KMBN-103: Financial Accounting& Analysis (Unit-2)

Accounting Standards:-

An accounting standard is a common set of principles, standards, and procedures that define the basis of financial accounting policies and practices.

- Accounting standards apply to the full breadth of an entity's Internal financial picture, including assets, liabilities, revenue, expenses, and shareholders' equity.
- External entities such as banks, investors, and regulatory agencies, count on accounting standards to ensure information about a given entity is relevant and accurate.
- Accounting standards improve the transparency of financial reporting in all countries.
- Accounting standards specify when and how economic events are to be recognized, measured, and displayed.
- Accounting standards ensure the financial statements from multiple companies are comparable. Because all entities follow the same rules, accounting standards make the financial statements credible and allow for more economic decisions based on accurate and consistent information.

Examples of an accounting standard include revenue recognition, asset classification, allowable methods for depreciation, what is considered depreciable, lease classifications, and outstanding share measurement.

Indian Accounting Standard (IND AS)

Indian Accounting Standard (abbreviated as **Ind-AS**) is the Accounting standard adopted by companies in India and issued under the supervision of Accounting Standards Board (ASB) which was constituted as a body in the year 1977. ASB is a committee under Institute of Chartered Accountants of India (ICAI) which consists of representatives from government department, academicians, other professional bodies. **ICAI is an independent body formed under an act of parliament.**

The Ind AS are named and numbered in the same way as the International Financial Reporting Standards (IFRS). National Financial Reporting Authority (NFRA) recommend these standards to the Ministry of Corporate Affairs (MCA). MCA has to spell out the accounting standards applicable for companies in India.

International Financial Reporting Standards (IFRS):-

IFRS are accounting standards issued by the IFRS Foundation and the International Accounting Standards Board (IASB). The IASB was founded on April 1, 2001, as the successor to the International Accounting Standards Committee (IASC). It is responsible for developing International Financial Reporting Standards (IFRS Standards), **previously known as International Accounting Standards (IAS)**

They constitute a standardised way of describing the company's financial performance and position so that company financial statements are understandable and comparable across international boundaries.They are particularly relevant for companies with shares or securities listed on a public stock exchange.

International Financial Reporting Standards (IFRS) are a set of accounting rules for the financial statements of public companies that are intended to make them consistent, transparent, and easily comparable around the world.

IFRS specify in detail how companies must maintain their records and report their expenses and income. They were established to create a common accounting language that could be understood globally by investors, auditors, government regulators, and other interested parties.

The standards are designed to bring consistency to accounting language, practices, and statements, and to help businesses and investors make educated financial analyses and decisions.

Qualitative characteristics of financial information:-

The Conceptual Framework for Financial Reporting defines the fundamental qualitative characteristics of financial information to be:

1. Relevance
2. Faithful representation
3. Comparability
4. Verifiability
5. Timeliness
6. Understandability

Elements of financial statements.

The Conceptual Framework defines the elements of financial statements to be:-

- **Asset**: A present economic resource controlled by the entity as a result of past events which are expected to generate future economic benefits
- **Liability**: A present obligation of the entity to transfer an economic resource as a result of past events
- **Equity**: The residual interest in the assets of the entity after deducting all its liabilities
- **Income**: increases in economic benefit during an accounting period in the form of inflows or enhancements of assets, or decrease of liabilities that result in increases in equity. However, it does not include the contributions made by the equity participants (for example owners, partners or shareholders).
- **Expenses**: decreases in assets, or increases in liabilities, that result in decreases in equity. However, these do not include the distributions made to the equity participants.

ASAF Accounting Standards Advisory Forum

List of International Financial Reporting Standards:-2021

IFRS 1 First-time Adoption of International Financial Reporting Standards

IFRS 2 Share-based Payment

IFRS 3 Business Combinations

IFRS 4 Insurance Contracts

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations

IFRS 6 Exploration for and Evaluation of Mineral Resources

IFRS 7 Financial Instruments: Disclosures

IFRS 8 Operating Segments

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IFRS 10 Consolidated Financial Statements

IFRS 11 Joint Arrangements

IFRS 12 Disclosure of Interests in Other Entities

IFRS 13 Fair Value Measurement

IFRS 14 Regulatory Deferral Accounts

IFRS 15 Revenue from Contracts with Customers

IFRS 16 Leases

IFRS 17 Insurance Contracts

IAS 1	Presentation of Financial Statements
IAS 2	Inventories
IAS 7	Statement of Cash Flows
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
IAS 10	Events after the Reporting Period
IAS 11	Construction Contracts

