

Accounting Work Book

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Learn Accounting Logically and Practically

Zaheer Swati

"There's no business like show business, but there are several businesses like accounting" *David Letterman*

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Dedicated To

Abdul Rehman Khan

&

Vareesha Noor



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ACCOUNTING BASICS

1.1 Definitions of Accounting

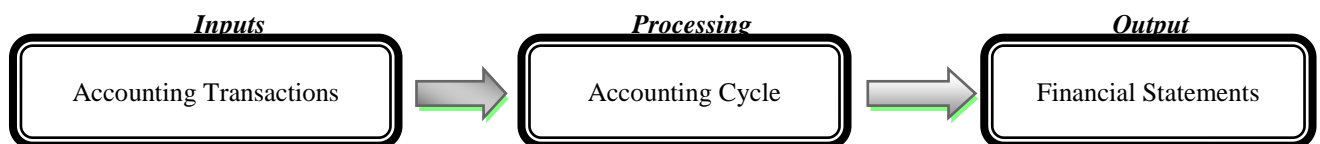
- Accounting is the language of the business
- Language is a way to communicate ideas or information, so in this way accounting is considered a way or path in business studies in order to communicate different aspects of business financial matters
- For instance, a manager says that his/her organization gain profit, so all respondents are easily understand that his organization get some thing in the form of money/value. In this example the word profit is a term of business language.

Def According to American Institute of Certified Public Accountants (AICPA), *Accounting is an art of recording classifying and summarizing in a significant manner and in terms of money, transactions and events which are, in part at least, of a financial character, and interpreting the results thereof.*

Def Accounting Principles Board (APB) defined Accounting in the following words. *Accounting is a services activity. Its function is to provide quantitative information primarily financial in nature, about economic entities that is intended to be useful in making economic decisions in making reasoned choices among alternative courses of action.*

Def American Accounting Association 1966 (AAA) defines accounting *as the process of identifying, measuring, and communicating economic information to permit informed judgment and decisions by the use of information.*

FOCUS In other context, *it is systematic process of recording, classifying and summarizing economic event in terms of money in order to facilitate economic decision makers.* So in this point of view this subject is a sequence of different steps in order to produce information which facilitate in the way of business decisions.



1.2 Forms of Accounting

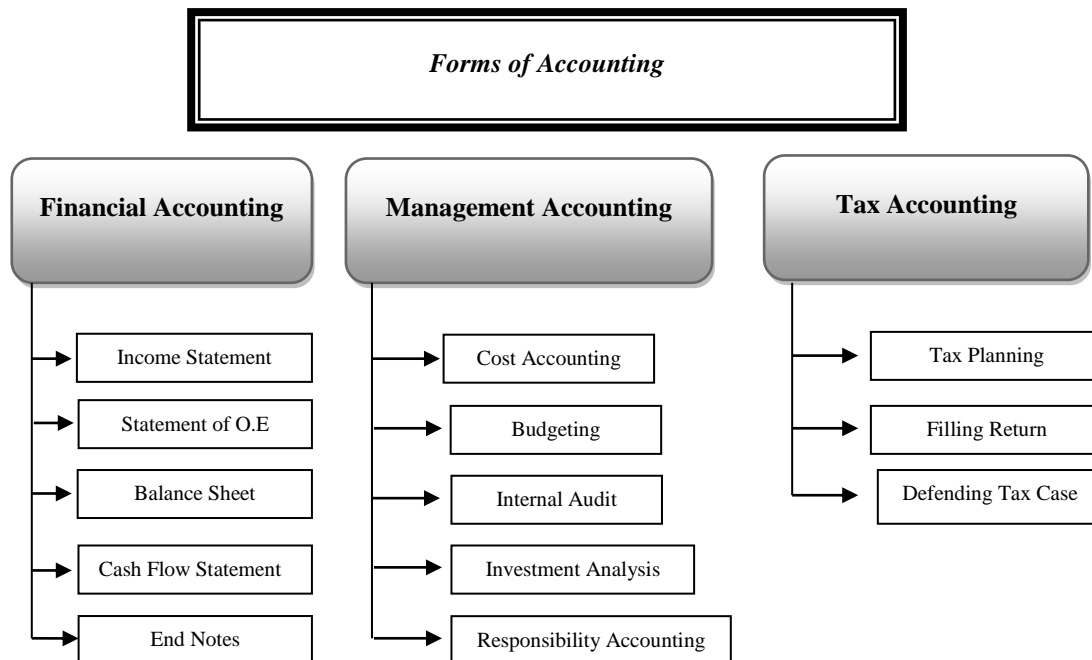
- Just as there are many types of economic decisions, there are many types of accounting information
- Financial Accounting, Management Accounting and Tax accounting often are describing three types of accounting information that are widely used business decisions

1.2.1 Financial Accounting

- ❖ Financial Accounting refers to information describing the financial resources, obligations and activities of an economic entity
- ❖ It is the maintenance of daily record of all financial transactions in such manner that it would help in the preparation financial statements
- ❖ Financial Accounting information is designed primarily to assist investors and creditors
- ❖ Accounting information also used for preparation of income tax return
- ❖ Financial Accounting information is used for so many purposes that it often is called “General-Purpose Accounting
- ❖ End results of Financial Accounting are financial statements

1.2.2 Management Accounting

- ✓ Management Accounting is meant specifically to assist the management in its operational and strategic planning
- ✓ This objective is achieved through preparation periodic reports about product, activities, departments and individuals
- ✓ Cost Accounting and Responsibility Accounting are the two significant parts of management accounting
- ✓ The most important role of Management Accounting is to set targets in the form of budget or standards, measure the actual performance and then make variance
- ✓ It is specific purpose accounting



1.2.3 Tax Accounting

- ❖ The financial statements are prepared according to the general accepted accounting principles (GAAP), International Accounting Standards (IAS), International Financial Reporting Standards (IFRS) and/or prevailing rules of country
- ❖ Since these rules and regulation allow flexibility in the accounting treatment of different items, some of them may not be acceptable to tax authorities
- ❖ Taxable profit must be calculated according to the tax laws of country, based on information provided by the financial statements
- ❖ The preparation of tax returns has therefore become a specialized field. Every enterprise would like to minimize tax return. This required tax planning

1.3 Users of Financial Information

- ✓ Accounting is the information system that identifies, records, and communicates the economic events of an organization to interested users
- ✓ Accounting information is needed by two sets of parties, which are internal and external
- ✓ Internal users are associated with management of the organization
- ✓ The external users consist of several explicit groups which are outside the organization and has interest (financial and non-financial) in an organization

1.3.1 Internal Users

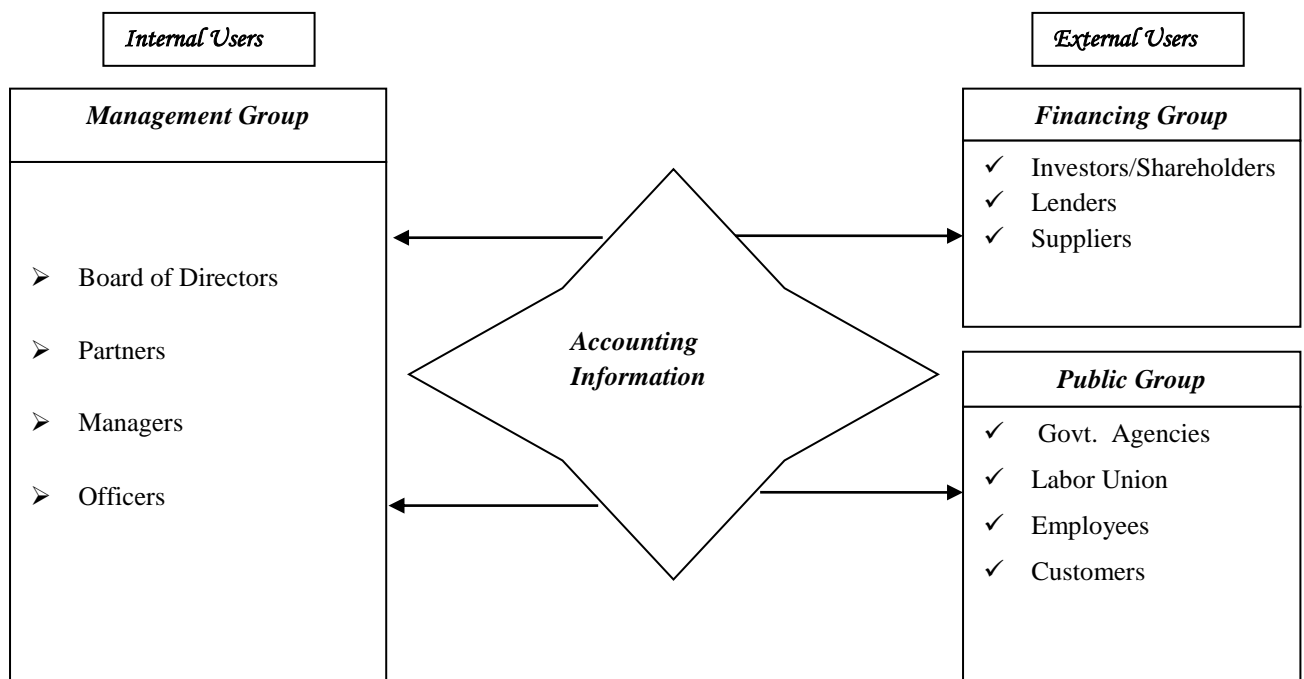
Internal users of accounting are parties who have directly connected with a company

- Internal users require financial statements to make important business decisions that affect its continued operations
- Financial analysis is then performed on these statements to provide management with a more detailed understanding of the figures
- Financial accounting as well as management accounting use for internal purpose

1.3.2 External Users

External users of accounting are potential investors, customers, banks, government agencies and other parties who are outside the business but need financial information about the business for a diverse number of reasons

- Prospective investors make use of financial statements to assess the viability of investing in a business
- Financial institutions (banks and other lending companies) use financial information to decide whether to grant a company with fresh working capital or extend debt securities (such as a long-term bank loan or debenture) to finance expansion and other significant expenditures
- Government entities (Tax Authorities) need financial statements to ascertain the accuracy of taxes and other duties declared and paid by a company
- Media and the general public are also interested in financial statements for a variety of reasons



1.4 Purpose of Accounting

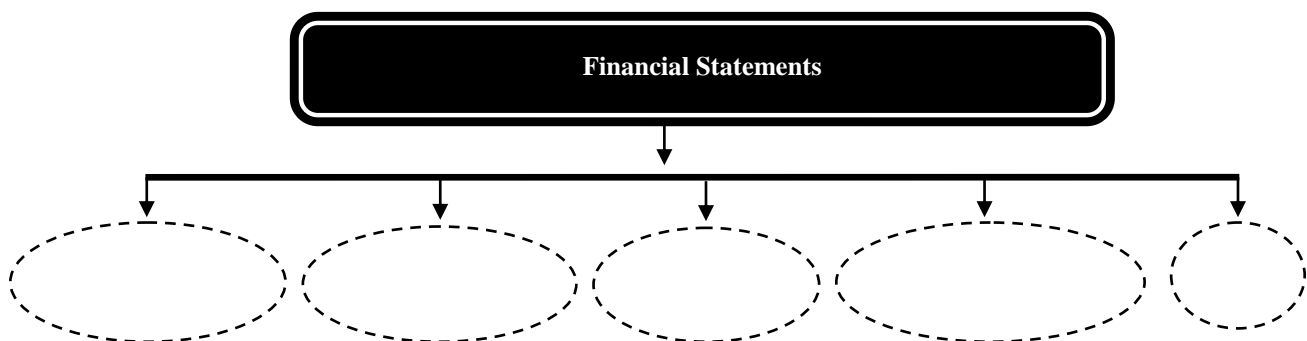
- The purpose of accounting is to provide the information that is needed for sound economic decision making
- The main purpose of financial accounting is to prepare financial statements that provide information about organization
- Financial accounting is performed according to GAAP in America and IAS/IFRS in rest of countries with in the laws and rules of particular country

