EDU SERUMX COLLEGE OF COMMERCE and MANAGMENT

SYLLABUS

Class – BBA I Year

Subject – Financial Accounting (Core)

Unit	Topics
Unit 1	**Accounting & Its Role in Business**
	- Importance of Accounting in Business
	- Relationship between Accounting & Other Financial Areas
	Double Entry System
	- Meaning and Application
	Book Keeping
	- Definition, Importance
	- Advantages, Concepts, and Conventions
	Difference between:
	- Financial Accounting, Cost Accounting, and Management Accounting
Unit 2	**Types of Books of Accounts & Their Preparation**
	Books of Accounts:
	- Journal
	- Ledger
	- Trial Balance
	Depreciation:
	- Calculation & Methods
	Computerized Accounting Software:
	- Cloud Books, Wave, Tally
Unit 3	**Preparation of Final Accounts**
	Trading Account
	Profit & Loss Account
	Balance Sheet
	EMI Chart Preparation
Unit 4	**Bank Reconciliation Statement**
	- Purpose and Preparation
	Branch Accounts
	- Concepts and Recording
	Department Accounts
Unit 5	**Special Accounts**
	Royalty Accounts
	Hire Purchase Accounts:
	- Accounting records in the books of purchaser and vendor

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UNIT – 1&2

Fundamental Principles of Financial Accounting

Definition (according to the American Institute of Certified Public Accountants):

- Accounting is the art of recording, classifying, and summarizing financial transactions and events in monetary terms, and interpreting the results.

Key Characteristics of Accounting:

1. **Science and Art**: Accounting is both a science (systematic knowledge) and an art (practical application).
2. **Recording Financial Transactions**: It deals only with financial transactions and events.
3. **Monetary Terms**: All transactions are recorded in terms of money.
4. **Systematic Records**: Accounting keeps complete, accurate, and permanent records of all transactions.
5. **Analysis**: It analyzes the results of transactions in detail.

Objectives of Accounting:

1. **Systematic Record**: To maintain a systematic record of the firm's financial transactions. This is the first step in creating financial statements.
2. **Performance Measurement**: To ascertain the performance of the business by preparing the income statement (profit and loss account) that shows profits or losses.
3. **Protection of Assets**: Accounting helps track the firm's assets and liabilities, ensuring the business's resources are properly controlled.
4. **Financial Reporting**: Accounting forms the basis for financial reporting, which helps understand the business's financial health (e.g., liquidity and solvency).
5. **Decision Making**: Accounting helps businesses make informed decisions by identifying, measuring, and communicating financial data.

Accounting as a Science and Art:

- **Science**: Accounting is a science because it follows systematic principles, concepts, and assumptions that are universally accepted and verifiable.
- **Art**: Accounting is an art because it involves the practical application of knowledge to maintain records and manage day-to-day business activities.

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Book-Keeping:

- **Definition**: Book-keeping is the proper and systematic maintenance of books of accounts.
- It begins with identifying business transactions that must be financial in nature (e.g., selling goods for cash).

Steps in Book-Keeping:

1. **Identify Transactions**: Recognize which activities are financial transactions (e.g., buying or selling goods).
2. **Initial Record**: Record the transactions in books.
3. **Ledger Preparation**: Prepare ledger accounts for each type of transaction.
4. **Balance Ledger**: Summarize the ledger accounts by balancing them.
5. **Prepare Trial Balance**: Create a trial balance to ensure that the books are correct and balanced.

DIFFERENCE BETWEEN BOOK-KEEPING AND ACCOUNTING

No	Basis of Difference	Book-Keeping	Accounting
1	**Transaction**	Trading transactions are recorded in primary books.	Entries written in primary books are checked and verified.
2	**Posting**	Entries are posted in the ledger from the journal and subsidiary books.	Posting is checked to ensure whether the entries are correctly posted or not.
3	**Total and Balance**	Involves totaling of journals and finding balances of the ledger.	Based on ledger balances, final accounts are prepared.
4	**Objectives**	The objective is to write all trading transactions in a systematic manner.	The objective is to analyze the transactions recorded in the books.
5	**Adjustments and Rectification**	Adjustments and rectifications of errors are not included.	Accounting includes adjustments and rectifications of errors.
6	**Scope**	The scope of Book-Keeping is narrow.	The scope of Accounting is wide.
7	**Final Accounts**	Final accounts are not prepared in Book-Keeping.	Final account preparation is a must.