IAS 12	Income Taxes
IAS 16	Property, Plant, and Equipment
IAS 17	Leases
IAS 18	Revenue
IAS 19	Employee Benefits
IAS 20	Accounting for Government Grants and Disclosure of Government Assistance
IAS 21	The Effects of Changes in Foreign Exchange Rates
IAS 23	Borrowing Costs
IAS 24	Related Party Disclosures
IAS 26	Accounting and Reporting by Retirement Benefit Plans
IAS 27	Separate Financial Statements
IAS 28	Investments in Associates and Joint Ventures
IAS 29	Financial Reporting in Hyperinflationary Economies
IAS 32	Financial Instruments: Presentation
IAS 33	Earnings per Share
IAS 34	Interim Financial Reporting
IAS 36	Impairment of Assets
IAS 37	Provisions, Contingent Liabilities, and Contingent Assets

IAS 38	Intangible Assets
IAS 39	Financial Instruments: Recognition and Measurement
IAS 40	Investment Property
IAS 41	Agriculture

1) IFRS 1- *First-time Adoption of International Financial Reporting Standards*

It sets out the procedures that an entity must follow when it adopts IFRSs for the first time as the basis for preparing its general purpose financial statements. This IFRS grants limited exemptions from the general requirement to comply with each IFRS effective at the end of its first IFRS reporting period. There are many benefits of implementing IFRS in India in terms of economy, industry, and investors.

2) IFRS 2- *Share-Based Payment*

It requires an entity to recognize share-based payment transactions (example: granted shares, share options, or share appreciation rights) in its financial statements, also including transactions with employees or other parties to be settled in cash, other assets, or equity instruments of the entity. Specific requirements are included for equity-settled and cash-settled share-based payment transactions, as well as those where the entity or supplier has a choice of cash or equity instruments.

3) IFRS 3- *Business Combinations*

It outlines the accounting when an acquirer obtains control of a business (example: an acquisition or merger). Such business combinations are accounted for using the 'acquisition method', which generally requires assets acquired and liabilities assumed to be measured at their fair values at the acquisition date. The main advantage of IFRS is it facilitates the easy comparison of different companies, as data is presented on the same basis.

4) IFRS 4- *Insurance Contracts*

It applies, with limited exceptions, to all insurance contracts (including reinsurance contracts) that an entity issues and to reinsurance contracts that it holds. In light of the International Accounting Standard Board's comprehensive project on insurance contracts, the standard provides a temporary exemption from the requirements of some other IFRSs, including the requirement to consider International Accounting Standard- 8 Accounting Policies, Changes in Accounting Estimates and Errors when selecting accounting policies for insurance contracts.

5) IFRS 5- *Non-current Assets Held for Sale and Discontinued Operations*

It outlines how to account for non-current assets held for sale (or for distribution to owners). In general terms, assets held for sale are not depreciated, are measured at the lower of carrying amount and fair value fewer costs to sell, and are presented separately in the statement of financial position. Specific disclosures are also required for discontinued operations and disposals of non-current assets.

6) IFRS 6- *Exploration for and Evaluation of Mineral Resources*

It has the effect of allowing entities to adopt the standard for the first time to use accounting policies for exploration and evaluation assets that were applied before adopting IFRSs. It also modifies impairment testing of exploration and evaluation assets by introducing different impairment indicators and allowing the carrying amount to be tested at an aggregate level (not greater than a segment).

7) IFRS 7- *Financial Instruments: Disclosures*

It requires disclosure of information about the significance of financial instruments to an entity, and the nature and extent of risks arising from those financial instruments, both in qualitative and quantitative terms. Specific disclosures are required in relation to transferred financial assets and a number of other matters.

8) IFRS 8- *Operating Segments*

It requires particular classes of entities (essentially those with publicly traded securities) to disclose information about their operating segments, products and services, the geographical areas in which they operate, and their major customers. Information is based on internal management reports, both in the identification of operating segments and measurement of disclosed segment information.

9) IFRS 9- *Financial Instruments*

It is the International Accounting Standard Board's replacement of International Accounting Standard 39 Financial Instruments: Recognition and Measurement. It includes requirements for recognition and measurement, impairment, recognition, and general hedge accounting.

10) IFRS 10– *Consolidated Financial Statements*

It outlines the requirements for the preparation and presentation of consolidated financial statements, requiring entities to consolidate entities it controls. Control requires exposure or rights to variable returns and the ability to affect those returns through power over an investee.

11) IFRS 11– *Joint Arrangements*

It outlines the accounting by entities that jointly control an arrangement. Joint control involves the contractually agreed sharing of control and arrangements subject to joint control are classified as either a joint venture; representing a share of net assets and equity accounted or a joint operation; representing rights to assets and obligations for liabilities, accounted for accordingly.