1.5 Approaches of Accounting

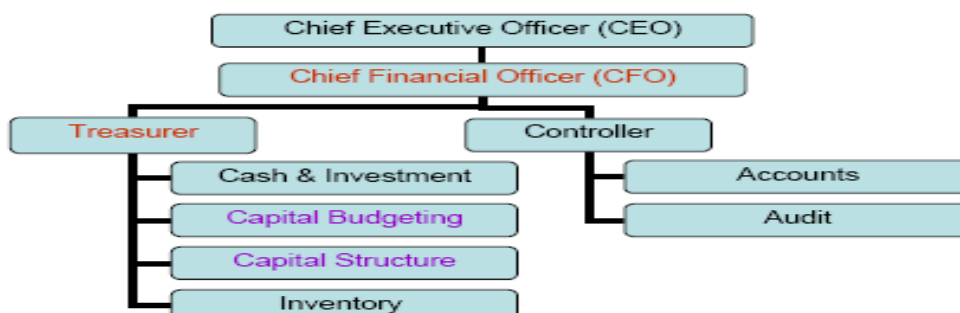
Approaches of Accounting	
American or Modern approach	British or English or Conventional approach
American Approach	British Approach
Account Receivables	Sundry Debtors or Debtors, Book Debts
Account Payable	Sundry Creditors or Creditors
Inventory	Stock
Owner's Equity	Capital
Assets = Equities	Equities = Assets
Assets = Liabilities + Owner's Equity	Owner's Equity + Liabilities = Assets
Shareholder	Stockholder
Payable	Outstanding
Note Payable	Bill Payable
Check	Cheque
Note Receivable	Bill Receivable

1.6 Financial Statements

End results of financial accounting are financial statements



1.7 Organizational Structure



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TYPES OF BUSINESS

- The word “Business” means the state of being busy
- Generally, an organization (combination of resources) entity engaged for making profit
- In other words all legal and economic activities undertaken towards achieving organizational objective of an enterprise referred to Business

Different authors define business in their own context; however, central idea is same



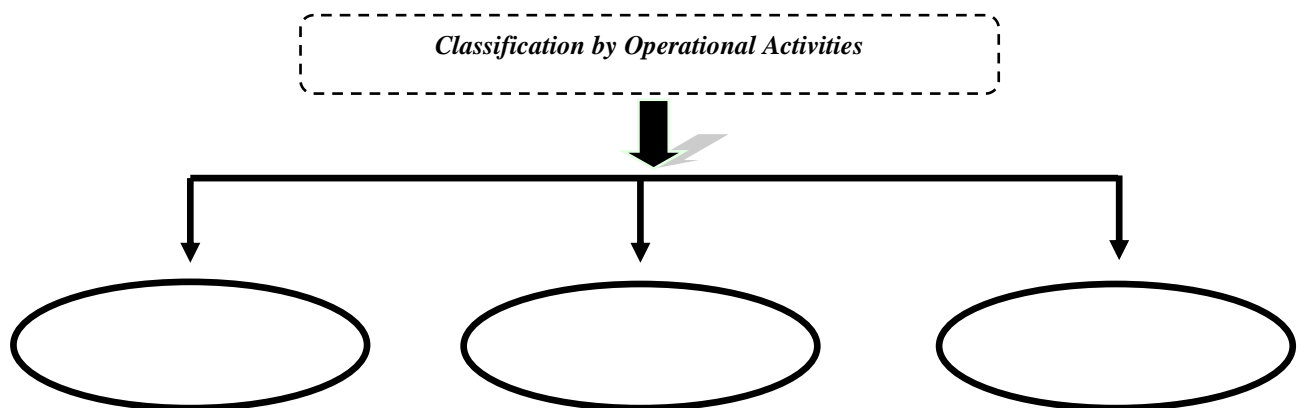
- *Every human activity which is engaged in for the sake of earning profit may be called business*
- *Business may be defined as human activities directed toward providing or acquiring wealth through buying and selling of goods*
- *An institution organized and operated to provide goods and services to the society, under the incentive of private gain is business*



Concluded that, the term business includes all human activities concerned with earning money or it is an activity in which produce or exchange goods and services for mutual gain or profit. The goods and services produced or purchased for personal use are not included in business. Business can be classified into different types under different basis by different authors. Some forms under some basis are discussed below:

2.1 Classification by Operational Activity

From operational activities point of view business can be classified into three main classes of activities. These activities are as follows

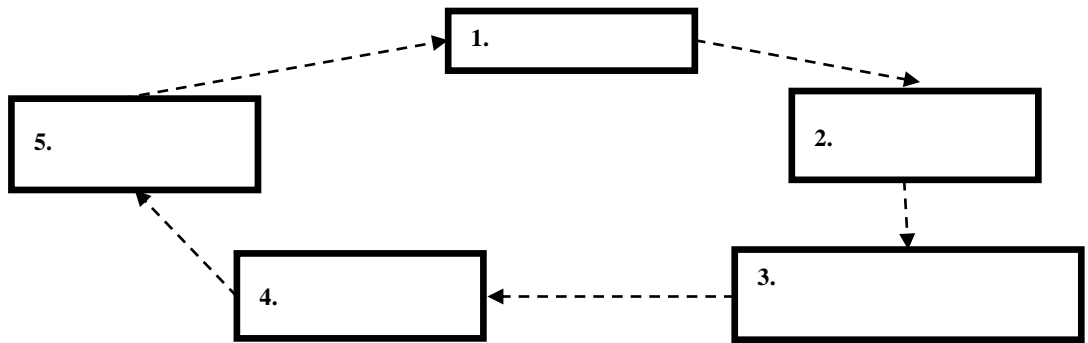


2.1.1 Merchandising Activity:

- This type of business does not change the shape of the goods rather by adding their profit
- Business received goods in finished form and sell to customers as it is

2.1.2 Manufacturing Activities:

- ❖ The enterprises which are involved in manufacturing activities, start their activities from purchase of raw material and put labor and factory overhead on the raw material and develop products
- ❖ Produced products are looks entirely different from raw material
- ❖ Hence we can say that in this type of business value addition is carries out



2.1.3 Services Activities:

✚ The organizations involve in providing service like banking, education, insurance, management development and training are called services activities

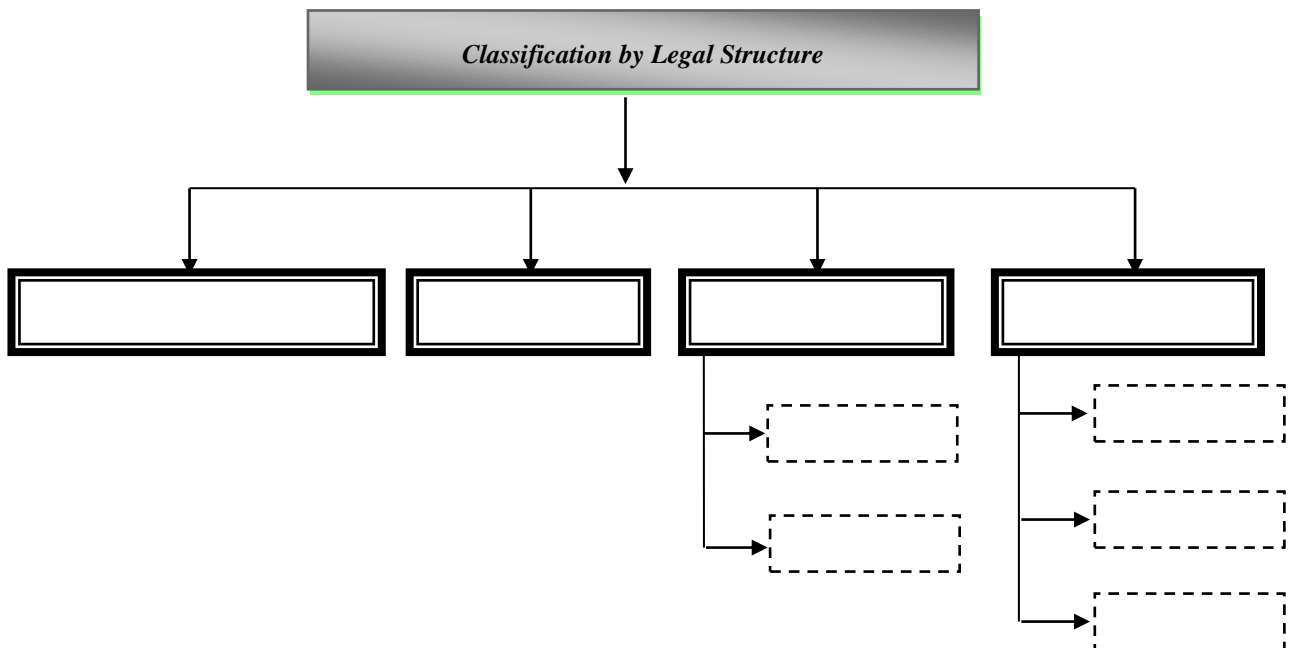
2.2 Classification by Sector

- Basically there are two sector public and private
- The public sector business organizations, for profit or non profit, are the ones controlled by the government, for instance, Pakistan Railways and WAPDA
- The firms owned by private entrepreneurs are private sector organizations like Bestway Cement etc



2.3 Classification by Legal Structure

In terms of the legal structure, firm can be categorized into the following four categories.



2.3.1 Sole Proprietorship

- ❖ A business owned by one person and the owner may operate by own or may employ others
- ❖ The owner of the business has total and unlimited personal liability of the debts incurred by the business



Stafford states, *it is the simplest form of business organization, which is owned and controlled by one man*

G. Baker defined as; *sole proprietorship is a business operated by one person to earn profit*

- ❖ Sole proprietorship is the oldest form of business organization in which one man invests his capital himself. He is all in all in doing his business. He enjoys the whole of the profit or bearing a loss

2.3.2 Partnership

- ✓ Partnership is the second stage in the evolution business organization
- ✓ It means the association of two or more persons to carry on as co-owners
- ✓ The persons who constitute this organization are individually termed as partners and collectively known as firm; and the name under which their business is conducted is called “The Firm Name”
- ✓ In ordinary business, the number of partners should not exceed 20, but in case of banking business it must not exceed 10. This type of business organization is very popular in Pakistan
- ✓ The law related to partnership is called Partnership act 1932 in Pakistan

According to Section 4 of Partnership Act 1932; *Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all*

2.3.3 Companies

- Joint Stock Company is the third major form of business organization
- It is entirely different organizational from sole proprietorship & partnership
- There are two advantages of Joint Stock Company. First of all, it enjoys the advantage of increased capital. Secondly, the company offers the protection of limited liability to the investors and disadvantage is double taxation (Corporate + Income Tax)
- The law relating to Joint Stock Company has been laid in Companies Ordinance, 1984



The most widely quoted definition of a company was given by an American judge, Justice Marshal in 1891, in which he defined a corporation as; *an artificial being, invisible, intangible and existing only in law*

According to S.E. Thomas; *a company is an incorporated association of persons formed usually for the pursuit of some commercial purpose.*

- There are two types of companies which are discussing below.

