawing	3150

2) The following balances at 31 December 2003 have been extracted from Hassan's books.

Accounts	**$**
Sales	160000
Sales returns	2600
Purchases	84000
Purchase returns	3400

Wages	26000
Heating and lighting	3160
Rent payable	5000
Rent receivable	1000
Postage and telephone	2900
Discount allowed	6100
Advertising	2740
Discount received	5900
Plant and Machinery	50000
Delivery Van	9000
Bank	2300
Trade debtors	7400
Trade Creditor	3700
Drawing	8800
Capital	?

Required : Prepare a trial balance at 31 December 2003 from the balances extracted from Hassan's books and calculate the balance on his capital account.

CHAPTER-10

Trading and Profit and Loss Account

Income Statement

Most people carry on business in order to make a living. They depend upon the profit of the business. They compare the revenue earned by the business with its expenses. If the revenue exceeds expenses the business has made a profit. On the other hand, if the expenses exceed the revenue the business has made a loss and the trader has no income. Profit or loss is found by the preparation of a Trading and Profit and Loss account covering a period of time

Importance of Trading and profit &loss account

1) It helps to find out gross profit and net profit of business.
2) It helps to find out total expenses of business.
3) It helps to find out total income of business.
4) It helps to find out the performance of business.

FORMAT OF TRADING AND PROFIT AND LOSS ACCOUNT FOR A LEVEL

Trading and Profit and Loss account for the year ended ……………..

	$	$
Sales		xx
Sales return		(xx)
		xx
Less, Cost of sales		
Opening stock	xx	
Purchase	xx	
Purchase returns	(xx)	
Carriage inward	xx	
Closing stock	(xx)	xx
Gross profit	**xx**	
Add, other income		
Discount received		xx
Rent received		xx
		xx

Less, overhead

Wages	xx
Rent	xx
Heating and lighting	xx
Postage and telegram	xx
Motor van expenses	xx
Discount allowed	xx
Carriage outward	xx
Loan interest	xx
Salary	xx
Sundry expenses	xx
Net profit	**xx**

Format of Trading and Profit and Loss account for 10+2

Trading account of ………………….

For the year ended………..

Dr Cr

Particular	Amount	Particular	Amount
To opening	Xx	By closing stock	Xx
stock		By sales	
To purchase	Xx	xx	Xx
xx	Xx	Less sales return	
Less, purchase	Xx	xx	
return xx	Xx	By gross loss	Xx
To wages	Xx	transferred to P/L	
To carriage	Xx	account	
inward	Xx		
To octroi			
To fuel and	Xx		
power			
To factory rent			
To factory	Xx		
insurance			
To other factory			
expenses			
To gross profit			
transferred to			
P/L account			
	Xx		Xx

Profit and Loss a/c of ………………………..

For the year ended ……………………………………

Particular	Amount	Particular	Amount
To gross loss		By gross profit	
transferred from		transferred from	
trading account	Xx	trading account	Xx
To salaries	Xx	By other income	Xx
To rent	Xx	By discount	Xx
To insurance	Xx	received	Xx
To depreciation	Xx	By commission	
To electricity	Xx	received	Xx
charges	Xx	By profit on sale	Xx
To commission	Xx	of fixed asset	
To manager's	Xx	By net loss	
salary			
To other office			
expenses	Xx		
To other selling	Xx		
and distribution			
expenses			
To net profit			
	Xx		Xx

Exercise

1) Andrew began trading on 1 January 2011. The following trial balance as at 31 December 2011 has been extracted from her books.

Account	$	$
Sales		200000
Sales return	6300	
Purchases	86500	
Purchases return		5790
Rent received	3000	
Discount received	3210	
Discount allowed	5110	
Wages	61050	
Rent paid	12000	
Electricity	5416	
Insurance	2290	
Motor van expenses	11400	

Sundry expenses	3760	
Loan interest	1000	
Land and building	84000	
Plant nad machinery	22000	
Motor van	19000	
Trade debtors	12425	
Trade creditors		4220
Bank	5065	
Loan	20000	
Drawing	25904	
Capital		127000

Adrew had unsold stock of $10000 at 31 December 2011

Required: Prepare Andrew's Trading and Profit and Loss account for the year ended 31 December 2011.