12) IFRS 12- *Disclosure of Interests in Other Entities*

It is a consolidated disclosure standard requiring a wide range of disclosures about an entity's interests in subsidiaries, joint arrangements, associates and unconsolidated 'structured entities'. Disclosures are presented as a series of objectives, with detailed guidance on satisfying those objectives.

13) IFRS 13-*Fair Value Measurement*

It applies to IFRSs that require or permit fair value measurements or disclosures and provides a single IFRS framework for measuring fair value and requires disclosures about fair value measurement. The Standard defines fair value on the basis of an exit price notion and uses a fair value hierarchy, which results in a market-based rather than entity-specific measurement.

14) IFRS 14-*Regulatory Deferral Accounts*

It permits an entity which is a first-time adopter of International Financial Reporting Standards to continue to account, with some limited changes, for ‘regulatory deferral account balances’ in accordance with its previous GAAP, both on initial adoption of IFRS and in subsequent financial statements. Regulatory deferral account balances, and movements in them, are presented separately in the statement of financial position and statement of profit or loss and other comprehensive income, and specific disclosures are required.

15) IFRS 15 – *Revenue From Contract*

It specifies how and when an IFRS reporter will recognize revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard provides a single, principles-based five-step model to be applied to all contracts with customers. It applies to an annual reporting period beginning on or after 1 January 2018.

16) IFRS 16 – *Lease Accounting*

It specifies how an IFRS reporter will recognize, measure, present, and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16’s approach to lessor accounting substantially unchanged from its predecessor, International Accounting Standard- 17. It applies to annual reporting periods beginning on or after 1 January 2019.

17) IFRS 17: *Insurance Contract*

IFRS 17 is applicable for yearly reporting periods starting on or after 1st January 2021. This must be accommodated with IFRS 9 and IFRS 15 from the list of IFRS standards, permitted application earlier. The insurance contract consists of both a service and a financial instrument contracts. Many such insurance contracts will ultimately generate cash flow with considerable variability over a long span.

Difference between IFRS (formally IAS-International Accounting Standard) & IND AS Indian Accounting Standard:-

IFRS stands for International Financial Reporting Standards, It is prepared by the IASB (International Accounting Standards Board). It is used in around 144 countries and is regarded as one of the most popular accounting standards.

IND AS is also known as Indian Accounting Standards or Indian version of IFRS. Indian AS or IND AS is used in the context of Indian companies.

Let us look at some of the points of difference between the IFRS and IND AS.

IFRS	IND AS
Definition	
IFRS stands for International Financial Reporting Standards, it is an internationally recognised accounting standard	IND AS stands for Indian Accounting Standards, it is also known as India specific version of IFRS
Developed by	
IASB (International Accounting Standards Board)	MCA (Ministry of Corporate Affairs)
Followed by	
144 countries across the world	Followed only in India
Disclosure	
Companies complying with IFRS have to disclose as a note that the financial statements comply	Such a disclosure is not mandatory for companies complying with Indian Accounting
Financial Statement Components	
It includes the following 1. Statement of financial position 2. Statement of profit and loss 3. Statement of changes in equity for the period 4. Statement of cash flows for the period	It includes the following: 1. Balance Sheet 2. Profit and loss account 3. Cash flow statement 4. Statement of changes in equity 5. Notes to financial statements 6. Disclosure of accounting policies
Balance Sheet Format	
Companies complying with IFRS need have specific guidelines for preparing balance sheet with assets and liabilities to be classified as current and non-current	Companies complying with IND AS need have no such requirements for balance sheet format, but the guidelines are defined for presenting balance sheet

Double Entry System of Accounting:-

A double-entry bookkeeping system is where a corresponding entry is made for every transaction, i.e. debits and credits. The basis of the double-entry bookkeeping system is that every transaction has two parts and affects two ledger accounts. The double-entry system of bookkeeping deals with two or more accounts for every business transaction.

The principles to be followed while recording the double-entry system of accounting are as follows:

- Debit is written to the left, credit on the right
- Every debit must have a corresponding credit
- Debit receives the benefit, and credit gives the benefit

There are rules to be kept in mind while posting the double-entry transactions The following are the rules for the different types of accounts:

Types of Account / Golden Rules of Accounting

1. **Debit the receiver, credit the giver.**
2. **Debit what comes in, credit what goes out**
3. **Debit all expenses and losses and credit all incomes and gains**

3 Golden Rules of Accounting	Real Account	Personal Account	Nominal Account
Debit >	What Comes In	The Receiver	Expenses and Losses
Credit >	What Goes Out	The Giver	Incomes and Gains

Types of Account:-

Personal Account

A personal account is a general ledger account. All accounts related to persons, whether natural persons like individuals or artificial persons like companies, fall in this category.