2.3.3.1 Public Limited Company:

- Company which is formed by a least ‘7’ members, and there no restrictions to maximum number of shareholders
- This company can invite public to subscribe its shares or debentures by issuance of prospectus
- The shares of a public company are freely transferable or subscribe
- The word 'Limited' is used at the end of the name of public company

2.3.3.2 Private Limited Company:

- It is a company which is formed by at least '2' members and maximum number of members which is fifty (50)
- A private company cannot invite public to subscribe to its shares or debentures by issue of prospectus
- The transfers of shares is generally restricted by the articles of association of a private company
- In case of a private company, the word 'Private Limited' must be used at the end of the name of a company

2.3.4 Hybrid

- ❖ Those combine limited liability advantage of a company with single tax advantages of a sole proprietor/ partnership

2.3.4.1 S-Type Corporation:

- ✚ S-Type corporations are limited liability corporations without double taxation
- ✚ In a regular corporation, the company itself is taxed on business profits. In addition, the owners pay individual income tax on money that they draw from the corporation as salaries, bonuses, or dividends
- ✚ In contrast, in an S corporation, all business profits "pass through" to the owners, who report them on their personal tax returns (as in sole proprietorships or partnerships)

2.3.4.2 LLP:

- ✓ Limited Liability Partnership (LLP) is also a form of partnership with allows limited liability to the owners
- ✓ These organizations are similar in many ways to the partnership; however, LLPs offer more flexibility and benefits to the owners

2.3.4.3 PC:

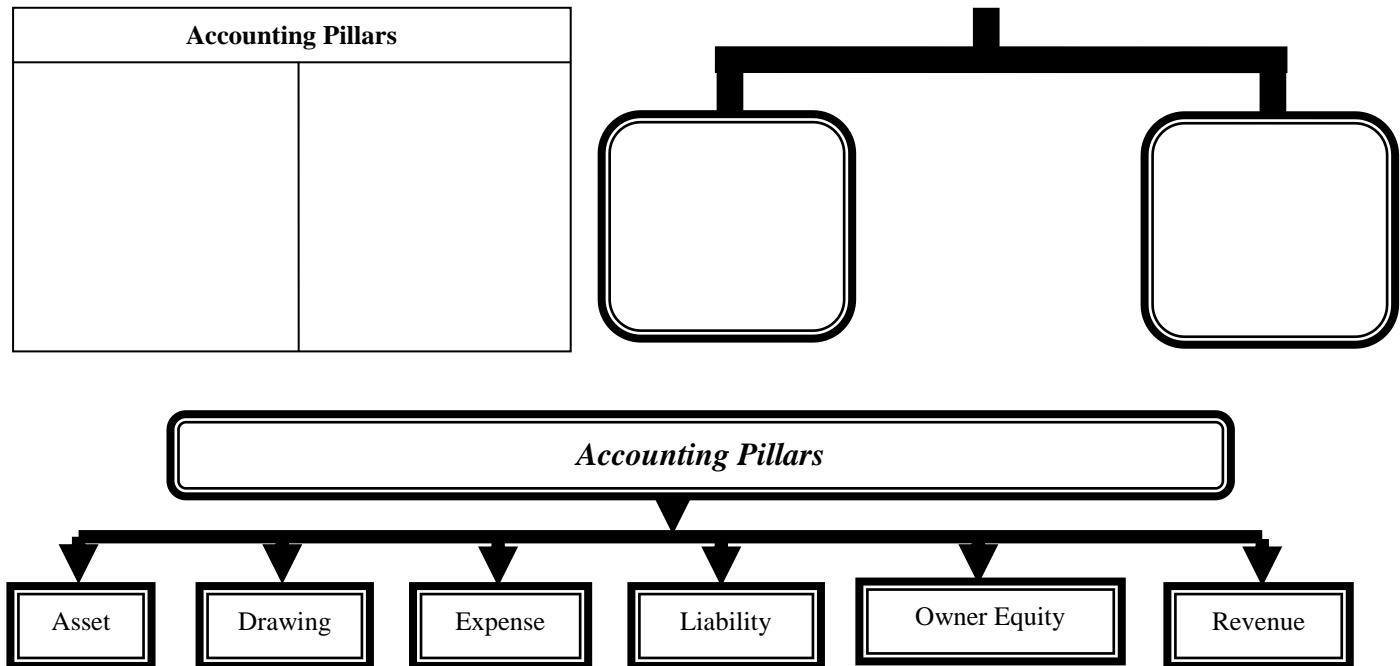
- Personal Corporations (PC) or Professional Corporations are generally formed by professionals to protect them against litigations. Professionals like doctors, lawyers etc. prefer to register their business as Professional Corporations

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TYPES of ACCOUNTS

There are six Accounting Pillars:



3.1 Assets



All Economic Resources of business organization. Assets are defined in Statement of Financial Accounting Concept 6 (SFAC 6); as *future economic benefits obtained or controlled by a particular entity as a result of past transactions or events* (Para. 25)

- A resource having economic value that an individual, corporation or country owns or controls with the expectation that it will provide future benefit
- It has four types, Tangible Assets, Intangible Assets, Natural Resources and Financial Assets

Tangible Assets: Machinery, Furniture, Building, Equipments, Plant, Car, Inventories, Fixture and Fittings, Computer, Books etc. etc.

Intangible Assets: Patents, Goodwill, Copy Rights, Trade Mark etc. etc.

Natural Resources: Land, Mines, Coal, Forest etc. etc.

Financial Assets: Cash, Note Receivables, Marketable Securities, Bank, Prepaid items, etc. etc.

3.2 Liabilities

- ✓ All Economic Obligations of business organization|



Liabilities are defined by SFAC 6 as *future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events* (Para. 35)

- ✓ Whenever a person purchases something on credit he promises to pay for the goods on a future date. This is his obligation to pay cash at a future date and thus it becomes his liability
- ✓ Liabilities are typically divided into two categories: short-term or Current Liabilities and Long Term Liabilities

Current Liabilities: Account Payable, Bank Overdraft/Overdrawn, Note Payable outstanding or payables, etc.

Long Term Liabilities: Bank Loan, Debenture, Bonds, Mortgage Loan etc. etc.

3.3 Drawing

- De-investment of the owner from business
- Drawing is defines as withdrawal made by owner in the form of cash and other assets for their personal use
- This will be reduce the owner equity account
- This is the case only sole proprietorship and partnership
- There is no drawing account in case of corporation. Drawing decrease owner equity in the business

3.4 Owner Equity

- Investment in the business by owner



According to SFAC 6 *the residual interest in the net assets of an entity that remains after deducting its liabilities* (Para. 49)

3.5 Expenses

- All Outflows of the business for earning|



According to SFAC 6 as *outflows from delivering or producing goods, rendering services or carrying out other activities that constitute the entity's ongoing major or central operations* (Para. 80).

- Expenses are economic costs that a business incurs through its operations to earn revenue

Wages, Salaries, Rent, Octri, Fright, Carriage, Stationery, Repairs, Carriage, Discount, Transportation, Commission and all accounts have debit balance (Dr) etc.

3.6 Revenue

- ❖ All inflows of the business.
- ❖ Revenue = Cost + Profit or (Loss)



According to SFAC 6 as *inflow from delivering or producing goods, rendering services or other activities that constitute the entity's ongoing major or central operations* (Para. 78)

- ❖ Revenue is the amount of money that a company receives from its operating activities in a given period, mostly from sales of products and/or services to customers
- ❖ It is not to be confused with the terms "profits" or "net income" which generally means total revenue less total expenses in a given period; Profit = Revenue - Cost
- ❖ Revenue is calculated by multiplying the price at which goods or services are sold by the number of units sold

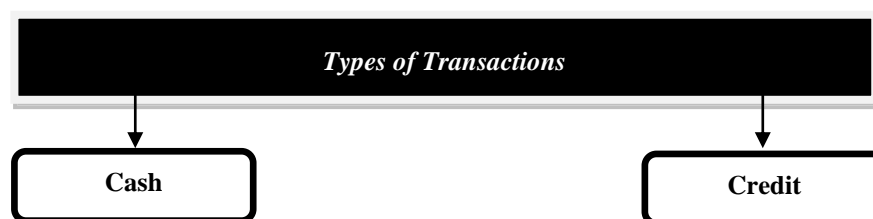
Sales, fees etc. and all accounts have credit balance like commission (Cr) etc.

3.7 Transactions

- Transactions are heartbeat of every business
- All economic activities are called transactions
- Any dealing between two persons involving money or a valuable thing is called transaction
- Every person cannot fulfill all his needs like food, clothing, housing etc. on his own. He, therefore, depends on other people to provide him with some of his needs

3.8 Forms of Transactions

- Translating every transaction in terms of money does not always mean that the money changes hands, the same time at which the transaction takes place. It may be paid before or after the goods are exchanged
- When the money value of an item being purchased is paid, at the same time the item is exchanged. The transaction is said to be a cash transaction
- On the other hand, if the payment is delayed to a future date, the transaction is termed as a credit transaction



3.9 Chart of Accounts

- Account is formal record that represents certain resources and claims to such resources, transactions or other events that result in changes to those resources and claims
- Chart of accounts is a list of ledger account names and numbers arranged in the order in which they appear in the financial statements
- The chart serves as a useful source for locating a given account within the ledger. The numbering system for the chart of accounts must leave room for new accounts. A range of numbers is assigned to each financial statement category

Example # 3.1: For each of the following, write Accounting Pillars and Normal Balance?

<i>S.no</i>	Items	Accounting Pillars	Normal Balance
<i>1</i>	Cash		
<i>2</i>	Accounts Payable		
<i>3</i>	Income Taxes		
<i>4</i>	Stock		
<i>5</i>	Transportation cost		
<i>6</i>	Prepaid Rent		
<i>7</i>	Sales		
<i>8</i>	Note Payable		
<i>9</i>	Bill Receivables		
<i>10</i>	Salary Outstanding		
<i>11</i>	Rent and Taxes		
<i>12</i>	Common Stock		
<i>13</i>	Sundry Debtors		
<i>14</i>	Commission (Cr)		
<i>15</i>	Leasehold Land		
<i>16</i>	Utility Bills		
<i>17</i>	Other Income		
<i>18</i>	Land and Building		
<i>19</i>	Insurance Premium		
<i>20</i>	Payable and Outstanding		
<i>21</i>	Owner Invested Machinery		
<i>22</i>	Drawings		
<i>23</i>	Bank Charges		
<i>24</i>	Salaries received		
<i>25</i>	Fuel Expense		
<i>26</i>	Loan to Employees		
<i>27</i>	Bank Account		
<i>28</i>	Wages earned		
<i>29</i>	Marketable Securities		
<i>30</i>	Unearned Revenue		