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Accounting Concepts

1. **Business Entity Concept**
   This concept treats the business as a separate entity from its owner. It means the personal transactions of the owner are kept separate from business transactions. For example, if the owner invests ₹50,000, it is treated as a liability for the business until the owner withdraws it.
2. **Going Concern Concept**
   This assumes that a business will continue to operate indefinitely unless there's evidence suggesting otherwise. Assets are valued at their original cost, not their current market value. This ensures assets are used over their useful life.
3. **Dual Aspect Concept**
   Every transaction has two aspects: one benefit is received (debit), and one is given (credit). This is the foundation of the double-entry system. It ensures the accounting equation (Assets = Liabilities + Owner's Equity) always balances.
4. **Historical Cost Concept**
   According to this concept, assets are recorded at their original cost, not their current market value. This ensures that businesses do not inflate their asset values and maintains consistency.
5. **Money Measurement Concept**
   This concept says that only transactions that can be measured in monetary terms are recorded. Non-monetary events (e.g., a conflict between managers) are not recorded.
6. **Realization Concept**
   Revenue is recognized when a sale is made, not when cash is received. This ensures businesses do not inflate their profits by recording revenue prematurely.
7. **Accrual Concept**
   This concept recognizes transactions when they occur, not when cash changes hands. For example, income earned but not yet received and expenses incurred but not yet paid are still recorded.
8. **Matching Concept**
   Costs are matched with the revenues they help generate in the same accounting period. This helps in accurately calculating profit for that period.
9. **Accounting Period Concept**
   This assumes a business's activities are divided into periods (usually a year). At the end of each period, financial reports are prepared, even if the business has not been liquidated. This helps in comparing performance over time.
10. **Verifiable Objective Concept**
    accounting data should be clear, accurate, and based on evidence. Each transaction should be backed by source documents (e.g., invoices, receipts) that can be checked and verified by auditors.

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Accounting Conventions

1. **Convention of Conservatism**
   This convention suggests that accountants should be cautious while preparing financial statements. They should not anticipate profits, but should account for possible losses. For example, inventory is valued at the lower of cost or market price, and provisions are made for bad debts before determining profits.
2. **Convention of Consistency**
   According to this convention, accounting methods should remain consistent over time. For instance, if a business uses a particular method to calculate depreciation, it should continue using the same method unless there's a good reason to change. Any changes made should be clearly explained. This helps in comparing financial results over different periods or between different companies.
3. **Convention of Material Disclosure**
   This convention states that only significant or "material" information should be disclosed in financial statements. This ensures that the most important facts are shared, without overwhelming users with insignificant details. For example, alongside asset values, the method of valuation should also be disclosed. What is considered material depends on the situation and the judgment of the accountant.

Accounting Systems

1. **Cash System**
   - **What it is:** Only cash transactions are recorded (money received or paid). Credit transactions are noted separately and recorded in the Cash Book when paid or received.
   - **Who uses it:** Small businesses, professionals, or non-trading organizations where most transactions are in cash.
2. **Mahajani System**
   - **What it is:** This is an old accounting method in India. Transactions are recorded in long books called "Bahis," using languages like Hindi, Urdu, or regional dialects.
   - **Who uses it:** It’s a traditional, scientific method based on certain principles but is less commonly used today.
3. **Single Entry System**
   - **What it is:** Some transactions are recorded once, others twice, and some are recorded in full. It is an incomplete system where only cash books and personal accounts are maintained.
   - **Who uses it:** This system is rarely used today because it's unscientific and incomplete.
4. **Double Entry System**
   - **What it is:** Every transaction is recorded twice – once as a debit and once as a credit. This ensures both sides of the accounts remain balanced.
   - **Who uses it:** This is the most complete and scientific method, widely used in businesses for accurate and balanced accounting.

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Double Entry System

The **Double Entry System** is the most popular and widely used method of accounting. It is based on the idea that every transaction has two parts:

- **What you receive (Debit)**
- **What you give in return (Credit)**

Evolution of Double Entry System

- It started in Italy in the 15th century.
- In 1494, the mathematician Lucas Pacioli wrote a book called *De Computiset Scripturise*, which first explained the system.
- Later, this system was improved and spread to other countries.

Stages of Double Entry System:

1. **Recording transactions in the journal**: All transactions are first recorded in a journal.
2. **Classifying transactions**: The journal entries are then transferred (posted) to the ledger accounts.
3. **Closing books and preparing final accounts**: After classifying, the books are closed, and the final financial statements (like profit and loss account, balance sheet) are prepared.

Merits (Advantages) of Double Entry System:

1. **Complete Record**: Each transaction is recorded in two places (debit and credit), providing full details.
2. **Better Understanding of Business**: It helps understand the business's financial health, such as assets, liabilities, and capital.
3. **Mathematical Accuracy**: Since every debit has a corresponding credit, the system allows for easy checks of calculations using a trial balance.
4. **Prevents Fraud**: Double recording makes it harder to commit fraud or mistakes, and fraud can be detected more easily.
5. **Profit & Loss Information**: This system helps prepare a profit and loss account to know the business's earnings or losses.
6. **Financial Health**: A balance sheet gives an easy understanding of the business's financial status.
7. **Comparative Analysis**: It allows comparing the current year's financial results with previous years for better decision-making.