In the case of a personal account, when a business receives something from another business or individual, the first business becomes the receiver, and the second business or individual from which it was received becomes the giver.

Golden Rule 1 says, **Debit the receiver, credit the giver.** Applying the rule to our example, the books should reflect a debit on the personal account and a credit on the business account.

Let's take the example of buying a gift from a gift shop. In your account, the transaction will reflect as such.

Date	Account	Debit	Credit
XXXX	Purchase Account	Rs.5000	
	Gift Shop		Rs.5000

Real Account

In a real account, the closing balance is retained and carried forward at the end of the year. These carried forward amounts then become the opening balances for the next year. These accounts usually pertain to assets, liabilities and equity.

Golden Rule 2 says, **Debit what comes in, Credit what goes out.** In a real account, if a business receives something of value (property or goods), it is represented in the books as debited. If something of value goes out from the business it is represented in the books as credited. An example is given below.

The example below is of a furniture purchase worth Rs. 10000 in cash.

Date	Account	Debit	Credit
XXXX	Furniture Account	Rs. 10000	
	Cash Account		Rs. 10000

Nominal Account

A nominal account is the type of account in which all accounting transactions are stored for one fiscal year, transferring balances to permanent accounts at the end of a fiscal year. This allows for resetting the balances to zero and starting afresh. Nominal accounts are usually related to Revenues, Expenses, Gains and Losses.

Golden Rule 3 says,**Debit all expenses and losses, credit all incomes and gains.**If a business incurs a loss or expense, then the books' respective entry is represented as a debit. If the business earns a profit or gains income by way of rendering services, then the entry in the book is represented as credit. An example below demonstrates this. A business pays rent for the premises it holds and is an expense for the business.

Date	**Account**	**Debit**	**Credit**
XXXX	Rent account	Rs.12000	
	Cash Account		Rs.12000

Format of Journal Entries

Journal entries in the books of XYZ Ltd.

Date	Particulars	Ledger Folio	(Dr.) Amount Rs.	(Cr.) Amount Rs.
	Debit A/c ....Dr. To Credit A/c (Being...)			

Compound Entries

When transactions **affect more than two accounts**, we make **compound entries**. These are common when the recordings are related in nature or happen during the same day.

Remember: debits and credits must always be equal. The principle stays the same, there are just more accounts that change.

Example.

XYZ company decides to buy new computer software for Rs1,000 from ABC LTD. They pay Rs.700 in cash right away and agree to pay the remaining Rs.300 later.

First, we figure out which accounts have changed and by how much. In this scenario, those are three:

- Asset account, which increases by Rs1,000 when buying the new computer software.
- Cash account, which decreases Rs.700 in Cash from paying.
- ABC LTD. account, which increases Rs300 from the remaining unpaid amount.

The next step is to translate them into debit and credit.

Assets increase when debited, so Equipment will be debited for Rs1,000. Expenses decrease when credited, so Cash will be credited for Rs.700. Liabilities increase when credited, so ABC LTd. will also be credited for Rs.300.

Prepare a journal of Manohar Lal & sons from the following transactions:-

2018		**Amount**
March 1	Manohar Lal & Sons started a business with cash	60,000
March 2	Purchased furniture for cash	10,000
March 4	Purchased goods for cash	25,000
March 5	Bought goods from Kamlesh	15,000
March 10	Paid cash to Kamlesh	15,000
March 16	Purchased goods from Sohan	6,000
March 18	Purchased goods from Sohan for cash	8,000
March 20	Paid rent for the office	1,000

Journal Entries In the Books of Manohar Lal & sons for the month of ....

Date	Particular		L.F.	Amount Dr.	Amount Cr.
March 1	Cash A/c	Dr.	-	60,000	-
	To Capital A/c (Business started with cash)	-	-	-	60,000
March 2	Furniture A/c	Dr.	-	10,000	-
	To Cash A/c (Furniture bought with cash)	-	-	-	10,000
March 4	Purchases A/c	Dr.	-	25,000	-
	To Cash A/c (Bought goods with cash)	-	-	-	25,000
March 5	Purchases A/c To Kamlesh's A/c (Bought goods from Kamlesh credited)	Dr.	-	15,000	15,000
March 10	Kamlesh's A/c	Dr.	-	15,000	-
	To Cash A/c (Cash payable to Kamlesh)	-	-	-	15,000
March 16	Purchases A/c	Dr.	-	6,000	-
	To Sohan's A/c (Goods purchases from Sohan)	-	-	-	6,000
March 18	Purchases A/c	Dr.	-	8,000	-
	To Cash A/c (Goods bought in cash from Sohan)	-	-	-	8,000
March 20	Rent A/c	Dr.	-	1,000	-
	To Cash A/c (Office rent payable)	-	-	-	1,000

Rules of Journalizing

Below are the equation accounting approach which accounting follows to record the transactions.