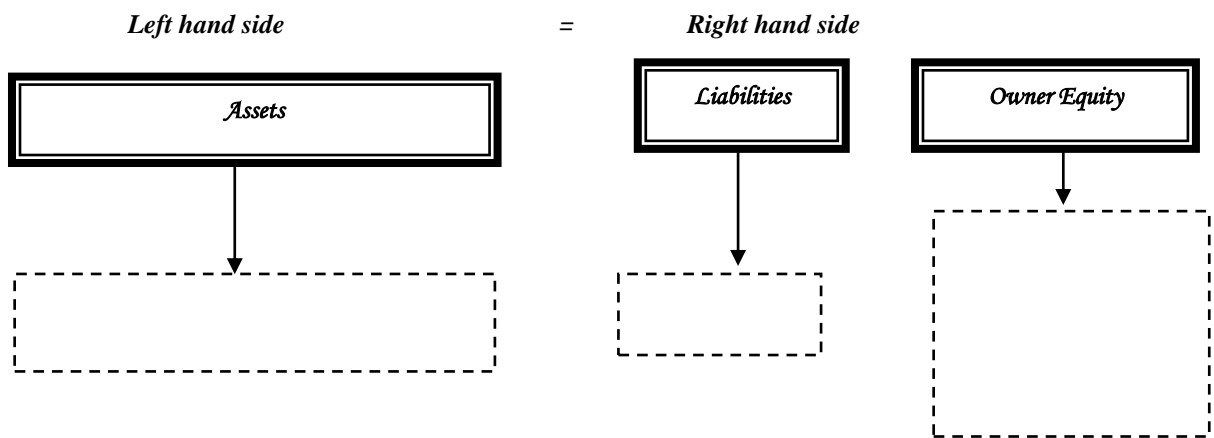
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ACCOUNTING EQUATION

- ❖ Double entry bookkeeping states that for every debit entry there should be pass a credit entry. Every transaction has twofold effect; this concept has a result of Accounting Equation or Balance Sheet Equation or Fundamental Equation

$$\begin{aligned}
 \text{Resources} &= \text{Source} \\
 &\text{Or} \\
 \text{Assets} &= \text{Equities / Claims (Claims may be internal or external)} \\
 &\text{Or} \\
 \text{Asset} &= \text{Liabilities + Owner Equity} \\
 &\text{Or}
 \end{aligned}$$

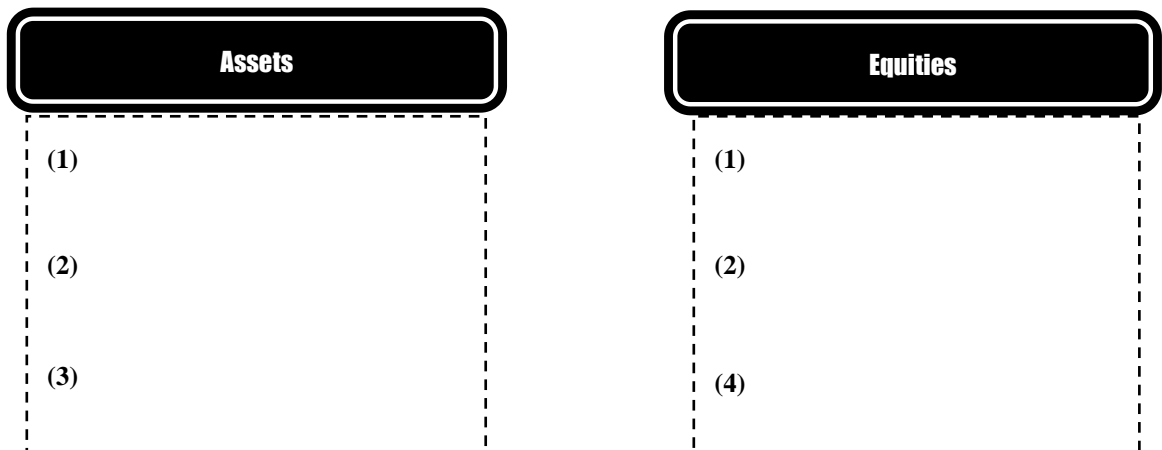


Which of the following is correct form of Equation?

Assets	=	Liabilities	+	Owner's Equity	
Assets	-	Liabilities	=	Owner's Equity	
Liabilities	=	Assets	-	Owner's Equity	
Asset	-	Liabilities	-	Owner's Equity	= 0

- ❖ At any point of time total assets must be equal to total equities. In other words we can say that left hand side which is resource side must be equal to right hand side which is of course source side

4.1 Four Effects



Example # 4.1: For each of the following transactions indicate the effects on the Accounting Equation of the Company i.e. (Increase, Decrease, Conversion or No Effect)?

(1) The owner invests personal cash in the company?

Assets	Liabilities	Owner's Equity
↑	<i>Nil</i>	↑

(2) The owner withdraws company's assets for personal use?

Assets	Liabilities	Owner's Equity

(3) The company purchases equipment with its cash?

Assets	Liabilities	Owner's Equity

(4) The company repays the bank loan by introducing reinvestment of owner in the company?

Assets	Liabilities	Owner's Equity

Example # 4.2: From the list of accounts below, determine which assets are and which equities are. List the assets under the Asset Column and the equities under the equities Column. Then add each column and complete the Fundamental Accounting Equation?

Accounts		Asset	Equities
<i>Cash</i>	<i>Rs.5,000</i>	<i>Rs. 5,000</i>	
Accounts Receivable	10, 600		
Building	35,000		
Accounts Payable	5,000		
Inventory	200		
Computer Equipment	18,000		
Bank Loan	6,000		
Mortgage Payable	10,000		
Owner Equity	47,800		
TOTAL	Rs. 137,600		

Example # 4.3: For each of the following equations, a figure is missing. In the space provided, please supply the missing figure that will balance the equation.

Assets	Liabilities	Owner's Equity
100	20.00	80
	720	70
2,000		1,600
11,218	10,000	
	25	985
340		328
8793	0	
	1,501	499

Example # 4.4: Prepare Accounting Equation on the basis of following transactions?

1. Arush Khan and Company started business with cash Rs. 100,000
2. She purchased Furniture for cash Rs. 2,000
3. Purchases Machinery on credit from Umer Abbasi Rs.10,000
4. Cash withdraw by owner Rs. 20,000
5. Cash Sales of Rs. 6,000
6. Credit sales to Ayesha Iqbal Rs.2,000
7. Paid rent Rs. 2,500 and wages Rs. 1,500

S. No	Assets				Equities	
	Cash	Furniture	Machinery	A/C Receivables	A/C Payable	O.E
1	100,000					100,000
Bal	100,000					100,000
2						
Bal						
3						
Bal						
4						
Bal	78,000	2,000	10,000		10,000	80,000
5						
Bal						
6						
Bal						
7						
Bal	80,000	2,000	10,000	2,000	10,000	84,000
Total	Rs. 94,000				Rs. 94,000	

Example # 4.5: On 1st January, 2016 the balances of Muhammad Danish & Bros. are as follows?

Assets		Equities	
Cash	25,000	Creditor	40,000
Debtor	17,000	Capital	94,000
Inventory.....	22,000		
Building	70,000		
Total	Rs. 134,000		Rs. 134,000

Transaction during the January was

January

- 1) Purchase inventory for cash Rs. 3,600
- 5) Sold inventory for cash Rs. 12,000 costing Rs. 10,500
- 7) Cash paid to creditor Rs. 25,000
- 9) Sold inventory for cash Rs. 5,000 and on credit Rs. 3,000 costing Rs. 6,000
- 11) Inventory returned by a cash customer Rs. 2,000 costing Rs. 1,900
- 15) Cash received from debtors Rs. 14,000
- 18) Cash paid for furniture purchased for owner domestic use Rs. 1,000
- 20) Paid salaries Rs. 1,400

Requirement: Show the effects of above transaction on the accounting equation:

S. No	Assets				Equities	
	Cash	Debtor	Inventory	Building	Creditor	Capital
Bal	25,000	17,000	22,000	70,000	40,000	94,000
1						
Bal						
5						
Bal	33,400	17,000	15,100	70,000	40,000	95,500
7						
Bal						
9						
Bal						
11						
Bal	11,400	20,000	11,000	70,000	15,000	97,400
15						
Bal						
18						
Bal	24,400	6,000	11,000	70,000	15,000	96,400
20						
Bal						
Total		Rs. 110,000			Rs. 110,000	

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ACCOUNTING VARIATION PROFORMA

S.No	Transaction	Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit

5.1 Chart of Accounts

Assets:

Machinery, Furniture, Leasehold Premises, Building, Equipment, Plant, Account Receivables, Note Receivables, Land, Car, Marketable Securities, Cash, Goodwill, Leasehold building, Bank, Computer, Fixture and Fittings, Copy Rights, Leasehold land, Inventories, Loan to employees, Prepaid items etc. etc.

Drawing:

Any withdrawal made by Owner in the form of Physical assets like furniture, inventory etc. or in the form of Financial asset like cash etc.

Expense:

Wages, Salaries, Rent, Octri, Frieght, Carriage, Repairs, Maintenance, Discount, Rebate, Transportation, Commission, Miscellaneous Expense, Entertainment Expense (which have debit balance or paid)

Liability:

Note Payable, Account Payable, Bank Loan, Debenture, Bonds, Mortgage Loan and any outstanding or payables and unearned

Owner Equity:

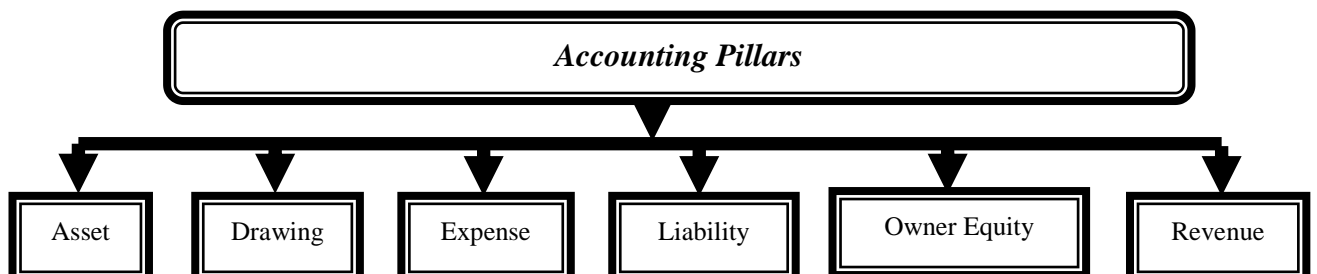
Any assets invested by owner may be in form of monetary or physical assets.