2) Serina's trial balance at 31 March 2011 was as follows.

Account	$	$
Sales		40000
Stock	5000	
Purchases	20500	
Wages	6000	
Rent	10000	
Electricity	2600	
Carriage inward	1320	
Carriage outward	1080	
Sundry expense	1250	
Plant and Machinery	8000	
Office equipment	1000	
Trade debtor	1900	
Trade creditor		800
Bank	820	
Drawing	6330	
Capital		25000

Stock at 31 March 2012 was $3000.

Required: Prepare Serina's Trading and Profit and Loss account for the year ended 31 March 2004.

CHAPTER-11

Balance Sheet (Statement of financial position)

A balance sheet is a list of the assets and liabilities & capital of a business at a particular date. It is prepared to find out financial position of business. It is part of final account. It is not an account. It is not part of double entry model. It is based on this equation.

Assets = capital +liabilities

Importance of balance sheet

It helps to find out financial position of business.

It helps to find out total assets of business.

It helps to find out total liabilities of business.

Format of balance sheet for A level

	$	$
Noncurrent assets		
Plant and machinery		xx
Land and building		xx
Vehicle		xx
Furniture		xx
		Xx
Current assets		
Closing stock	xx	
Trade debtors	xx	
Prepare expenses	xx	
Income due	xx	
Bank balance	xx	
	Xx	
Current liabilities		
Trade creditors	(xx)	
Expenses due	(xx)	
Advance income	(xx)	
Bank overdraft	(xx)	xx
		Xx

Less, long term liabilities

Loan	xx
	Xx
Financed by	
Capital	xx
Net profit	xx
Net loss	(xx)
Drawing	(xx)

Format of balance sheet for 10+2

Balance sheet of ……………………………….

as at ………………………………………..

Capital and liabilities	Amount	Assets	Amount
Bill payable	Xx	Cash in hand	Xx
Trade creditor	Xx	Cash at bank	Xx
Outstanding	Xx	Bills receivable	Xx
expenses	Xx	Trade debtors	Xx
Advance income	Xx	Stock	Xx
Reserve		Furniture	Xx
Capital		Plant and	Xx
xx		machinery	Xx
Add net profit	Xx	Land and	
xx		building	
Less net loss			
xx			
Less drawing			
xx			
	Xx		Xx

Xx

Exercise

1) Andrew began trading on 1 January 2011. The following trial balance as at 31 December 2011 has been extracted from her books.

Account	$	$
Sales		200000
Sales return	6300	
Purchases	86500	
Purchases return		5790
Rent received		3000
Discount received		3210
Discount allowed	5110	
Wage	61050	
Rent paid	12000	
Electricity	5416	
Insurance	2290	
Motor van expenses	11400	
Sundry expenses	3760	
Loan interest	1000	
Land and building	84000	
Plant and machinery	22000	
Motor van	19000	
Trade debtors	12425	
Trade creditors		4220
Bank	5065	
Loan		20000
Drawing	25904	
Capital		127000

Adrew had unsold stock of $10000 at 31 December 2011

Required: Prepare Balance sheet

2) Serina’s trial balance at 31 March 2011 was as follows.

Account	$	$
Sales		40000
Stock	5000	
Purchases	20500	
Wages	6000	

Rent	10000	
Electricity	2600	
Carriage inward	1320	
Carriage outward	1080	
Sundry expenses	1250	
Plant and Machinery	8000	
Office equipment	1000	
Trade debtor	1900	
Trade creditor		800
Bank	820	
Drawing	6330	
Capital		25000

Stock at 31 March 2012 was $3000.

Required: Prepare balance sheet

CHAPTER 12

Depreciation

Depreciation is the part of the cost of a fixed asset that is consumed during the period it is used by a business. For example, a motor car purchased for $10000 may be worth only $8000 after a year later because it is not as good as new after a year's use. The asset has suffered depreciation of $(10000-8000) = $2000.

Assets may depreciate for a number of reasons.