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Demerits (Limitations) of Double Entry System:

1. **Complexity**: The rules of debit and credit can be hard to follow, especially for beginners.
2. **Error Possibility**: Even though it's scientific, errors can still happen if not followed carefully.
3. **Training Required**: A good understanding of accounting principles is needed to use the system effectively.
4. **Costly for Small Traders**: It can be expensive for small businesses due to its complexity.
5. **Mistakes Can Lead to Wrong Results**: A small mistake can lead to incorrect financial results, affecting decisions.

Classification of Accounts

Accounts are classified into three main types:

1. Personal Accounts

These accounts relate to individuals, businesses, or organizations.

- **Natural Personal Accounts**: These represent real people, like "Shyam's Account" or "Gopal's Account."
- **Artificial Personal Accounts**: These represent organizations or institutions that are treated as persons in business. Examples include "ABC Club Account" or "Insurance Company Account."
- **Representative Personal Accounts**: These represent a group or person, often for amounts owed. For example, an "Outstanding Rent Account" represents money owed to the landlord, or an "Outstanding Salaries Account" represents money owed to employees.

2. Real Accounts

These accounts are related to things, assets, or properties.

- **Intangible Accounts**: These are for things you can't touch, but can measure in money. Examples include "Goodwill Account" or "Patents Account."
- **Tangible Accounts**: These are for physical things that you can touch, like "Furniture Account," "Stock Account," or "Building Account."

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3. Nominal Accounts

These accounts deal with income, gains, expenses, and losses.

- **Revenue Accounts**: These represent income or earnings, such as "Rent Received," "Interest Received," or "Commission Paid."
- **Expenditure Accounts**: These represent costs or losses, such as "Rent Paid," "Interest Paid," or "Salary Paid."

At the end of the financial year, the balances from Nominal Accounts are transferred to the **Trading Account** or **Profit and Loss Account** to calculate the net profit or loss for the period.

In simple terms:

- **Personal Accounts**: Accounts for people or organizations.
- **Real Accounts**: Accounts for things you own or use.
- **Nominal Accounts**: Accounts for income and expenses.

Rules of Double Entry System (Simplified)

In the Double Entry System, every transaction is recorded with two parts: one debit and one credit. The rules for these are:

1. **Personal Accounts**:
    - **Debit the Receiver**: If someone receives something from the business, we debit their account.
    - **Credit the Giver**: If someone gives something to the business, we credit their account.
2. **Real Accounts**:
    - **Debit What Comes In**: If something enters the business (like an asset), we debit it.
    - **Credit What Goes Out**: If something leaves the business (like an asset being sold), we credit it.
3. **Nominal Accounts**:
    - **Debit All Expenses and Losses**: When we incur an expense or a loss, we debit the account.
    - **Credit All Incomes and Gains**: When we earn money or gain something, we credit the account.

Capital and Revenue Classification

- **Capital Expenditure**:
    - This is spent on acquiring or improving long-term assets that bring lasting benefits. Examples include the cost of land, buildings, machinery, etc. These are investments that improve the business's ability to earn in the long term.

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- **Revenue Expenditure**:
  - This is spent on day-to-day operations to maintain the business's current productivity. It covers short-term costs that help run the business, like salaries, rent, utilities, advertising, and other operating expenses.
- **Deferred Revenue Expenditure**:
  - This is an expense that provides benefits beyond the current accounting period but is expected to last for a shorter time than capital expenditure. Examples include heavy advertising campaigns or research and development costs. These are written off over a few years.

Capital vs. Revenue Receipts

- **Capital Receipts**:
  - These are money received for long-term investments or assets. Examples include the sale of fixed assets (like land or machinery) or loans received.
- **Revenue Receipts**:
  - These are money received from normal business operations, such as the sale of goods or services, rent, interest, or royalties.

Accounting Standards

Accounting standards are a set of guidelines or rules that ensure consistency and transparency in preparing financial statements. They help businesses present a true and fair view of their financial position. Different businesses might use different methods, but standard rules are necessary to reduce confusion and make the financial data comparable.

ACCOUNTING STANDARDS ISSUED BY THE ICAI

The Institute of Chartered Accountants of India has thus far issued the following standard effective from the date noted against them.

Accounting Standard (AS)	Title	Effective Date
AS-1	Disclosure of Accounting Policies	01-04-1991
AS-2	Valuation of Inventories	1-4-1991 (Revised)
AS-3	Cash Flow Statement	1-6-1991 (Revised)
AS-4	Contingencies and Events Occurring After the Balance Sheet Date	01-04-1995
AS-5	Net Profit or Loss for the Period, Prior Items and Changes in Accounting Policies	01-04-1996
AS-6	Depreciation Accounting	01-04-1995
AS-7	Accounting for Construction Contracts	01-04-1991
AS-8	Accounting for Research and Development	01-04-1991