Revenue:

Sales, fees etc. all accounts have credit balance like commission (Cr) or received like discount received

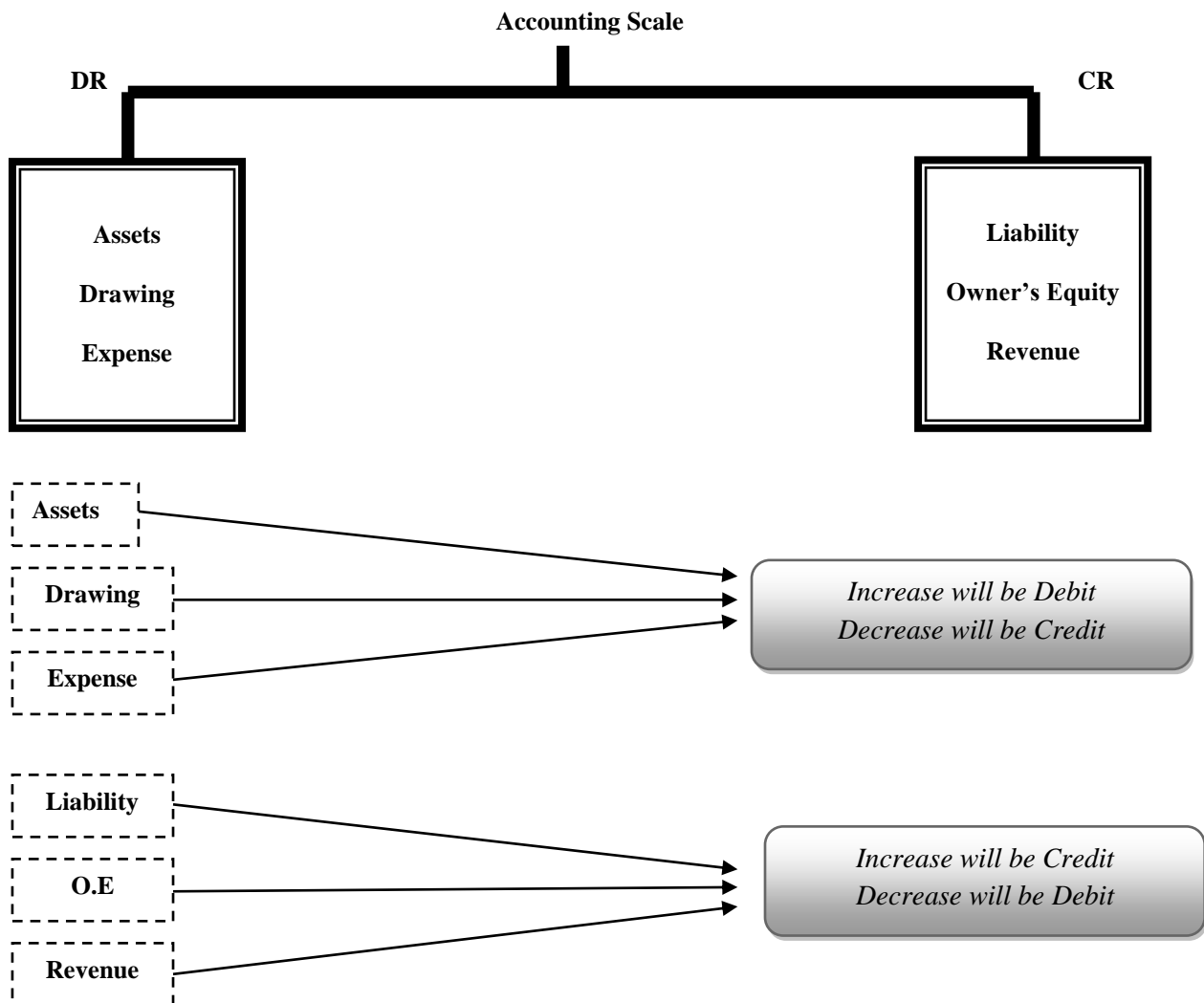
5.2 Accounting Pillars

There are six Pillars of Accounting



5.3 Golden Rules of Debit and Credit

- ◆ The term debit means left, and credit means right. They do not mean increase or decrease
- ◆ Debit is abbreviated Dr and credit is abbreviated Cr
- ◆ The act of entering an amount of the left side of an account is called debiting. Making an entry on the right side is called crediting
- ◆ When the totals of the two sides are compared, an account will have a debit balance if the left side (Dr side) is greater. Conversely, the account will have a credit balance if the right side (Cr side) is greater



5.4 Contra Accounts

- | | | | |
|-----------------------------------|----------------------|----------------------|------------|
| 1. Purchase Return | Return Outward | Contra Expense | Cr Balance |
| 2. Sales Return | Return Inward | Contra Revenue | Dr Balance |
| 3. Accumulated Depreciation | | Contra Assets | Cr Balance |
| 4. Provision for Bad Debts | | Contra Assets | Cr Balance |

5.5 Normal Balances

Items	Normal Balance	
	Dr.	Cr.
<i>Assets</i>	<i>Debit Balance</i>	
Liabilities		
Expenses		
Revenue		
Owner's Equity		
Drawing		
Purchase Return/ Return Outward		
Sales Return/ Return Inward		
Accumulated Depreciation		
Provision for Bad Debts		

Example 5.1: For each of the following items write Accounting Pillars and Normal Balances:

Items	Accounting Pillars	Normal Balance
<i>Cash at bank</i>	<i>Assets</i>	<i>Dr</i>
Financial charges paid		
Accumulated Depreciation		
Stock in trade		
Salaries payable		
Advance deposit and prepayments		
Carriage inward		
Commission received		
Sundry debtors		
Purchases Return/ Return outward		
Investment by Owner		
Bank charges (Dr)		
Profit or Capital gain		
Provision for bad debts		
Cash in hand		
Mark up (Cr)		
Sundry creditors		
Transportation outward		
Due from customers		
Unearned Revenue		
Deinvestment by owner for personal use		
Sales Return/ Return Inward		
Outstanding wages		

Example 5.2: Use Accounting Variation Proforma for following transactions

Jan. 2 Owners invested Cash of Rs. 70,000 in new business (Hint: Owner's Equity is Source)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Cash	Asset	Increase	70,000	
Owner's Equity	Owner's Equity	Increase		70,000

Jan. 3 An additional Rs. 10,000 was borrowed from a local bank as bank loan (Hint: Liability is Source)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit

Jan. 5 Paid Rs. 1,500 in office Rent for the month (Hint: Expenses always debited with its own Name)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit

Jan. 6 Cash Sales Rs. 1,000 (Hint: Revenue always credited with its own Name)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Cash	Asset	Increase	1,000	
Sales	Revenue	Increase		1,000

Jan. 9 Inventory costing Rs. 2,000 were purchased on account (Hint: Account Payable for credit buying)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Account Payable	Liability	Increase		2,000

Jan. 10 Credit Sales Rs. 3,000 (Hint: Account Receivable for credit sales)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Sales	Revenue	Increase		3,000

Jan. 12 Purchase goods for Rs. 6,000 cash (Hint: When goods or merchandising bought we debit purchase account)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
	Expense	Increase	6,000	
	Asset	Decrease		6,000

Jan. 14 Rs. 1,200 was paid on account to the vendor/supplier

(Hint: Reducing Liability)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
		Decrease	1,200	
		Decrease		1,200

Jan. 15 Received cash from customer Rs. 3,000

(Hint: Assets realized or conversion of assets)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Cash			3,000	
Account Receivable				3,000

Jan. 17 Paid insurance premium for two years Rs. 2,400

(Hint: More than one year expense is asset)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Prepaid Insurance	Asset	Increase	2,400	
				2,400

Jan. 19 Goods return by cash customer of Rs. 200

(Hint: Sales return is always debited)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Sales Return				

Jan. 20 Goods return to credit supplier of Rs. 500

(Hint: Purchase return is always credited)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Purchase Return				

Jan. 21 Received commission of worth Rs. 700

(Hint: Revenue always credited with its own Name)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Commission	Revenue	Increase		700

Jan. 22 Purchase Machinery of Rs. 10,000; Rs. 2,500 paid and for remaining sign a Note

(Hint: Compound entry)

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Machinery	Asset	Increase	10,000	

Jan. 22 Total services performed for Rs. 4,500, cash received Rs. 2,000 and remaining Note receivable

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
	Asset	Increase	2,000	
	Asset	Increase	2,500	
	Revenue	Increase		4,500

Jan. 22 Sales for client who have paid in advance in March 12

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Unearned Sales	Liability	Decrease	3,000	

Jan. 25 Account receivable collected for Rs.1,500

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit

Jan. 28 Purchased supplies of worth Rs. 25,000; paid 10,000 cash and remaining account payable

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Supplies			25,000	
Cash				10,000
Account Payable				15,000

Jan. 30 Received Rs. 3,000 cash from customer to whom sales to be delivered in future

Charts of Accounts	Accounting Pillars	Reasons	Debit	Credit
Cash	Asset	Increase	3,000	
Unearned Sales	Liability	Increase		3,000

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Accounting 1 MGT



Registration No _____

Signature _____

BBA 2

Prototype Quiz No. 1

Instructions

Please read the following instructions carefully before attempting any question:

- Write your student Registration No. and Signature; Failure to do so will result in paper cancellation.
- All questions are compulsory. This exam consists of **30 marks for Objective Type Questions, Equation 10 marks and Variation Proforma 10 Marks** and time allowed is one 80 minutes.
- For each OTQ statement, read the choices available carefully and **“Encircle” (don’t tick mark)** one which you consider is the most suitable answer. Zero marks will be given if more than one option is **“Encircled”**.
- Cutting and overwriting in objective type questions is not allowed; if done so, that particular question will be marked Zero.
- Remember not to spend too much time on Objective type questions. It is important to manage your time and response to test questions effectively.
- Do not ask any questions about the contents of this examination from anyone.
- If you believe that some essential piece of information is missing, make an appropriate assumption and use it to solve the problem and will discuss in paper debate.
- Students are advised to solve paper in blue & black ink and do not use red, green ink and pencil.
- Writing irrelevant/immoral material will be severely penalized.
- This examination is closed book, closed notes, closed neighbors.
- Use of **mobile phones** is strictly prohibited; switch it off if it is in your custody.
- Failure to comply with the Teacher’s directions will result in your exam paper being cancelled.

(Not to Turn the Title Page Prior to Instructions)

OTQ / 20 Equation / 10 Proforma / 10 Total = / 40

For Solution Click www.accountancyknowledge.com/accounting-papers/quiz-1/

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Q# 1 Multiple choice Questions**(Marks 20)**

1. Which of the following provides information about the financial information's, obligations and activities on the economic entity that is intended for use primarily by external decision makers?
(a) Management accounting (b) Financial accounting
(c) Tax accounting (d) Environmental Accounting
2. Which of the following statement is true about purpose of accounting?
(a) The purpose of accounting provide information to manager
(b) Accounting purpose gives quantitative information to economic decision makers
(c) Provision of base for decision making is purpose of accounting
(d) All of above statement are true regarding purpose of accounting
3. The controller's responsibilities are primarily in nature, while the treasurer's responsibilities are primarily related to?
(a) Operational; Financial accounting (b) Financial management; Operations
(c) Accounting; Financial management (d) Financial management; Accounting
4. The outcome of financial accounting is to?
(a) Record all transactions in the books of accounts (b) Calculate profit
(c) Provide management with detailed analyses of costs
(d) Present the financial results to the organization by means of recognized statements
5. Which of the following persons are most likely to use accounting information?
(a) Business owners (b) Lending institutions
(c) All of the above (d) None of the above
6. Which of the following financial statements also called statement of financial position?
(a) Balance Sheet (b) Income Statement
(c) Statement of changes in equity (d) Statement of cash flows
7. The question of what additional information should be provided to external users refers to?
(a) Reporting (b) Recognition (c) Disclosure (d) Measurement
8. A necessary element of internal control is?
(a) Database (b) Information and communication
(c) Systems analysis (d) Systems design
9. All of the form of Business Organizations except?
(a) Partnership (b) S type
(c) LLP (d) Unlimited Liabilities Companies
10. Organizations which combine the limited liability advantage in sole ownership are called?
(a) S Type (b) Hybrid (c) PC (d) LLP
11. Which of the following account is affected from the Drawings of cash in sole-proprietorship business?
(a) Shareholder account (b) Capital account
(c) Liability account (d) Expense account

12. Which of the following is a liability?
(a) Petty cash (b) Loose tools (c) Unearned Revenue (d) Leasehold premises
13. What is the meaning of the word 'limited' in the name of a limited company?
(a) The number of shareholders is limited to 50
(b) The liability of the company for its own debts is limited
(c) The liability of shareholders for the company's debts is limited
(d) There is a limit on the amount of debts that the company can contract
14. What is owned by a business and used in carrying out its operating activities is best described as?
(a) Liabilities (b) Owner's Equity (c) Revenues (d) Assets
15. Which of the following accounts will be used in equation, if the goods are sold on credit to Mr Muhammad Abdullah?
(a) Cash account and Owner's equity (b) Account Receivable and Owner's equity
(c) Cash and Account Receivable (d) Account Payable and Owner's Equity
16. If the cost of sales is Rs. 60,000, sales are Rs. 95,000 and operating expenses are Rs. 20,000 during the year. What would be the Net Profit?
(a) Rs. 15,000 (b) Rs. 35,000 (c) Rs. 55,000 (d) Rs. 60,000
17. Which of the following statement true?
(a) Expenses decrease shareholders' equity (b) Profit and gains increase shareholders' equity
(c) Revenue increase shareholders' equity (d) All of given options are true
18. A company paid cash of Rs. 350 for salary of employees. Which accounting equation's categories would be affected by this transaction?
(a) Assets and Owner's Equity (b) Expense and liabilities
(c) Assets and liabilities (d) Assets only
19. Which of these items would be accounted for as an expense?
(a) Repayment of a bank loan (b) Dividends of stock holders
(c) The purchase of land (d) Payment of the current period's rent
20. The reporting earning of income previously collected has what effect on the basic accounting equation?
(a) Increase in assets, decrease in liabilities
(b) Increase in assets, increase in stockholder's equity
(c) Decrease in liabilities, increase in stockholder's equity
(d) Decrease in assets, decrease in stockholders' equity

Q # 2 You are required to make Accounting Equation*(Marks = 10)*

After playing several seasons of professional football, Haider Sultan had saved enough money to start a business, to be called Auto Rental. The transactions during March 2009, while the new business was being organized are listed below.