- **Wear and tear:** assets become worn out through use.
- **Obsolescence:** assets have to be replaced because new, more efficient technology has been developed.
- **Passage of time:** an asset acquired for a limited period of time, such as a lease of premises for a given number of years, loses value as time passes.
- **Using up, or exhaustion:** mines, quarries and oil wells depreciate as the minerals etc. are extracted from them.

Advantage or need for providing depreciation

a. It helps to know the true profit or loss: Depreciation is an expense and become an important element of cost of production. Although it is not visible like other expense and never paid to the outsiders, it is desirable to charge depreciation on fixed assets as these are used for earning purposes. So depreciation must be deducted out of the income earned from their use in order to calculate true net profit or loss.

b. It shows true financial position: Financial position can be ascertained from the balance sheet and for the preparation of the balance sheet fixed assets are required to be shown at their true value. If assets are shown in the balance sheet without any charge made for their use or depreciation, then their value must have been overstated the balance sheet and will not reflect the true financial position of the business.

c. It makes provision for replacement fo assents: Assets used in the business need to replace at the end of their estimated useful life. Depreciation can be taken as a source of fund for the replacement of assets.

Methods of calculating depreciation

1) Straight line method/ Fixed installment/ depreciation on cost: Under this method, amount of depreciation in every year will be same. Under this method , depreciation is charged on cost of fixed assets.

a. If estimated life is given and depreciation rate is not given, depreciation Is calculated on the basis of following formula.

$$\text{Depreciation per year} = \frac{\text{Cost of fixed assets- srap valus}}{\text{estimated life}}$$

e.g , cost of plant and machine	=	$50000
scrap value	=	$5000
estimated life	=	10 years
depreciation per year	=	$\frac{50000-5000}{10}$
	=	$4500

b. If depreciation rate is given, depreciation is calculated in this way.

Depreciation per year = (cost of machine-scrap value) × depreciation rate
R

e.g,	cost of machine	=	$50000
	depreciation rate	=	10%
	depreciation per year	=	50000 ×10%
		=	$5000

Year	$
1	5000
2	5000
3	5000
4	5000
5	5000
6	5000
7	5000
8	5000
9	5000
10	5000

2) Reducing balance method/ diminishing balance method/ written down method: Under this method, depreciation is calculated on the basis of written down value method.

Depreciation: Book value of Fixed assets x rate

e.g	cost of machine	=	$50000
	depreciation rate	=	10%
	1^{st} year, cost	=	$50000
	Less, depreciation	=	<u>5000</u>
	2^{nd} year, Book value		45000
	Less, depreciation	=	<u>4500</u>
	3^{rd} year,Book value		4050
	Less, depreciation		<u>4050</u>

Exercise -1

1) A motor vehicle cost $ 18000. It is expected to have a useful life seven years and to be sold for $4000 at the end of that time.

Required: Find out depreciation per year.

2) A machine costing $40000 and with an expected useful life of five years is to be depreciated by reducing balance method. Depreciation rate is 20%.

Required: Find out depreciation for 5 years.

CHAPTER – 13

Accounting principles or concepts

Accounting principles are basic rules that are applied in recording transactions and preparing financial statements. They are also known as concepts. These rules are necessary to ensure that accounting records provide reliable information. All business should apply these rules in their financial statements. These rules are as follows:

Business entity concept: Every business is regarded as having an existence separate from that of its owner. This has already been recognized when an owner's capital has been debited in the business Bank account and credited to the owner's Capital account. The credit in the capital account shows that the owner is a creditor of the business, which owes him the money. This can only the case if the business is regarded as being separate from the owner as no one can owe himself money.

Money measurement: Only transactions that can be expressed in monetary terms are recorded in ledger accounts. Goods, fixed assets, debtors and creditors etc. may be recorded in ledger accounts because they have resulted from transactions that can be expressed in monetary term.

Historical cost: transactions are recorded at their cost to the business. Cost cannot be disputed as invoices or other documentary evidence may be produced to support it. This treatment is said to be objective because it is based on fact and not on opinion. It ignores the changing value of money.