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AS-9	Revenue Recognition	01-04-1991
AS-10	Accounting for Fixed Assets	01-04-1991
AS-11	Accounting for the Effects of Changes in Foreign Exchange Rates	01-04-1995
AS-12	Accounting for Government Grants	01-04-1994
AS-13	Accounting for Investments	01-04-1995
AS-14	Accounting for Amalgamation	01-04-1995
AS-15	Accounting for Retirement Benefits in the Financial Statements of Employers	01-04-1995
AS-16	Borrowing Costs	01-04-2000
AS-17	Segment Reporting	01-04-2001
AS-18	Related Party Disclosures	01-04-2001
AS-19	Leases	01-04-2001
AS-20	Earnings Per Share	01-04-2001
AS-21	Consolidated Financial Statements	01-04-2001
AS-22	Accounting for Taxes on Income	01-04-2002
AS-23	Accounting for Investments in Associates in Consolidated Financial Statements	01-04-2002
AS-24	Discontinuing Operations	01-04-2002
AS-25	Interim Financial Reporting	01-04-2002
AS-26	Intangible Assets	01-04-2003
AS-27	Financial Reporting of Interest in Joint Ventures	01-04-2002
AS-28	Impairment of Assets	01-04-2004
AS-29	Provisions, Contingent Liabilities and Contingent Assets	01-04-2004

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Journal

A **journal** is the first place where business transactions are recorded. It's known as the "book of original entry" because all transactions are initially recorded here before being transferred to other accounts. The process of recording in the journal is called **journalizing**.

Basic Journal Entry Format:

- **Date**: When the transaction occurred
- **Particulars**: The accounts involved
- **L/F (Ledger Folio)**: The reference number of the account in the ledger
- **Debit Amount**: The amount to be debited
- **Credit Amount**: The amount to be credited

Example Journal Entry:

Date Particulars L/F Debit Amount Credit Amount

25/07/2009 Account A Dr. X

To Account B X

(Explanation)

Compound Journal Entry

When multiple similar transactions happen on the same day, one **compound journal entry** can be used instead of separate entries. This simplifies the process when multiple debits or credits are involved.

Example of Compound Journal Entry:				
Date	**Particulars**	**L/F**	**Debit Amount**	**Credit Amount**
25-07-2009	Postage A/c Dr.		X	
	Stationery A/c Dr.		Y	
	Cartage A/c Dr.		Z	
	To Cash A/c			X + Y + Z

Types of Discounts

1. **Trade Discount**:
   - Given by sellers to buyers to promote sales.
   - A percentage off the selling price.
   - **Not recorded in the books**. Only the discounted price is recorded.
2. **Cash Discount**:
   - Given when payment is made early, usually as a percentage of the amount due.
   - **Recorded in the books**.
   - If a **debtor** receives a discount, it's a **gain** and credited to the **Discount A/c**.
   - If a **creditor** allows a discount, it's a **loss** and debited to the **Discount A/c**.

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Types of Cash Books:

1. **Single Column Cash Book**: Records only cash transactions.
2. **Cash Book with Discount**: Includes both cash and discount transactions.
3. **Cash Book with Bank & Petty Cash Book**: Records cash, bank, and petty cash transactions.

Distinctions between Trade Discount and Cash Discount

S.No.	Trade Discount	Cash Discount
1	Allowed at the time of making purchases or sales.	Allowed at the time of making payments or receipts of cash.
2	Calculated as a certain percentage on the invoice price of goods purchased or sold.	Calculated as a certain percentage on the amounts due to creditors or amounts due from debtors.
3	Not shown in the books of accounts. Only the net amount of purchase or sale is recorded.	Shown in the books: discount allowed is a debit entry, discount received is a credit entry.
4	Allowed to promote more sales or purchases.	Allowed to encourage parties to make payments on time.

Cash Book

Meaning of Cash Book: A **Cash Book** is a record where all transactions involving cash receipts and payments are recorded. It tracks all cash-related activities as soon as they happen.

- It acts as both a **journal** and a **ledger** for cash transactions.
- It has two sides:
  - **Debit side**: All cash receipts.
  - **Credit side**: All cash payments.

Features of Cash Book:

1. Only cash transactions are recorded.
2. It serves as both a **journal** and **ledger** for cash transactions.
3. Cash receipts are recorded on the **debit side**, and cash payments are recorded on the **credit side**.
4. It only records cash transactions.
5. All cash transactions are entered in chronological order.

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Types of Cash Book

1. **Single Column Cash Book**
   - This is the simplest form of cash book. It records only **cash receipts** and **cash payments**.
   - It has one column on both the debit and credit sides to record cash transactions.

Dr. Single				Column Cash Book Cr.			
Date	Particulars	L.F.	Amount Rs	Date	Particulars	L.F.	Amount Rs

2. **Double Column Cash Book**
   - It records **cash receipts** and **cash payments**, just like the single column cash book, but also includes a **bank column** to record transactions related to the bank account.
   - It has two additional columns: one for **cash** and one for **bank** on both the debit and credit sides.

(Dr side)						(Cr side)					
Date	**Particulars**	**L/F**	**Discount Allowed**	**Cash (Dr)**	**Bank (Dr)**	**Date**	**Particulars**	**L/F**	**Discount Received**	**Cash (Cr)**	**Bank (Cr)**

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3. **Triple Column Cash Book**
    - This is a more detailed cash book that includes **cash**, **bank**, and **discount** columns.
    - It records cash receipts and payments, bank transactions, and any **cash discounts** given or received.
    - It is useful for businesses that deal frequently with discounts.