March 1 Haider Sultan started business of Auto Rental by invested Rs. 540,000 Cash and Rs. 60,000 of worth Furniture in the business.

March 9 Purchased two new Cars at Rs. 80,000 each from Fleet sales company. Paid Rs. 90,000 Cash and agreed to pay Rs. 70,000 by March 31 the remaining balance.

March 18 Purchased goods of worth Rs. 4,000; Rs. 1,000 for Fuel expenses has been paid and Rs. 3,000 for Repair and Maintenance expense are payable.

March 23 The new company purchased Land and a Building at a cost of Rs. 120,000 of which Rs. 72,000 was regarded as applicable to the Land and Rs. 48,000 to the Building. The transaction involved a Cash payment of Rs. 41,500 & the issuance of a Note Payable for Rs. 78,500.

March 25 Revenue earned during the month by Cash Rs. 80,000.

Haider Sultan

	<i>Cash</i>	<i>Furniture</i>	<i>Car</i>	<i>Land</i>	<i>Building</i>	<i>N. Pay.</i>	<i>A. Pay.</i>	<i>O.E</i>
1								
Bal								
2								
Bal								
3								
Bal								
4								
Bal								
5								
Bal								
Total								

Q # 3 Following Variation Proforma for Journal Entries have been provided, you are required to check changes in following transaction with the help of Proforma

(Marks = 10)

Variation Proforma for Journal Entries

S.No	Transactions	Account Title	Pillar of	Reasons	Debit (Rs.)	Credit (Rs.)
		Involved	Accounts			
1	Owner withdrawal Furniture in business Rs. 20,000					
2	Goods Sales to Vendor on Account Rs. 44,000					
3	Payment made to Creditor on Account Rs. 7,500					
4	Further Investment made by owner Rs. 5,000					
5	Paid Wages to employee by Cash Rs. 200					

ACCOUNTING CYCLE

Bookkeeping should not be confused with accounting or accountancy. Persons with little knowledge of accounting may fail to understand the difference between these terms and often used to mean the same thing. Therefore, it is useful to make a distinction

6.1 Bookkeeping

- Bookkeeping is a small part of the field of accounting and the simplest part, just like arithmetic is a small part of the broad discipline of mathematics
- Its work is clerical nature and can be performed by office workers, machine and computers. The functions of Bookkeeping is to properly record the financial transactions in the books of account
- Bookkeeping is recording or first phase of an accounting system

6.2 Accounting

- The process of accounting begins where the bookkeeping process ends
- Accounting is broad subject and final phase
- The function of accounting is to classify the recorded transactions, summarize them, interpret them, and collect and communicate necessary information to the management and other interested parties
- Accounting includes not only maintenance of accounting records, but also the preparation and interpretation of Financial Statements

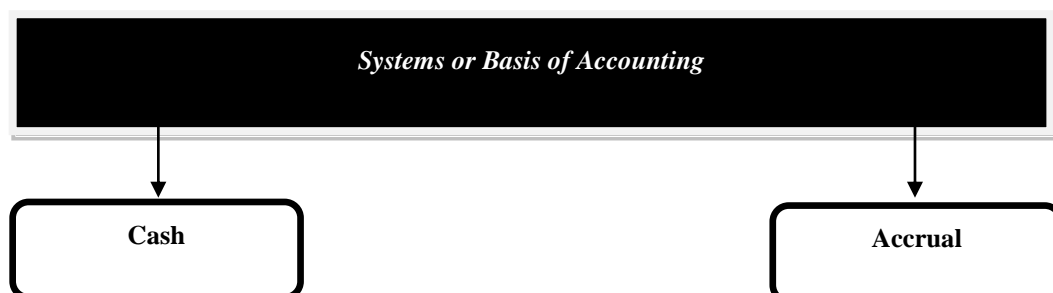
6.3 Accountancy

- The two words accounting and accountancy are often used to mean the same thing. But it is not correct
- Accountancy is the main subject while, accounting is one of its branches
- The word "accountancy" is far extensive; i.e. the scope of accountancy is far a wide and extensive compared to accounting
- It covers the entire body of theory and practice, e.g. bookkeeping, accounting, costing, auditing, taxation etc.



6.4 Systems or Basis of Accounting

There are two systems or basis of accounting, Cash and accrual. The difference between the two systems of accounting is when revenues and expenses are recorded



6.4.1 Cash Accounting

- With cash basis accounting, revenue is recognized (recorded) when cash is received. Expenses are recognized only when cash is paid
- It is the accounting system in which revenue and expenses are recorded when actual cash / cheque is received or paid
- The same principle applies for income and other transactions as well i.e. income is recorded when cash is actually received
- No Account Payable or Account Receivables
- Let's take the example of utility bills like electricity, telephone etc. The bill of January is received on 5th February and paid on 15th February. If the organization is following cash accounting practice it will record the expense of electricity on 15th February
- Cash-based accounting refers to keeping a record of cash inflows and cash outflows

6.4.2 Accrual Accounting

- ✓ Accrual basis accounting requires accountants to follow the revenue recognition principle and the expense recognition principle
- ✓ It is the accounting system in which events are recorded as and when they occur
- ✓ This means that revenue is recorded when it is earned
- ✓ Expense is recorded when incurred i.e. the organization has obtained the benefit from it
- ✓ Consider the same example the electricity is utilized in the month of January so the expense should be recorded in the month of January 31st
- ✓ Similarly the case of revenue
- ✓ Account Payable and Account Receivable available
- ✓ Cash basis accounting does not satisfy the requirements of Generally Accepted Accounting Principles (GAAP), whereas accrual basis accounting does.
- ✓ Accrual basis accounting provides an objective measurement of net income

6.5 Methods of Recordings

There are two methods of recording for transactions

6.5.1 Single Entry Book-Keeping

- This is the conventional style of keeping records
- In single entry book keeping system, as it is clear from the name, only one aspect of the transaction is recorded
- This actually is not a system but is a procedure by which small business concerns, like retailers and small shopkeepers, keep record of their sale / income. In this system, there are usually two to three registers
- "Naqad Khata" is one register cash received from customers is recorded
- Whereas the other one is a person-wise record of goods sold on credit "Udhar Khata"
- That means only one aspect of transaction i.e. either cash receipt/payment or credit is maintained
- Single entry is faulty, incomplete, inaccurate, unscientific and unsystematic style of account keeping

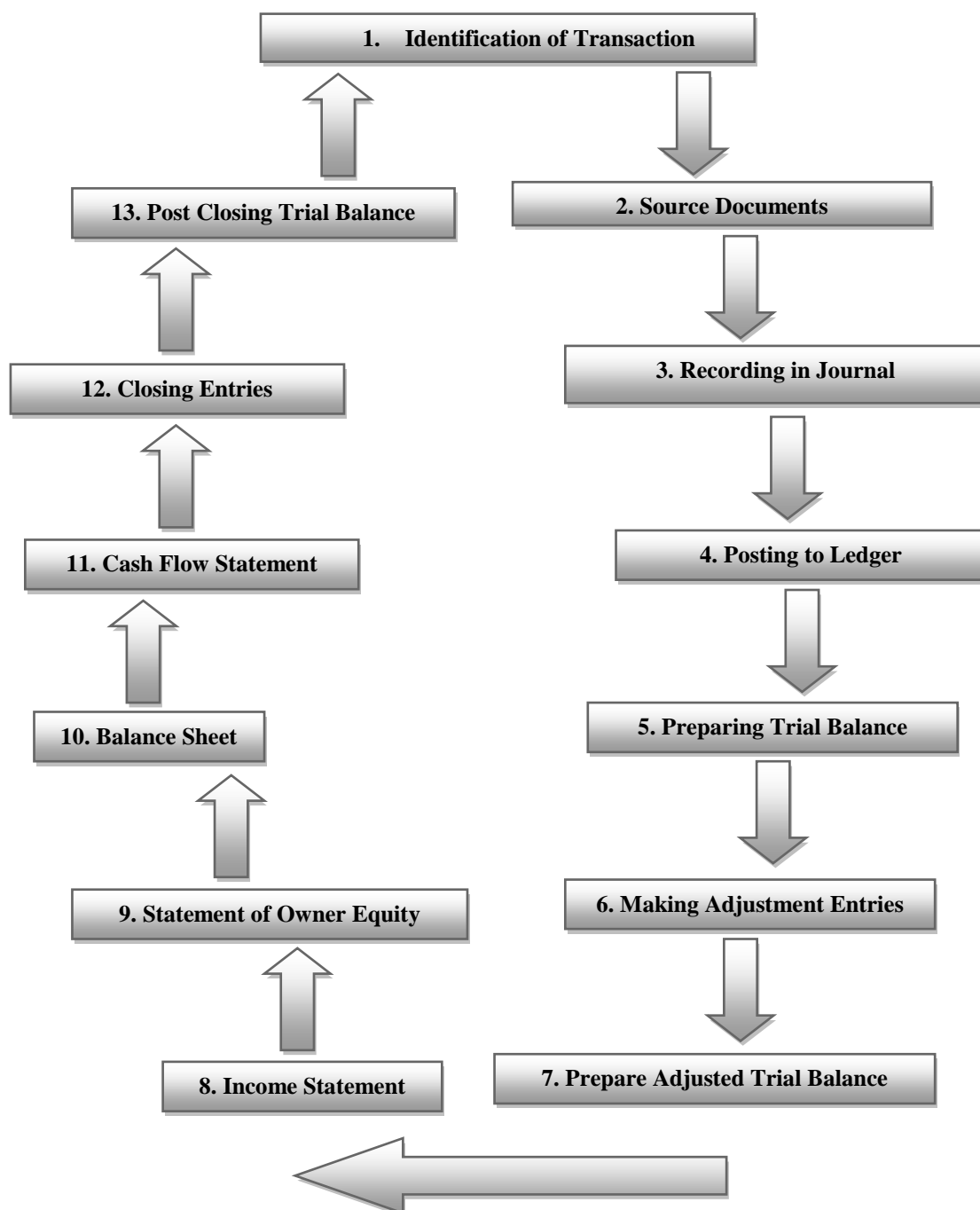
6.5.2 Double Entry Book-Keeping

- ❖ Locus Pacioli, an Italian wrote a first book on double entry system in 1494

- ❖ The concept of double entry is based on the fact that every transaction has two aspects i.e. receiving a benefit and giving a benefit
- ❖ The accounting system that records both the aspects of transaction in books of accounts is called double entry system
- ❖ 'Debit' (derived from Latin word *Debere* which means to owe) and 'Credit' (derived from Latin word *Credere* which means that which one believes in, including persons, like creditor) are denoted by 'Dr' and 'Cr' respectively. The ultimate result of the system is that for every Debit (Dr) there is an equal Credit (Cr)