Realization concept: when accountants speak of realization. They mean that something becomes an actual fact, or that something has been converted into money. For example, if a man goes into a shop and says that he will return tomorrow and buy a pair of shoes, there is no sale yet; but if the man returns the next day and buys the shoes, the sales has become a fact. By selling the shoes, the shopkeepers has converted goods into money. The sale has been realized. This principle is important as it prevents revenue from being credited in the accounts before it has been earned.

Duality: the concept of duality recognized that there are two aspects for each transactions-represented by debit and credit entries in accounts. The concept is the basis of the accounting equation:

Assets = capital + liabilities

Consistency: transactions of a similar nature should be recorded in the same way in the same accounting period and in all future accounting periods. Consistency in the treatment of transactions is important to ensure that the profits or losses of different periods, and balance sheet, may be compared meaningfully.

Materiality: sometimes a business may depart from the generally accepted principles for recording some transactions. They may do this when the amounts involved are not considered material in relation to the amounts of the other items in their profit and loss accounts and balance sheet.

A company would treat the purchase of any assets not exceeding , say ,$1000 as revenue expenditure instead of adding it to its fixed assets, as it would not make any noticeable difference to the figure of fixed assets in the balance sheet. It would not be considered a material item.

Accruals (matching): according to this principle, trading and profit and loss should be prepared on the basis of accrual basis but not on cash basis so that expenses are matched to the revenue earned : that is , expenses should be shown have been incurred rather than as they have been paid.

Prudence: the prudence concept is intended to prevent profit from being overstated. If profit is overstated, a trader may believe that his income is more than it really is, and he may withdraw too much money from the business. That would lead to the capital invested in the business being depleted. If it happens too often the business will collapse because there will not be enough money to pay creditors or to renew assets when they are worn out. The principle is sometimes known as the concept of conservatism. It is safer for profit to be understated rather than overstated. The is :

- Profits should not be overstated
- Losses should be provided for as soon as they are recognized.

Going concern: a business is a going concern if there is no intention to discontinue it in the foreseeable future. It is commenced to continue in the foreseeable future. It is assumed that the accounts of a business are prepared on a going concern basis.

Substance over form: these words are used to describe the accounting treatment of something that does not reflect the legal position. The practical view is preferred to the legal view in the accounting treatment. This is known as 'substance over form'.

Multiple choice questions

1) The personal spending of the owner of a business is not recognized as a business expense.

Which accounting principle is being applied?

a. business entity
b. consistency
c. money measurement
d. prudence

2) A business obtained a machine by means of a hire purchase agreement. It showed the machine in its balance sheet at the cash price of $30 000 although only $10 000 has been repaid.
Which accounting principle is involved?

a. accruals b. materiality
c. prudence d. substance over form

3) Which of the following is the definition of a business as a going concern?

a. The assets owned by the business exceed its liabilities.
b. The business has accumulated revenue reserves.
c. The business is currently liquid and able to pay its creditors.
d. The business will continue in operational existence for the foreseeable future.

4) A sole trader pays private expenses from the business bank account and records them asdrawings.
Which accounting principle is applied?

a. business entity b. going concern
c. matching d. prudence

5) There is great uncertainty about the continuance of a business. This has caused the proprietor to make a large reduction in the valuation of the year-end stock.
Which accounting concept does this illustrate?

a. going concern b. matching
c. materiality d. substance over form

6) Which item is related with profit and loss account?

a. Carriage inward b. Closing stock
c. Carriage outward d. Purchase return

7) Which item is shown in debit side of profit and loss account?

a. Discount received b. Commission received
c. Closing stock c. Opening sock.

CHAPTER-14

Business

The literal meaning of business is 'the state of being busy'. But technically, it can't satisfy the actual meaning of businesses because the human beings are always busy in fulfilling their basic needs. To get a clear concept of business, the human activities are to be classified as economic and non-economic activities. Business includes only the economics activities of human being which are performed to generate wealth or profit.

Forms of business organization

Sole trading concern: sole trading concern, also known as sole proprietorship or single entrepreneurship is the simplest and the oldest form of business organization which is owned, managed and controlled by a single person. In sole trading concern, an individual makes all the investment, bears all the risks, enjoys all profits, managers and controls business himself.

Partnership organization: partnership is the form of business organization which is established by two or more persons on the basis of agreement with their joint capital, labour, resource and skills for carrying on large scale business for mutual gain.