Assets	Increase in Assets	Debit (Dr.)
	Decrease in Assets	Credit (Cr.)
Capital	Increase in Capital	Credit (Cr.)
	Decrease in Capital	Debit (Dr.)
Liabilities	Increase in Liabilities	Credit (Cr.)
	Decrease in Liabilities	Debit (Dr.)
Revenue	Increase in Revenue	Credit (Cr.)
	Decrease in Revenue	Debit (Dr.)
Expenses	Increase in Expenses	Debit (Dr.)
	Decrease in Expenses	Credit (Cr.)

Ledger

A ledger account has a listing of all general accounts in the accounting system's chart of accounts. The purpose of ledger account is to organize the financial information which is needed to prepare financial statements of a business.

The book wherein various entries of the journal are posted in brief permanently according to **debit and credit** under separate heads of accounts is called ledger.

Business organizations need to write and prepare **ledger account** wherein **all the transactions** are recorded permanently under different heads of accounts.

Characteristics Of Ledger Accounts

The following are characteristics of ledger account;

1. There are two sides of a ledger account, one is debit which is seen on left side of the account while the other is credit which is the right side of the account.

2. The debit entries of all financial transactions are recorded on the debit side while the credit entries of all financial transactions are recorded on the credit side of the account.

3. The difference between the debit and the credit side represents the balance. A debit balance represents the excess of debit side over credit side while the credit balance shows the excess of credit side are over debit side.

4. At the end of the period, both sides are balanced and the excess balance is written over the closing balance at the end of the period.

5. At the end of the accounting period, the closing balance is forwarded to the following year as a beginning balance for the new year.

Transactions ⇒ Journal ⇒ Ledger

5 simple steps for writing and preparing ledger are:-

1. Drawing the Form – Get pen and paper, start drawing the ledger account.
2. Posting transactions from journal to respective ledger account.
3. Folioing – Put the page number for a journal entry on the ledger account's folio column.
4. Casting – Separating debit and credit amount.
5. Balancing – find the difference between debit and credit to get debit or credit balance of the account.

1. Drawing the Form – Get pen and paper, Start Drawing the Ledger Account.

Every leaf of the account is divided into two equal parts by a bold vertical line or two sharp vertical lines. The left side of it is the debit side and the right side is the credit side.

Thereafter, both sides are again divided into four columns i.e., this is divided into eight columns having four on the debit side and four on the credit side.

In the first column of both the sides' dates, the second particulars, and the third journal folio and the fourth amount are written.

2. Posting Transactions from Journal to Respective Ledger Account.

The act of transferring the transactions from the journal to the respective accounts of the ledger is called posting. The two accounts involved in each transaction are maintained in the ledger.

A debit account of the journal is posted on the debit side of that account and the credit account of the journal is posted on the credit side of that account.

In this regard, it is to be carefully noted that at the time of posting in the debit side of the ledger account, credit account of the journal is to be written in particular column and in the credit side of the ledger account debit account of that journal is to be written in particular column.

3. Folioing – Put the Page Number for a Journal Entry on the Ledger Account's Folio Column.

The page of the journal from which the journal entries are transferred to the particular ledger account that page number is written in the folio column of a ledger account and the page of the ledger wherein the account is posted the number of that page is written in the journal in the ledger folio column of the journal.

In this way writing of page number of the journal in the ledger and that of the ledger in the journal is called folioing.

4. Casting – Separating Debit and Credit Amount.

The amount of debit and credit of each ledger account is totaled separately on both sides. In this way totaling of debit and credit is called casting.

5. Balancing – Find the Difference between Debit and Credit to get Debit or Credit balance of the Account.

After the totaling of debit and credit of ledger accounts, it shows that the total of both sides is made equal putting the difference on both sides the account is considered balanced.

In this case, nothing is left to be done. But if the total of both sides is unequal, in that case, the difference is to be determined.

Thereafter the amount of difference is added in the deficit side to equalize both sides. This sort of difference between the two sides of accounts is called balance.

The act of equalizing the total of both the sides by adding debit balance in the credit side and the credit balance in the debit side is called balancing.

Debit balance

If the total amount of the debit side is greater than the total amount of credit side of the ledger than the difference between both sides is called debit balance.

For example,

the total of the debit of a particular ledger account is Rs.10,000 and the total of credit of that ledger account is $8,000, -then the difference between these two sides amounting to Rs. 2,000 is a debit balance.

As per the rule of **debit and credit under the double-entry system**, all expenditures and assets accounts show debit balance.

Therefore debit balances of ledger accounts mean expenditure and assets.