Date	Particulars	L.F.	Discount (Rs)	Cash (Rs)	Bank (Rs)

4. **Petty Cash Book**
    - This type of cash book is used to record small, day-to-day expenses (like office supplies, postage, etc.) that don't warrant a detailed entry in the regular cash book.

Advantages of a Petty Cash Book

1. **Saves Time**: By recording minor expenses in the petty cash book, the chief cashier's time is saved.
2. **Less Work for Posting**:
    - Only a few expense categories need separate accounts.
    - Monthly totals for each expense type can be posted together, simplifying ledger entries.
3. **Fewer Mistakes**: The chief cashier regularly checks the petty cash book, reducing the chance of errors.
4. **Controls Small Expenses**: The petty cashier is only allowed to spend up to a set amount, keeping expenses within budget.
5. **Prevents Fraud**: Any potential misuse is limited to the petty cash balance, reducing the risk of larger fraud.
6. **Specialization**: By having separate books for main and petty cash, each book handles specific types of cash entries efficiently.

Posting of Petty Cash Book in Ledger

1. **As Part of the Journal/Double Entry System**: Entries in the petty cash book follow double-entry principles and are part of the main accounting system.
2. **As a Memorandum Book**: Alternatively, it can serve as a record-keeping book, providing details on petty expenses without affecting the double-entry system directly.

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Imprest vs. Non-Imprest System of Petty Cash Book

- **Imprest** (or **Float**) is the amount of money given to the petty cashier by the main cashier to cover minor expenses for a set period.
- Petty cash books can be managed using either the **imprest system** or the **non-imprest system**.

Features of the Imprest System of Petty Cash

1. **Estimated Amount**: The chief cashier calculates the expected petty expenses for a set period.
2. **Advance Given**: The chief cashier provides this estimated amount to the petty cashier at the start of the period.
3. **Expense Reporting**: At the end of the period, the petty cashier submits the petty cash book with all receipts and vouchers to the chief cashier.
4. **Review by Chief Cashier**: The chief cashier reviews the petty cash book to ensure all expenses are accurate and legitimate.
5. **Replenishment**: The chief cashier reimburses the petty cashier with the amount spent, so the petty cashier's cash is restored to the initial balance.
6. **Consistent Balance**: The petty cashier begins each new period with the same fixed amount of petty cash, creating consistency in managing minor expenses.

Ledger

A **ledger** is the main or final book in double-entry accounting. It organizes transactions recorded in other books into specific accounts. This allows businesses to see each account's position over a set period.

Characteristics of a Ledger

1. **Primary Book**: The ledger is the main book in accounting.
2. **Index**: The first few pages are for an index, making it easy to locate specific accounts. These pages aren't numbered.
3. **Pages for Each Account**: Each account has a dedicated page (called a folio) in the ledger.
4. **Debit and Credit for Every Transaction**: Every transaction has one account debited and another credited.
5. **Final Entry Book**: The ledger is the last step in daily bookkeeping.
6. **Organizes Transactions**: While journals hold all entries, the ledger organizes these into individual accounts.

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Importance/Advantages of a Ledger

1. **Account Information**: Shows details about each account.
2. **Income and Expense Details**: Breaks down income and expenses by account.
3. **Financial Position Assessment**: Helps in understanding the financial health of the business.
4. **Accuracy Check**: Serves as a check for accuracy in records.
5. **Profit and Loss Insight**: Shows if the business is making a profit or loss.
6. **Time-Saving**: Organizing transactions makes it easier to find details quickly.
7. **Asset Information**: Lists all assets and their value.
8. **Liability Information**: Shows all the business's debts or obligations.
9. **Overall Business Position**: Gives a complete picture of the business's status.
10. **Evidence in Disputes**: Can be used as proof in case of business disagreements.

Difference between journal and Ledger

S. No.	Basis of Difference	Journal	Ledger
1	Nature of Book	Book of first or original entry	Book of final entry
2	Record	Chronological record	Analytical record
3	Weight in Legal Evidence	Greater weight as legal evidence	Lesser weight as it is based on the journal
4	Unit of Classification of Data	Transaction	Account
5	Process of Recording	Called "journaling"	Called "posting"
6	Place	Transactions for one account are recorded on different dates	Transactions for one account are recorded in one place

Posting

When the transactions entered in journal are recorded in the ledger, it is called posting. It other words, posting is the process transferring the debits and credits of journal entries to the ledger account. The subject of such posting to have a fixed classified record of various transactions pertaining to each account.

Balancing of Ledger Accounts

- **Asset, Liability, and Capital Accounts**: At the end of an accounting period, asset, liability, and capital accounts usually have a balance. This balance is carried forward to the next period, as the business continues with these assets, liabilities, and capital. To show the closing balance, we use:
  - **"Balance c/d"** (carried down) to show the closing balance of the current period.