Joint stock Company: a joint stock company, simply, is an association of individuals with the common capital divided into a number of transferable shares. It is an artificial person incorporated by law which perform the work like a living person doing within the limitation of prescribed law. It has separate legal entity which is indifferent from the existence of its shareholders.

Public enterprises: it is government enterprises which are owned, managed and controlled by the government. Such organization is run mainly to provide services to the people but profit motive is also the part of their working.

Co-operative organization: it is and autonomous organization, established by low income group of people on the basis of mutual co- operation and equality.

Multinational company: it refers to such company which carries on its business operations in two or more countries having same name. it is a large industrial organization whose main parent company is established in one country and operates the business in a number of other countries. For example, Coca-Cola company.

CHAPTER-15

Accruals and payments

Accruals are expenses that have been incurred but not paid for. For example, an unpaid electricity bill is an accrued expense; the electricity has been consumed, but not paid for. It is also known as due, outstanding, owing. Prepayments are payments made in advance of the benefits to be derived from them.

Items	Trading and Profit and Loss account		Balance sheet	
	Debit	Credit	Debit	Credit
Expenses due given in additional information	Added in related expenses			Shown as current liability
Expenses due given in trial balance				Shown as current liability
Income due given in additional information		Added in related income	Shown as current assets	
Income due given in trial balance			Shown as current assets	
Prepaid expenses given in additional information	Deducted from related expenses		Shown as current asset	
Prepaid expense given in trial balance			Shown as current asset	
Advance income given in additional information		Deducted from related income		Shown as current liability
Advance income given in trial balance				Shown as current liability

For example,

Rent paid	$ 3000	
Additional information		
Rent due	$1000	
solution		
Trading and profit and loss account		
	Dr ($)	Cr ($)
Rent paid (3000+1000)	4000	

Exercise-1

Devram extracted a trial balance at 31 December 2003 from his books after he had prepared his Trading account for the year ended on that date. It was as follows.

	$	$
Fixed assets	40000	
Stock at 31 December 2003	7000	
Trade debtors	1600	
Trade creditors	1400	
Bank	2524	
Long term loan		10000
Gross profit		30000
Rent	2600	
Electricity	926	
Stationery	405	
Motor expenses	725	
Interest on loan	500	
Drawings	5120	
Capital		20000

Further information

1. At 31 December 2003, rent had been prepaid in the sum of $300.
2. The following amounts were owing at 31 December 2003: electricity $242; stationery $84; motor expenses $160.
3. The long term loan was made to the business on 1 January 2003. Interest at the rate of 10% per annum is payable on the loan.
4. The stock of unused stationery on hand at 31 December 2003 was valued at cost: $100.

Required:

a. Prepare Devram's Profit and Loss Account for the year ended 31 December 2003.
b. Prepare the Balance sheet at 31 December 2003.

Exercise-2

Antonia's trial balance at 31 December 2003 was as follows.

	$	$
Sales		120000
Purchases	62400	
Sales return	7300	
Purchases return		4190
Wages	17310	
Rent	3200	
Heating and lighting	2772	
Motor expenses	1284	
Interest on loan	500	
Stock	5660	
Trade Debtors	12440	
Trade Creditors		6167
Bank	5050	
Loan		10000
Premises	24000	
Motor vehicle	7400	
Drawing	7036	
Capital		16000

Further information

1. Stock at 31 December 2003 was valued at $8000
2. The loan was received on 1 April 2003 and is repayable in 2006. Interest is charged at 10% per annum.
3. Expenses owing at 31 December 2003 were as follows.

	$
Wages	558
Heating and lighting	328

4. Rent in the sum of $800 was prepaid at 31 December 2003.

Required:

a. Prepare the Trading and Profit and Loss at 31 December the year ended 31 December 2003.
b. Prepare the Balance sheet at 31 December 2003.

CHAPTER-16

Bad and doubtful debts

Bad debts

When somebody owes money but is unable to pay, the debt is a bad one. As soon as debts are known to be bad. They should be created from the sales ledger by transferring them by journal entry to a Bad debts accounts. The debtor's account will be credited and a Bad debt account will be debited in journal.