Credit balance

On the other hand, if the total of credit money column of a particular ledger account is greater than that of debit money column, the balance is called credit balance.

For example,

the total credit money column of a particular account is Rs. 5,000 and that of the debit money column is Rs. 4,000, the difference between these two amounts Rs. 1,000 is a credit balance.

All income and liability accounts always show credit balance i.e. credit balances of ledger account mean incomes and liabilities.

Specimen of ledger accounts

A general ledger account has two sides debit (left part of the account) and credit (right part of the account). Each of the general ledgers debit and credit side has four columns.

- Date
- Particulars
- Journal folio i.e. reference number of the page from where the entries are taken for posting and
- Amount

Date	**Particulars**	**Journal Folio**	**Amount (Rs.)**	**Date**	**Particulars**	**Journal Folio**	**Amount (Rs.)**

Example:-

The following transactions in journal entry are posted them into ledger account:

2017	**Particulars**
Jan. 1	Mr. Jamal started business with cash $1,50,000
2	He purchased furniture for amount $30,000

3	He purchase goods for $50,000
5	He sold goods in cash $50,000
6	He paid salaries to amount $20,000

Solution:

Journal

Date	Particular	L.F	Amount	Amount
2017				
Jan. 1	Cash A/C ……………………………………………..Dr. Capital (Jamal invested cash and capital)	9 11	1,50,000	1,50,000
2	Furniture A/C…………………………………………Dr. Cash A/C (furniture purchased cash)	13 9	30,000	30,000
3	Purchases A/C……………………………………..Dr. Cash A/C (Goods purchased cash amount)	15 9	50,000	50,000
5	Cash A/C……………………………………………Dr. Sales A/C (Sold goods cash amount)	9 17	50,000	50,000
6	Salaries A/C…………………………………………..Dr. Cash A/C Return (Salaries paid to employee)	19 9	20,000	20,000

Ledger

Cash Account (No.9)

Date	Particular	J.R	Amount	Date	Particulars	J.R	Amount
2017				2005			
Jan.1	Capital A/C	1	1,50,000	Jan.2	Furniture A/C	1	30,000
Jan.5	Sales A/C	1	50,000	Jan.3	Purchases A/C	1	50,000
				Jan.6	Salaries A/C	1	20,000
					Balance c/d		**1,00,000**
	Total		**2,00,000**		**Total**		**2,00,000**

Capital Account (No.11)

Date	Particular	J.R	Amount	Date	Particulars	J.R	Amount
2017				2017			
Jan.6	**Balance c/d**		**1,50,000**	Jan.1	Cash A/C	1	1,50,000
	Total		**1,50,000**		**Total**		**1,50,000**

Furniture Account (No.13)

Date	Particular	J.R	Amount	Date	Particulars	J.R	Amount
2017				2017			
Jan.2	Cash A/C	1	30,000	Jan.6	**Balance c/d**		**30,000**

	Total		**30,000**		**Total**		**20,000**

Purchases Account (No.15)

Date	Particular	J.R	Amount	Date	Particulars	J.R	Amount
2017				2017			
Jan.3	Cash A/C	1	50,000	Jan.6	**Balance c/d**		**50,000**
	Total		**50,000**		**Total**		**50,000**

Sales Account (17)

Date	Particular	J.R	Amount	Date	Particulars	J.R	Amount
2005				2005			
Jan.6	**Balance c/d**		**50,000**	Jan.5	Cash A/C	1	50,000
	Total		**50,000**		**Total**		**50,000**

Salaries Account (19)

Date	Particular	J.R	Amount	Date	Particulars	J.R	Amount
2005				2005			
Jan.6	Cash A/C	1	20,000	Jan.6	**Balance c/d**		**20,000**
	Total		**20,000**		**Total**		**20,000**

Trial Balance

A trial balance is a bookkeeping worksheet in which the balance of all ledgers are compiled into debit and credit account column totals that are equal. A company prepares a trial balance periodically, usually at the end of every reporting period. The general purpose of producing a trial balance is to ensure the entries in a company's bookkeeping system **are mathematically correct.**

Trial Balance is a technique for checking the **accuracy** of the debit and credit amounts recorded in the **various ledger accounts**. It is basically a statement that exhibits the total of the debit and credit balances recorded in various accounts of ledger. Accordingly, Trial Balance is prepared to check the accuracy of the various transactions that are posted into the ledger accounts. It is certainly one of the important accounting tools as it reveals the final position of all accounts. Further, it is used in preparing the final accounting statements of the business.