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- **"Balance b/d"** (brought down) to carry that balance forward into the next period.

- **Expense and Revenue Accounts (Nominal Accounts)**:
  - These accounts, such as expenses or income, do not carry a balance forward to the next period. Expenses paid are for that period only, so they don't need to be carried forward.
  - Expenses are posted directly to the **debit side of the Profit and Loss Account**.
  - Income or revenue (like rent or interest received) is posted to the **credit side of the Profit and Loss Account**.

Balancing of ledger Accounts

Assets, liabilities and capital accounts have certain closing balance of the end of accounting period, so their values are to be carried forward to the next accounting period. This is why they are closed as "By Balance b/d" or "To Balance c/d. The balance of those accounts carried forward to the next accounting period, because the firm has to carry on tits business with these assets, liabilities and capital in hand. While closing these accounts we write the 'Balance c/d' to show the closing balance of the account. While closing nominal accounts or those accounts which are either an expense or revenue. we do not use the word balance c/d because the balance of these accounts need be carried forward to the next period. Whatever has been paid on account of expenses has been paid once and forever. This is the expense of the business. so it should be directly posted to the debit side of the profit and loss account or trading account. It the same way, account relating to income or gain or revenues are also closed by transfer to profit and loss account. Receipts i.e. rent, interest and discount are revenue of the business, so while closing these accounts their balance will be transferred to profit and loss account.

Subsidiary Books in Accounting

Subsidiary books are specialized journals where specific types of transactions are recorded before being posted to the ledger. Here are key types and their formats:

Posting in the Ledger

Posting in the Ledger

1. **Purchase Day Book**:
   - **Supplier's Account**: Credit each supplier's account individually with "By Purchases A/c."
   - **Purchases A/c**: Debit the monthly total with "To Sundries as per Purchases Book."

Date	Particulars (Supplier's Name)	Invoice No.	L.F.	Amount (Rs.)	Net Amount (Rs.)

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Posting:

- Credit each supplier's account with "By Purchases A/c."
- Debit **Purchases A/c** with "To Sundries as per Purchases Book" for the total.

2. **Sales Book**:
   - **Customer's Account**: Debit each customer's account individually with "To Sales A/c."
   - **Sales A/c**: Credit the monthly total with "By Sundries as per Sales Book."

Date	Particulars (Customer's Name)	Invoice No.	L.F.	Amount (Rs.)	Net Amount (Rs.)

Posting:

- Debit each customer's account with "To Sales A/c."
- Credit **Sales A/c** with "By Sundries as per Sales Book" for the total.

3. **Purchase Returns Book**:
   - **Supplier's Account**: Debit each supplier's account with "By Purchases Returns A/c."
   - **Purchases Returns A/c**: Credit the monthly total with "To Sundries as per Purchase Returns Book.

Date	Particulars (Supplier's Name)	Debit Note No.	I.F.	Amount (Rs.)

Posting:

- Debit each supplier's account with "By Purchase Returns A/c."
- Credit **Purchase Returns A/c** with "To Sundries as per Purchase Returns Book" for the total.

4. **Sales Returns Book**:
   - **Customer's Account**: Credit each customer's account with "By Sales A/c."
   - **Sales Returns A/c**: Debit the monthly total with "To Sundries as per Sales Returns Book."

Date	Particulars (Customer's Name)	Credit Note No.	I.F.	Amount (Rs.)

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Posting:

- Credit each customer's account with "By Sales A/c."

  Debit **Sales Returns A/c** with "To Sundries as per Sales Returns Book" for the total.

5. **Bills Receivable Book**:
   - **Customer's Account**: Credit the drawer's account (customer's account) when the bill is received.
   - **Bills Receivable A/c**: Debit the monthly total of the Bills Receivable Book.

Date Received	Drawer	Acceptor	Where Payable	Date of Bill	Term	Due Date	I.F.	Amount (Rs.)	Remarks

Posting:

- Credit the drawer's account (customer's account) when the bill is received.
- Debit **Bills Receivable A/c** with the total for the period.

6. **Bills Payable Book**:
   - **Payee's Account**: Debit the payee's account when the bill is accepted.
   - **Bills Payable A/c**: Credit the monthly total of the Bills Payable Book.

Date of Acceptance	To Whom Given	Payee	Where Payable	Date of Bill	Term	Due Date	I.F.	Amount (Rs.)	Remarks

Posting:

- Debit the payee's account when the bill is accepted.
- Credit **Bills Payable A/c** with the total for the period.

Trial Balance

A **Trial Balance** is a list of all ledger accounts, showing their balances. The debit balances go in one column and the credit balances in another. Its main purpose is to check that the total debits match the total credits, ensuring that the books are arithmetically correct under the double-entry system.