6.6 Accounting Cycle

Accounting cycle refers to completed sequence of accounting steps and procedures which are required to be repeated in same order during each accounting period



6.6.1 Identification of Transactions

- In accounting, only business transaction or economic activities are recorded (except drawing in case of non-corporate form of business)
- A transaction is a particular type of event, which can be expressed in terms of money and brings changes in the financial position of a business unit
- A transaction involves transfer of something of value between two or more entities. A transaction may be an exchange in which each party receives as well as sacrifices values; in other words, in every transaction, there is a movement of value from one source to another
- A transaction can also be non-reciprocal transfer in which a business unit incurs a liability (penalty imposed by government) or transfer an asset to another entity (payment of income tax) or receives an asset (subsidy received from government)
- Transaction may be external (between business and second party) or internal (not involving second party like depreciation on machinery)

6.6.2 Source Documents

- ❖ Source documents are the evidences of business transactions (Audit requirements)
- ❖ Which provide information about the nature of the transaction, the date, the amount and the parties involved in it
- ❖ Since each transaction has an effect on the financial position of the business, there should be a documentary evidence to establish the monetary amount at which transactions are recorded
- ❖ According to the verifiable objective principle of Accounting, each transaction recorded in the books of accounts should have sufficient proof to support it
- ❖ That the transactions are properly authorized. The common documents that generally use are described below

6.6.2.1 Cash Memo:

- ★ When a trader sells goods for cash, he gives a cash memo
- ★ When a trader purchases goods for cash, he receives a cash memo
- ★ Details regarding the items, quantity, rate and the price are mentioned in the cash memo

6.6.2.2 Invoice or Bill:

- When a trader sells goods on credit, he prepares a sale invoice
- It contains full details relating to the amount, the terms of payment and the name and address of the seller and buyer
- The original copy of the sale invoice is sent to the purchaser and its duplicate copy is kept for making records in the books of accounts
- Similarly, when a trader purchases goods on credit, he receives a credit bill from the supplier of goods

6.6.2.3 Receipt:

- ❖ When a trader receives cash from a credit customer, he issues a receipt containing the date, the amount and the name of the customer
- ❖ The original copy is handed over to the credit customer and the duplicate copy is kept for record
- ❖ In the same way, whenever we make payment, we obtain a receipt from the party to whom we make payment

6.6.2.4 Debit Note:

- A debit note is prepared by the buyer and it contains the date of the goods returned, name of the supplier, details of the goods returned and reasons for returning the goods
- A duplicate copy or counter foil of the debit note is retained by the buyer. On the basis of debit note, the suppliers account is debited in the books

6.6.2.5 Credit Note:

- A credit note is prepared by the seller and it contains the date on which goods are returned, name of the customer, details of the goods received back, amount of such goods and reasons for returning the goods
- A duplicate copy of the credit note is retained for the record purpose
- On the basis of credit note, the customer's account is credited in the books

6.6.2.6 Pay-in-Slip:

- ◆ Pay-in-slip is a form available in banks and is used to deposit money into a bank account
- ◆ Each pay-in-slip has a counterfoil which is returned to the depositor duly sealed and signed by the bank official
- ◆ This source document relates to bank transactions. It gives details regarding date, account number, amount deposited (in cash or cheque) and name of the account holder

6.6.2.7 Cheque

- ✓ A cheque is a document in writing drawn upon a specified banker to pay a specified sum to the bearer or the person named in it and payable on demand
- ✓ Each cheque book has a counterfoil in which the same details in the cheque are filled
- ✓ The counterfoil remains with the account holder for his future reference. The counterfoil forms the source document for entries to be made in the books of accounts

6.6.2.8 Vouchers

- ★ A voucher is a written document in support of a business transaction
- ★ Vouchers are prepared by an accountant and each voucher is counter signed by an authorized person of the organization
- ★ The vouchers are properly filed according to their serial numbers so that the auditors may easily vouch them and these may also serve as documentary evidence in future.
- ★ Voucher may be receipt, payment and general

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JOURNAL ENTRY

- ❖ The word Journal has been derived from French word “Jour”. Jour means day
- ❖ So Journal means daily up to date record of economic transaction. It is just like a shopping bag which all transactions are recorded in order of their occurrences date wise (Chronological order)
- ❖ Every business transaction affects two or more accounts. Under double entry bookkeeping system equal debit and credit entries are made for every economic activity
- ❖ It is a book of Original Entry. It is first recording step. It records transactions in chronological order. Every transaction is to be recorded in Journal. Every organization has to maintain one Journal book at least, and General Journal is general purpose book of Prime Entry
- ❖ Entering transaction data in the journal is known as journalizing
- ❖ The journal makes three significant contributions to the recording process:
 - The journal discloses in one place the complete effect of a transaction
 - The journal provides a chronological record of transactions
 - The journal helps prevent or locate errors because the debit and credit amounts for each entry can be readily compared

7.1 Entry

Single record of the business transaction is called entry. We use this term to describe record transaction in Journal book

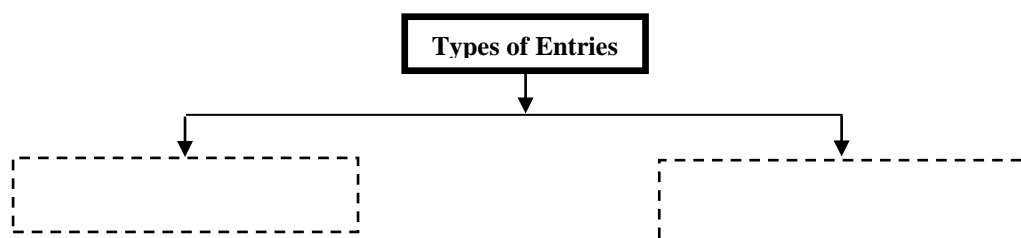
7.1.1 Parts of Entry

There are three parts of Entry. First write in first line just after date line is Debit, second must write in below line after indented ten spaces from date line is Credit and last part is Narration which is brief description of transaction write within parenthesis

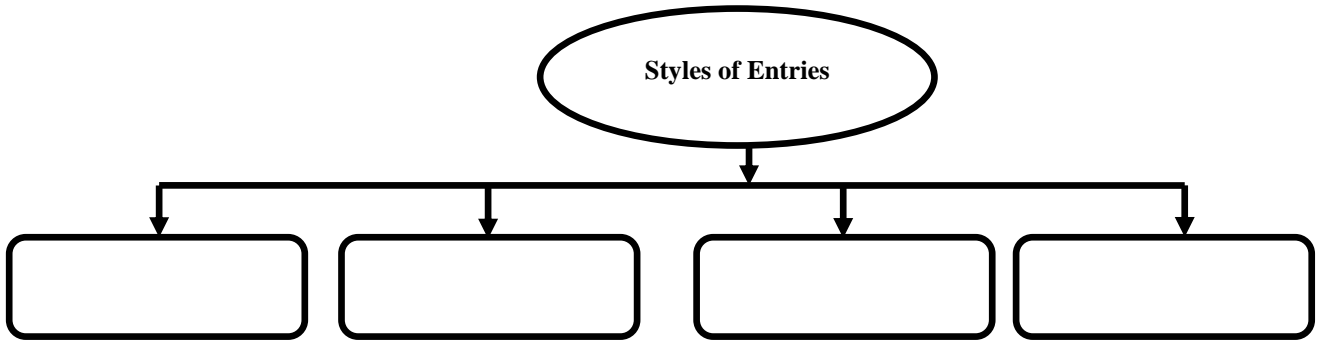
General Journal					
Date		Account Titles and Explanation	Ref	Amount (Rs)	
Year	Month			Date	Debit
		Debit elements of entry		*****	
		Credit elements of entry (Narration is brief description)			*****
		Total		*****	*****

7.1.2 Types of Entry

There are two types of Entries. First is simple entry and second is compound entry. Simple Entry has one Debit and one Credit while, Compound Entry has more than one Debit or more than one Credit or more than one Debit and Credit

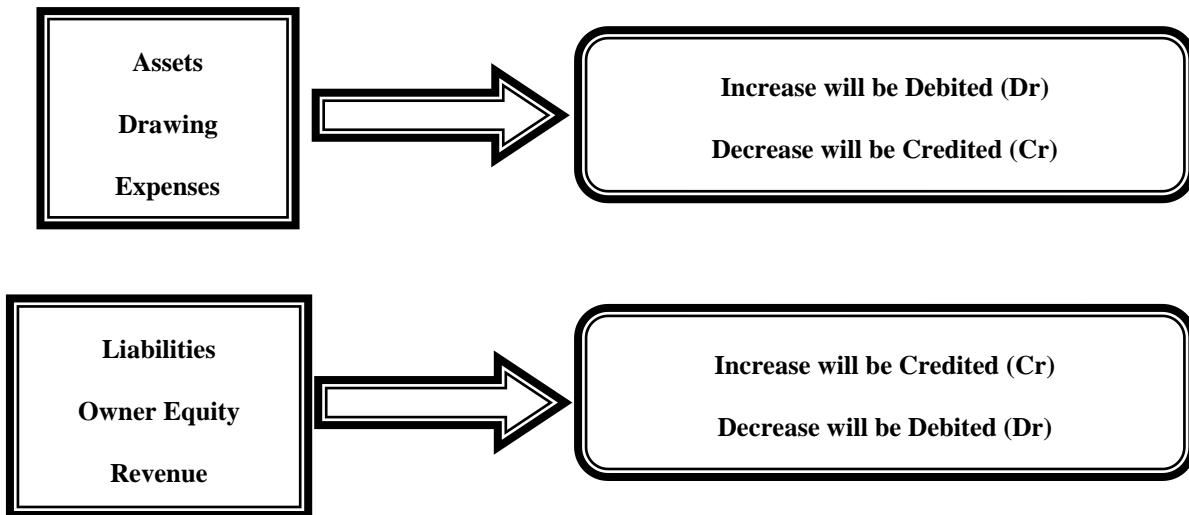


7.1.3 Styles of Entries



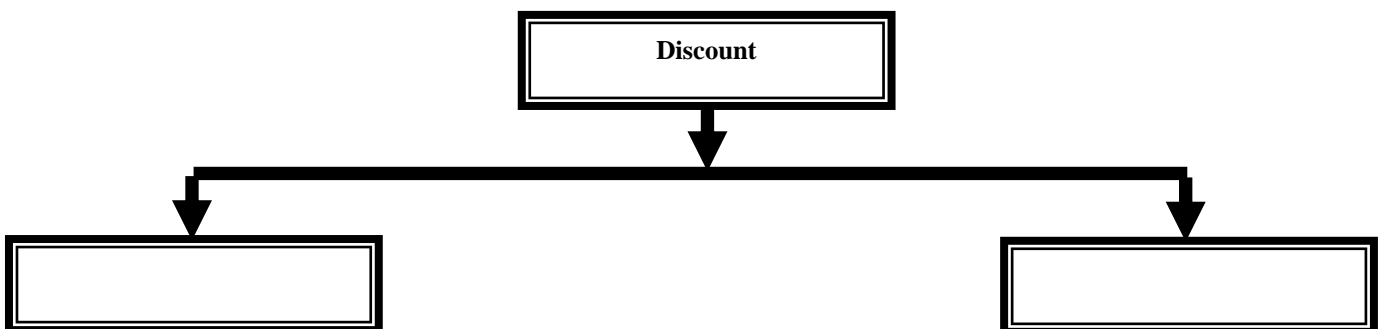
7.2 Application for Golden Rules of Debit and Credit