Rules for Preparation of Trial Balance

While preparation of trial balances we must take care of the following rules/points

1] The balances of the following accounts are always found on the debit column of the trial balance

- Assets
- Expense Accounts
- Drawings Account
- Cash Balance
- Bank Balance
- Any losses

2] And the following balances are placed on the credit column of the trial balance

- Liabilities
- Income Accounts
- Capital Account
- Profits

You must note that as per the accounting principle:

- **All assets, expenses and receivables must have debit balances and all**
- **Liabilities, incomes and payables must have credit balances**

Steps in Preparation of Trial Balance

1. Calculate the Balances of Each of the Ledger Accounts

Business transactions are first recorded in the form of journal entries following the basic accounting principles. These journal entries then go into the ledger accounts involved in the various business transactions.

For instance, consider the cash account of Kapoor Pvt Ltd in the above example. The cash transactions are recorded and the cash account is closed with the remaining debit balance of Rs 6,50,000 as on May 1, 2018. Likewise, balances of other ledger accounts are ascertained and accordingly the accounts are closed with the remaining debit or credit balances.

2. Record Debit or Credit Balances in Trial Balance

The remaining debit or credit balances in various accounts of ledger as ascertained above are then recorded in the Trial Balance. The balances of each of the accounts of ledger are recorded in the debit or the credit columns as the case may be.

For example, the remaining debit cash balance as on May 1, 2018 is recorded in the debit column of the trial balance. Further, the remaining credit balance of capital account of Rs 8,00,000 is recorded in the credit column of the trial balance. Similarly, the remaining debit or credit balances of all the accounts of ledger are recorded in the debit or credit columns of trial balance respectively.

3. Calculate Total of The Debit Column

Ascertain the total of the debit column. This is done after recording all the debit balances of the various accounts of ledger put into debit column of Trial Balance.

For instance, consider the total of the debit column of the Trial Balance of Rs 10,20,000. This is calculated after recording all the closing debit balances of various accounts of ledger. These accounts include cash, stock, furniture, drawings etc.

4. Calculate Total of The Credit Column

Ascertain the total of the credit column. This is done after recording all the credit balances of the various accounts of ledger put into credit column of Trial Balance.

For instance, consider the total of the credit column of the Trial Balance of Rs 10,20,000. This is calculated after recording all the closing credit balances of various accounts of ledger. These accounts include capital, interest etc.

5. Check if Debit is Equal To Credit

Finally, you need to check if the total of the debit column matches the total of the credit column. As specified earlier, trial balance is prepared to check the accuracy of the debit and credit balances of various accounts of ledger. Both the debit and credit columns of the Trial Balance must tally since every debit has every credit. However, it is an indication that there were some errors made while recording transactions in ledger or trial in cases where they are not equal.

Trial Balance Example

Kapoor Pvt Ltd entered into the following transactions for the month April 30, 2018.

April 1, 2018 – Kapoor Pvt Ltd started business with a capital of Rs 8,00,000
April 4, 2018 – Bought goods from Singhania Pvt Ltd on credit for Rs 2,00,000
April 5, 2018 – Sold goods to M/s Khanna for Rs 2,50,000
April 6, 2018 – Cash purchases Rs 2,50,000
April 8, 2018 – Cash sales Rs 1,50,000
April 10, 2018 – Goods returned to Singhania Pvt Ltd Rs 20,000
April 11, 2018 – Purchased furniture for Rs 1,50,000
April 12, 2018 – Cash paid to Singhania Pvt Ltd Rs 1,20,000
April 13, 2018 – Goods returned by M/s Khanna Rs 30,000
April 15, 2018 – Goods taken by Kapoor Pvt Ltd for private use Rs 30,000
April 16, 2018 – Cash received from M/s Khanna Rs Rs 1,20,000
April 17, 2018 – Kapoor Pvt Ltd took loan from M/s Sahani Rs 3,00,000
April 18, 2018 – Salary paid Rs 50,000
April 19, 2018 – Purchased stationery for Rs 10,000
April 20, 2018 – Money paid to M/s Sahani for loan Rs 1,80,000
April 21, 2018 – Interest received Rs 40,000

Cash Account					
Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
1/4/2018	To Capital	8,00,000	6/4/2018	By Purchases	2,50,000
8/4/2018	To Sales	1,50,000	11/4/2018	By Furniture	1,50,000
16/4/2018	To M/s Khanna	1,20,000	12/4/2018	By Singhania	1,20,000
17/4/2018	To M/s Sahani	3,00,000	18/4/2018	By Salary	50,000
21/4/2018	To interest	40,000	19/4/2018	By Stationery	10,000
			20/4/2018	By M/s Sahani	1,80,000

			30/4/2018	By Balance c/d	6,50,000
		14,10,000			14,10,000
1/5/2018	To Balance b/d	6,50,000			

Capital Account					
Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
30/4/2018	To Balance c/d	8,00,000	1/4/2018	By Cash	8,00,000
		8,00,000			8,00,000
			1/5/2018	By Balance b/d	8,00,000