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Main Characteristics of a Trial Balance

1. **Statement Form**: It's a statement in table form, with columns for debit and credit balances.
2. **Ledger Balances**: Shows the closing balances of all accounts from the ledger.
3. **Not an Account**: It's a summary, not an account itself.
4. **Prepared Anytime**: Can be prepared any time the accounts are balanced.
5. **Summary of Balances**: Lists all ledger balances in one place.
6. **Checks Accuracy**: Matches debit and credit totals to confirm entries are correct.
7. **Assists Final Accounts**: Helps in creating the Trading Account, Profit & Loss Account, and Balance Sheet.

Objectives of Preparing a Trial Balance

1. **Check Arithmetic Accuracy**: Equal debits and credits indicate correct calculations.
2. **Detect Errors**: Shows errors in adding or recording entries in books.
3. **Verify Ledger Postings**: Helps find mistakes in posting from subsidiary records.
4. **Identify Balancing Errors**: Finds mistakes in balancing ledger accounts.
5. **Verify Debtors & Creditors**: Confirms correctness of these schedules.

Limitations of a Trial Balance

- **Not Absolute Proof**: Errors can still exist even if the trial balance matches.
- **Errors Not Detected by Trial Balance**:
  - **Omission Errors**: When an entry is missing entirely.
  - **Commission Errors**: Wrong account, but correct side.
  - **Errors in Subsidiary Books**: Incorrect amount in subsidiary books.
  - **Compensating Errors**: Mistakes that cancel each other out.
  - **Principle Errors**: Misclassifying expenses or incomes, like capital vs. revenue.

Methods of Preparing a Trial Balance

1. Total Method: Lists the total debits and credits of each account from the ledger.

Title of Accounts	L.F.	Debit Total (Rs.)	Credit Total (Rs.)
		Total	**Total**

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2. **Balance Method**: Lists only the final debit or credit balance of each account.

Title of Accounts	L.F.	Debit Balance (Rs.)	Credit Balance (Rs.)
		Total	Total

3. **Total Cum Balance Method**: Combines both total and balance methods, showing debits, credits, and the balance of each account.

Title of Accounts	L.F.	Debit Total (Rs.)	Credit Total (Rs.)	Debit Balance (Rs.)	Credit Balance (Rs.)
		Total	Total	Total	Total

Depreciation Accounting

Depreciation is the decrease in value of fixed assets (like machinery, buildings, etc.) over time. This happens because of use, wear, age, or obsolescence. Depreciation is recorded as an expense in each accounting period, which helps calculate the correct profit or loss for that period.

Key Points about Depreciation

1. **Charged on Fixed Assets**: Applies to assets used long-term, except land.
2. **Book Value**: Calculated on the asset's book value, not market value.
3. **Permanent Reduction**: Depreciation permanently reduces the asset's value.
4. **Regular Expense**: Recorded every year as long as the asset is used.
5. **Gradual Decline**: Asset value decreases steadily over time.

Causes of Depreciation

1. **Wear and Tear**: Continuous use causes assets to wear out.
2. **Time**: Certain assets, like leases or patents, lose value over time, regardless of use.
3. **Obsolescence**: When newer models or technology replace old assets.
4. **Depletion**: Natural resources, like mines or oil wells, get used up.
5. **Accidents**: Damage from accidents can reduce asset value.

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Why Depreciation is Important

1. **Accurate Profits**: Reflects true profit or loss by accounting for asset value loss.
2. **True Financial Position**: Shows assets' true value on the balance sheet.
3. **Asset Replacement**: Saving part of profits each year helps in replacing old assets.
4. **Correct Cost of Production**: Depreciation affects production costs, helping set accurate prices.
5. **Tax Savings**: Calculating depreciation correctly helps reduce tax liability.

Factors Affecting Depreciation

1. **Asset Cost**: Total amount spent on buying and preparing the asset for use.
2. **Useful Life**: Expected period the asset will be useful.
3. **Scrap Value**: Estimated residual value when the asset is no longer useful.

Common Methods of Depreciation Calculation

1. **Fixed Installment (Straight-Line) Method**: Charges the same amount of depreciation every year, based on the asset's original cost.
   - Formula without scrap value:

     Depreciation per year=Original CostUseful Life\text{Depreciation per year} = \frac{\text{Original Cost}}{\text{Useful Life}}Depreciation per year=Useful LifeOriginal Cost

   - Formula with scrap value:

     Depreciation per year=Original Cost - Scrap ValueUseful Life\text{Depreciation per year} = \frac{\text{Original Cost - Scrap Value}}{\text{Useful Life}}Depreciation per year=Useful LifeOriginal Cost - Scrap Value

2. **Diminishing Balance (Reducing Balance) Method**: Charges depreciation on the asset’s remaining balance each year, so the amount decreases annually.