Bad debt recovered

A debt that has been written off as bad may be recovered at a later date if the debtor becomes able to pay. The debtor's account will be debited and a Bad debt recovered will be credited in journal.

Provision for doubtful debts

Although a debt may not actually have become bad, there may be doubt as to whether it will be paid; it may turn out eventually to be a bad debt. It would be misleading to include that debt as an asset in the balance sheet pretending that the amount is not in doubt. On the other hand, since it has not yet become bad, it would be wrong write it off. A provision is made to cover that and other doubtful debts.

Accounting treatment for bad and doubtful debt

item	Trading and profit and loss account		Balance sheet	
	debit	Credit	debit	Credit
Bad debt given in additional information	Shown as overhead		Deducted from debtors	
Bad debt given in trial balance	Shown as overhead			
Bad debt recovered		Shown as income		
Provision for doubtful debt given in additional information	Increase in provision for doubtful debt	Decrease in provision for doubtful debt	Deducted from debtors	

Exercise-1

Saul is a trader and his balance at 31 may 2004 was as follows:

Account	**$**	**$**
Freehold property at cost	180000	
Provision for depreciation of freehold property		45000
Plant and machinery at cost	97000	
Provision for depreciation on plant and machinery		53000
Motor Vehicle at cost	41000	
Provision for depreciation on motor vehicle		27000
Trade debtors	34600	
Provision for doubtful debt		1200
Trade creditors		5720
Bank	11374	
Sales		700000
Sales return	6670	
Purchases	410890	
Purchases return		3112
Wages	137652	
Rent paid	10000	
Rent received		1020
Heating and lighting	4720	
Telephone and postage	3217	
Stationery	6295	
Repair to machinery	17600	
Discounts allowed	3220	
Discount received		2942
Carriage inward	4240	
Carriage outward	1819	
Stock	40000	
Drawing	28797	
Capital		200000

Further information

1. Stock at 31 may 2004 cost $58000.
2. Depreciation is to be calculated as follows: freehold property at 4% per annum, straight line ; plant and machinery at 15% per annum; motor vehicles at 30% per annum on the reducing balance.
3. Include in trade debtors is a bad of $1800; the provision for doubtful debts is to be 5% of trade debtors.
4. $400 was owing for heating and lighting, and $220 for stationery. The stock of stationery at 31 May 2004 had cost $450.
5. Rent paid in advance was $2000; rent receivable was owing in the sum of $280.
6. Saul had taken goods for his own use. The goods had cost $2400. No entries for this had been made in the books.

Required

a) Prepare Saul's Trading and Profit and Loss Account for the ended 31 May 2004.
b) Prepare the balance sheet at 31May 2004.

Multiple Choice Questions 1

1) Joel occupies part of Natasha's business premises. Which entries in Joel's books record the rent?

	Debit account	**credit account**
a.	Bank	rent payable
b.	Bank	rent receivable
c.	Rent payable	bank
d.	Rent receivable	bank

2) A trader returns goods to the supplies and receives a refund. Which entries record the refund in the trader's books?

	Debit account	**credit account**
a.	Bank	purchases
b.	Bank	purchase return
c.	Purchases	bank
d.	Purchase	bank

3) Yasmina purchased some office equipment for use in her business. Th equipment was faulty and she returned it to the supplier who refunded

the cost to Yasmina. Which entries in Yasmina's books record the return of the equipment?

	Debit account	**credit account**
a.	Bank	purchases returns
b.	Bank	office equipment
c.	Purchase return	bank
d.	Office equipment	bank

4) Which of the following does not appear in a profit and loss account?

a. Carriage inward
b. Carriage outward
c. Discount allowed
d. Discount received

5) Which of the following statement is incorrect?

a. Assets=liabilities+capital
b. Capital=assets-liabilities
c. Capital-liabilities=assets
d. Liabilities=assets-capital

6) Tania purchased goods for $1000 less 25% trade discount. She was allowed cash discount of 10%. Which amount she enter in her purchases journal?

a. $650 b. $675 c. $750 d. $1000

7) Lara purchased goods costing $1800 less trade discount of 30%. He was allowed cash discount of 5%. How much should Lara have to pay for the goods?