Stock Account					
Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
4/4/2018	To Singhania Pvt Ltd	2,00,000	5/4/2018	By M/s Khanna	2,50,000
6/4/2018	To Cash	2,50,000	8/4/2018	By Cash	1,50,000
13/4/2018	To M/s Khanna	30,000	10/4/2018	By Singhania Pvt Ltd	20,000

17/4/2018			15/4/2018	By Drawings	30,000
			30/4/2018	By Balance c/d	30,000
		4,80,000			4,80,000
1/5/2018	To Balance b/d	30,000			

Singhania Pvt Ltd's Account

Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
10/4/2018	To Goods Return	20,000	4/4/2018	By Stock	2,00,000
12/4/2018	To Cash	1,20,000			
30/4/2018	To Balance c/d	60,000			
		2,00,000			2,00,000
			1/5/2018	By Balance b/d	60,000

M/s Khanna Account

Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
5/4/2018	To Stock	2,50,000	13/4/2018	By Goods Return	30,000

			16/4/2018	By Cash	1,20,000
			30/4/2018	By Balance c/d	1,00,000
		2,00,000			2,00,000
1/5/2018	To Balance b/d	1,00,000			

Furniture Account

Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
11/4/2018	To Cash	1,50,000	30/4/2018	By Balance c/d	1,50,000
		1,50,000			1,50,000
1/5/2018	To Balance b/d	1,50,000			

Drawings Account

Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
30/4/2018	To Stock	30,000	15/4/2018	By Balance c/d	30,000
		30,000			30,000
1/5/2018	By Balance b/d	30,000			

M/s Sahani Account

Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
20/4/2018	To Cash	1,80,000	17/4/2018	By Cash	3,00,000
30/4/2018	To Balance c/d	1,20,000			
		3,00,000			3,00,000
			1/5/2018	By Balance b/d	1,20,000

Salary Account

Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
18/4/2018	To Cash	50,000	30/4/2018	By Balance c/d	50,000
		50,000			50,000
1/5/2018	To Balance b/d	50,000			

Stationery Account

Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount

19/4/2018	To Cash	10,000	30/4/2018	By Balance c/d	10,000
		10,000			10,000
1/5/2018	To Balance b/d	10,000			

Interest Account

Dr.			Cr.		
Date	Particulars	Amount (in Rs)	Date	Particulars	Amount
19/4/2018	To Balance c/d	40,000	21/4/2018	By Cash	40,000
		40,000			40,000
			1/5/2018	By Balance b/d	40,000

Trial Balance of Kapoor Pvt Ltd As On April 31, 2018

Particulars	Amount (Debit)	Amount (Credit)
Cash	6,50,000	–
Capital	–	8,00,000
Stock	30,000	–
Singhania Pvt Ltd	–	60,000

M/s Khanna	1,00,000	–
Furniture	1,50,000	–
Drawings	30,000	–
M/s Sahani	–	1,20,000
Salary	50,000	–
Stationery	10,000	–
Interest	–	40,000
Total	**10,20,000**	**10,20,000**

Suspense Account

Although bookkeeping is supposed to be accurate, it might happen that some errors are made. Obviously, it will be necessary to find out why and correct the mistake. If the error cannot be found, it is necessary to insert a Suspense Account. This account is created to make the Trial Balance equal on both sides, in other words, to balance. If the error is not found before the financial statements are prepared, the Suspense Account will be included on the Balance Sheet as either a current asset or a current liability.

Here are its basic characteristics:

- intermediate
- temporary
- resolve problem/ambiguity
- zero balanced by posting to correct account
- balance indicated transactions in suspense/resolution
- track problems/errors.

Example

Trial balance as on 31st March, 2017

S. No.	Name of account	L.F.	Debit balance	Credit balance
1	Discount allowed		250	
2	Cash in hand		4,200	
3	Capital			50,000
4	Salaries		12,000	
5	Furniture		7,500	
6	Loan borrowed			7,000
7	Lighting		12,000	
8	Commission paid		3,000	
9	Purchases		29,050	
10	Sales			35,000
11	Suspense account		24,000	
	Total		92,000	92,000

The Suspense Account is added to the end of a Trial Balance because a bookkeeper of a business is unable to balance the Trial Balance as the error or errors cannot be found quickly (for the time being, it cannot be found, but maybe we can find the error). The suspense account will have a debit or credit balance, depending on which side we are short. This will make both columns balance. Here, we are putting in the errors which led to the Trial Balance not balancing.

Since the credit column was too high, we added a balancing Suspense Account with a $24,000 debit balance. If it had been the other way around – with the debit column being too high – we would have added this amount to the credit column.