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Difference between Fixed Instalment and Reducing Balance Method

Basis of Difference	Fixed Installment Method	Reducing Balance Method
Calculation of Depreciation	Calculated on the original cost.	Calculated on the remaining balance or opening book value.
Variation in Depreciation Amount	Depreciation amount remains the same every year.	Depreciation amount decreases each year.
Balance at End of Life	Balance is either zero or scrap value at end of asset's life.	Balance can never be zero at the end.
Rate of Depreciation	Generally has a lower rate.	Typically has a higher rate.
Burden on Profit & Loss	Not equitable in terms of repair and depreciation costs.	Provides an equitable burden across asset's life.
Applicability	Suitable for low-value assets with shorter life.	Suitable for assets that lose utility gradually and have high repair costs.
Validity	Not accepted by tax laws.	Approved by tax laws with tax rebates available.
Practicability	Same depreciation even if asset's value reduces.	Depreciation amount decreases as asset's utility declines.

Basic Journal Entries for Depreciation

1. **On Purchase of Asset**
   - **Entry**:
     - Asset A/c Dr
To Cash/Bank
2. **When Depreciation is Charged**
   - **Entry**:
     - Depreciation on Asset A/c Dr
To Asset A/c
3. **Transfer Depreciation to P&L Account**
   - **Entry**:
     - P&L A/c Dr
To Depreciation A/c
4. **On Sale of Asset (Profit)**
   - **Entry**:
     - Cash/Bank A/c Dr
To P&L A/c
To Asset A/c
5. **On Sale of Asset (Loss)**
   - **Entry**:
     - Cash/Bank A/c Dr
P&L A/c Dr
To Asset A/c

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Depreciation Methods with Special Journal Entries

1. Provision for Depreciation Method

- **To Provide Depreciation**:
  - Depreciation A/c Dr
    To Provision for Depreciation A/c
- **Transfer Depreciation to P&L**:
  - P&L A/c Dr
    To Depreciation A/c
- **On Sale of Asset**:
  - Provision for Depreciation A/c Dr
    To Asset A/c
- **Profit or Loss on Sale**:
  - **Profit**: Asset A/c Dr
    To P&L A/c
  - **Loss**: P&L A/c Dr
    To Asset A/c

2. Annuity Method

- **Depreciation and Interest**:
  - Calculate annual depreciation using the annuity table.
- **Entry**:
  - Depreciation A/c Dr
    Interest on Asset A/c Dr
    To Asset A/c

3. Depreciation Fund Method

- **Investment in Securities**:
  - Transfer annual depreciation to buy government securities.
- **Entry**:
  - Depreciation A/c Dr
    To Depreciation Fund A/c
- **Sale of Securities for Asset Renewal**:
  - Sell securities in the final year to renew the asset.

4. Depreciation Repairs & Renewals Fund Method

- **Annual Transfer**:
  - P&L A/c Dr
    To Depreciation Repairs & Renewals Fund A/c

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5. Insurance Policy Method

- **Premium Payment**:
  - P&L A/c Dr
    To Insurance Premium A/c
- **Policy Maturity for Asset Renewal**:
  - Receive lump-sum from policy for asset renewal.

6. Revaluation Method

- **Annual Revaluation**:
  - Depreciation A/c Dr
    To Asset A/c

7. Sum of the Year Digits Method

- **Formula**:
  - Depreciation=(Remaining YearsSum of Total Years)×(Cost - Scrap Value)\text{Depreciation} = \left(\frac{\text{Remaining Years}}{\text{Sum of Total Years}}\right) \times (\text{Cost - Scrap Value})Depreciation=(Sum of Total YearsRemaining Years)×(Cost - Scrap Value)

8. Machine Hour Rate Method

- **Calculation**:
  - Depreciation per Hour = Cost - Scrap ValueTotal Machine Hours\frac{\text{Cost - Scrap Value}}{\text{Total Machine Hours}}Total Machine HoursCost - Scrap Value
- **Journal Entry**:
  - Calculate and charge depreciation based on hours used.

9. Depletion Method

- **Calculation**:
  - Calculate depreciation per unit based on total estimated yield.

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Difference between Reserves & Provisions

S. No	Basis of Difference	Reserve	Provision
1	**Meaning**	A reserve is meant for meeting an unanticipated situation.	A provision is created for some specific object or known liability.
2	**Mode of Creation**	A reserve is created only out of profit. If there is no sufficient profit, a reserve cannot be created.	A provision is a charge against profit, created even if there is no profit.
3	**Time of Creation**	A reserve is created after ascertaining the profit.	A provision is created before ascertaining the profit or loss.
4	**Object**	Reserves strengthen the financial position and increase working capital.	Provisions are arrangements to provide funds for known liabilities.
5	**Utilization**	Reserves can be used to pay any liability or loss.	Provisions can be used only for the purpose they are created for.
6	**Distribution**	General reserves are available for profit distribution, like dividends.	Provisions cannot be used for profit distribution, such as dividends.
7	**Place in Accounting**	Reserves represent the excess of assets over liabilities.	Provisions help determine the real value of assets by accounting for liabilities.
8	**Presentation in Balance Sheet**	Reserves appear on the liabilities side.	Provisions are shown as a deduction from related assets or on the liabilities side.

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