a. $1080 b. $1197 c. $1260 d. $1800

8) Which item is revenue expenditure?

a. cost of painting new office premises during construction
b. cost of repairs to factory plant and machinery
c. legal fees for the purchase of new factory premises
d. wages of a company's own workmen for building an office extension

9) A transport business owned by a sole proprietor purchases a motor vehicle. This is charged to the Motor Vehicles Running Costs account. What are the effects of this on the end-of-year Balance Sheet?

a. fixed assets understated current assets understated
b. fixed assets overstated current assets overstated
c. fixed assets overstated capital account overstated
d. fixed assets understated capital account understated

10) A business that purchases a shop incurs the following costs.

purchase price of the shop	680 000
legal fees incurred in the purchase of the shop	7 200
cost of initial stock	12 500
cost of installing air conditioning	47 300

Which amount will be capitalized as the cost of the shop?

a. $680 000 b. $687 200 c. $734 500 d. $747 000

Multiple Choice Questions 2

1) A business purchases a vehicle for $10 000. The business depreciates its non-current (fixed) assets at 20 % using the diminishing value method. What is the depreciation charge for year 2?

a. $1600 b. $2000 c. $6400 d. $8000

2) An item of capital expenditure has been incorrectly treated as revenue expenditure in the accounts of a business. What is the effect of this error on the accounts of the business?

Assets profit

a. overstated overstated b. overstated understated
c. understated overstated d. understated understated

3) A business has a bank overdraft of $4800. It pays for materials invoiced at $3000 less a trade discount of 20 % and a settlement discount of 5 %.A cheque for $500 is received from a debtor. What is the bank balance after these transactions?

a. $2020 overdraft b. $6580 overdraft
c. $7150 overdraft d. $7580 overdraft

4) The personal spending of the owner of a business is not recognized as a business expense. Which accounting principle is being applied?

a. business entity b. consistency
c. money measurement d. prudence

5) A business obtained a machine by means of a hire purchase agreement. It showed the machine in its balance sheet at the cash price of $30 000 although only $10 000 has been repaid. Which accounting principle is involved?

a. accruals b. materiality
c. prudence d. substance over form

6) The table shows information from the books of a business at 30 April 2010.

Details	$
credit sales invoiced during financial year	79000
goods sent to customers on 28 April 2010 and invoiced 4 May 2010	6100
goods sent to customers during April 2010 on sale or return basis butnot sold by 30 April 2010	8300

What is the amount of sales for the year ended 30 April 2010?

a. $76800 b. $85100 c. $85300 d. $93400

Multiple Choice Questions 3

1) Davina bought goods on credit from Sharon for $600 less trade discount of $120. Which entries record this transaction in Davina's books?

	Dr	Cr
a.	Purchases $480	Sharon $480
b.	Purchases $480 Discount allowed $120	Sharon $600
c.	Purchases $600	Sharon $600
d.	Purchases $600	Sharon $480 Discounts received $120

2) Shirley bought goods from Corrine. The goods had a list price of $800. Corrine allowed Shirley trade discount of 20% and cash discount of 5%.
In Corrine books, which entries record the cheque she received from Shirley?

	Dr	Cr
a.	Bank $608 Discount allowed $32	Shirley $640
b.	Bank $608 Discounts received $32	Shirley $640
c.	Bank $608 Discounts allowed $152	Shirley $760
d.	Bank $608 Discounts Received $152	Shirley $760

3) Which item is charged in trading account?

a. Carriage outward b. Carriage inward
c. Sales expenses d. Discount allowed

4) The owner of a business has taken goods for his own use but no entry has been made in the books to record this. What is the effect of this on the Balance sheet?

	Stock	**Capital**
a.	No effect	no effect
b.	No effect	overstated
c.	Overstated	no effect
d.	Overstated	overstated

5) The following information has been extracted from a Balance sheet at 31 December 2003.

	$
Fixed assets	300000
Working capital	30000
Long term loan	20000
Profit for the year	35000
Drawing	25000

What is the balance on Capital account at 31 December 2003?

A. $300000 B. $320000 C. $340000 D. $350000