- We have divided six pillars into two groups. First group contains Assets, Drawing and Expenses have ruled that increase will be Debited and decrease will be Credited
- The second group contains Liabilities, Owner Equity and Revenue has ruled that decrease will be Debited and increase will be Credited. Now we would like to apply these rules one by one



7.3 Discount

- Discount is reduction in listed price
- There are two types i.e. Trade Discount and Cash Discount (if not mention than also cash discount)
- Trade Discount is not considering for entry while entries are passed for cash discount



Example # 7.1: Following transactions are related to Saifullah Naseem business. You are required to pass Journal Entries

June 1, 2016, Mr. Saifullah started business with cash Rs. 10,000 and Furniture Rs. 2,000

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
2016					
June	1	Cash Furniture Owner's Equity (Started business with cash and furniture)		10,000 2,000	12,000

June 5. Purchased merchandise/goods on credit Rs. 5,000 from Ali Store

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit

June 7. Sold goods/ merchandise on credit Rs. 6,000 to Ahmed Brothers

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
2016					
June	7				

June 15. Payment of creditors in full settlement of account Rs. 4,900 of June 5th transaction

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
2016					
June	15				

June 20. Received from debtors in full settlement of account Rs. 5,800 of June 7th transaction

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
2016				
June 20				

June 25. Rs. 500 was privately used by Saifullah

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
2016				
June 25				

June 27. Purchase furniture of worth Rs. 60,000, having 10% trade discount

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
2016				
June 27				

June 28. Paid Salaries Rs. 1,500

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
2016				
June 28				

Example # 7.2: Cases When Purchases are Credit?

There are five cases when purchases are recorded as credited

Case # 1 Goods Lost by Fire of Rs. 400

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Lost by Fire Purchases		400	400

Case # 2 Goods Lost by Theft of Rs. 500

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Lost by Theft Purchases		500	500

Case # 3 Goods distributed as Charity of Rs. 600

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Charity Purchases		600	600

Case # 4 Goods distributed as Free Sample of Rs. 700

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Free Sample Purchases		700	700

Case # 5 Goods withdrawal by Owner of Rs. 800

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Drawing Purchases		800	800

Example # 7.3: In the table below, indicate the accounts that would be debited and credited for each of the transactions?

1. Provide services to customers on account
2. Purchase land by paying cash
3. Purchase an insurance policy that will provide coverage for a two-year period
4. Acquire cash by issuing common stock
5. Receive payment from a customer for services that will be provided over the next six months
6. Cash deposited into bank
7. Purchased goods by cheque
8. Drew cash from bank for office use
9. Purchased goods from Miss Noreen
10. Cash sales made
11. Paid cash to Miss Noreen
12. Recognize expense for amount of office supplies already in stock, that had been used during the period
13. Discount Received by cash
14. Drew cash from bank for personal use of proprietor
15. Received cash from credit customer
16. Paid rent by cash
17. Furniture lost by fire

Solution

<i>S.no</i>	<i>Account Debited</i>	<i>Account Credited</i>
1	Account Receivable	Service Revenue
2	Land	
3		Cash
4	Cash	
5		Unearned Services
6	Bank	
7		Bank
8	Cash	
9		Account Payable_ Miss Noreen
10	Cash	
11		Cash
12	Supplies Expense	
13		Discount
14	Drawing	
15		Account Receivable
16	Rent	
17		Furniture

Practice MCQs

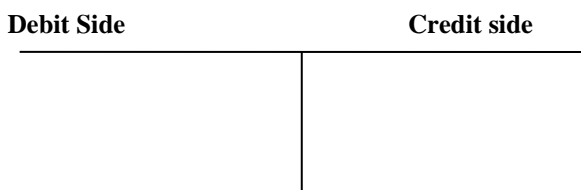
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GENERAL LEDGER

- Ledger accounts are used to post the economic activities
- Posting is the name of transferring accounts from the book of prime entry to related ledger accounts
- When all the transactions for a given period have been journalized, the next step is to classify them according to the account affected
- Ledger is a book that keeps separate record for each account
- Ledger is the book of secondary entry
- An account in its simplest form is a T-shape. It should be noted that Journal contains a chronological record while Ledger contains a classified record of all economic activities



8.1 Types of Ledger and Procedure

There are two types of ledger accounts

8.1.1 Standard General Ledger

Since the Ledger keeps record of transactions that affect one head of account, therefore, it should provide all the information that a user may need. Usually the ledger is required to provide following information.

- | | | | |
|-----------------|----------------------|------------|----------|
| (a) Account # | (b) Title of Account | (c) Page # | (d) Date |
| (e) Description | (f) Reference | (g) Amount | |

Account #			Title of Account				Page #	
Date	Description	Ref	Amount	Date	Description	Ref	Amount	
Total				Total				

8.1.1.2 Process of Posting

The process of posting is simple and involves following steps

- ❖ The debit part of journal entry is recorded on the debit side of the relevant account by credit account name (Source)
- ❖ The credit part of journal entry is recorded on the credit side of the relevant account by debit account name (Source)
- ❖ In the reference column of the general journal the code or page number of ledger account are noted
- ❖ In the reference column of the ledger account the page number of the journal is noted

Example # 8.1: Post following entries to Cash Standard Ledger Account?

General Journal			Page # 177		
Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
2015					
July	1	Cash Owner's equity		100,000	100,000
	5	Purchases Cash		15,000	15,000
	8	Cash Sales		25,000	25,000
	12	Account Receivable_ Raheel Store Sales		13,000	13,000
	16	Drawing Cash		4,000	4,000
	19	Cash Commission		2,000	2,000
	21	Machine Account Payable_ Ali sons		10,000	10,000
	23	Cash Account Receivable_ Raheel Store		10,000	10,000
	27	Salary Cash		1,000	1,000
	29	Account Payable_ Ali Sons Cash		8,000	8,000
Total				Rs. 188,000	Rs. 188,000

Account # 102		Cash Account				Page # 880	
Date	Description	Ref	Amount	Date	Description	Ref	Amount

8.1.1.3 Balancing an Account

- Find the total of debit side and Find the total of credit side. Put bigger value both sides in Total
- Calculate the difference between the two sides. This is the Balance (The balancing figure between the two sides)
- Write the balance on the smaller side with key words “Balance c/d”. However, the balance will be known by the larger side i.e. if the debit side is greater than the credit side, the balance will be known as debit balance and vice versa
- Bring down the debit balance on the debit side writing the words in Description column “Balance b/d”. Similarly, bring down the credit balance on the credit side be writing the words in the Description column “Balance b/d”.

Example # 8.2: Sardar Hammad is sole owner of business. He has been started business since 1990 in Karachi. Following are transaction for the month of August 2016, prepare General Journal, General Ledgers and Trial Balance

3. Reinvestment in the shape of Cash Rs. 80,000 and Furniture Rs. 20,000
5. Cash Sales Rs. 10,000 and on account Sales Rs. 12,000
6. Bought goods from Ahmed Co. Rs. 60,000 paid Rs. 15,000 cash and remaining Note payable pay within 30 days
9. Purchase Office Equipment from Waseem Shah worth Rupees Rs. 99,000, a cash down payment of Rs. 19,000 and balance will be paid by four installments, first due on 30 August
21. Goods return by credit customer of worth Rs. 12,000
30. Paid first installment of Rs. 20,000

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs.)	
			Debit	Credit
2016				
<i>Aug.</i>	3			
	Cash		80,000	
	Furniture		20,000	
	Owner's Equity_ Sardar Hammad (Reinvest by owner in the business)			100,000
	5			
	Cash		10,000	
	Account Receivable		12,000	
	Sales (Cash and credit Sales)			22,000
	6			
	Purchases		60,000	
	Cash			15,000
	Note Payable_ Ahmed Co. (Purchases by cash and credit from Ahmed)			45,000
	9			
	Office Equipment		99,000	
	Cash			19,000
	Account Payable_ Waseem Shah (Purchase O. equipment on installments by Waseem)			80,000
	21			
	Sales Return		12,000	
	Account Receivable (Goods return by credit customer)			12,000
	30			
	Account Payable_ Waseem Shah		20,000	
	Cash (Paid 1 st installment to Waseem Shah)			20,000
Total			Rs. 313,000	Rs. 313,000

Account # 1 **Cash Account** **Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>
Total				Total			

Account # 2 **Furniture Account** **Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>
Total				Total			

Account # 3 **Owner's Equity Account** **Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>
Total				Total			

Account # 4 **Account Receivable** **Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>
Total				Total			

Account # 5				Sales Account				Page #
Date	Description	Ref	Amount (Rs.)	Date	Description	Ref	Amount (Rs.)	
Total			22,000	Total			22,000	

Account # 6				Purchase Account				Page #
Date	Description	Ref	Amount (Rs.)	Date	Description	Ref	Amount (Rs.)	

Account # 7				Note Payable Account				Page #
Date	Description	Ref	Amount (Rs.)	Date	Description	Ref	Amount (Rs.)	
Total			45,000	Total			45,000	
				Sep. 1	Balance b/d		45,000	

Account # 8				Office Equipment Account				Page #
Date	Description	Ref	Amount (Rs.)	Date	Description	Ref	Amount (Rs.)	
Total			99,000	Total			99,000	
					Balance c/d		99,000	
Sep. 1	Balance b/d		99,000					

Account # 9				Account Payable				Page #
Date	Description	Ref	Amount (Rs.)	Date	Description	Ref	Amount (Rs.)	
				Sep. 1	Balance b/d		60,000	

Account # 10				Sales Return Account				Page #
Date	Description	Ref	Amount (Rs.)	Date	Description	Ref	Amount (Rs.)	

Sardar Hammad

Trial Balance

As on August 2016

S. No.	Heads of Account	Ref	Amount (Rs.)	
			Debit	Credit
1	Cash			
2	Furniture			
3	Owner Equity			
4	Account Receivable			
5	Sales			
6	Purchases			
7	Note Payable			
8	Office Equipment			
9	Account Payable			
10	Sales Return			
Total				

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8.1.2 Running Balance General Ledger

An alternative ruling of a ledger, which is generally adopted by commercial banks and some other business houses, is the entire ledger us divided into six columns.

Account #		Title of Account			Page #
Date	Description	Ref	Dr. Amount	Cr. Amount	Balance

Example # 8.3: Post following entries to cash Running Balance Ledger Account?

General Journal				Page # 177	
Date		Account Title and Explanations	Ref	Amount (Rs)	
2015				Debit	Credit
July	1	Cash Owner's equity		100,000	10,000
	5	Purchases Cash		15,000	15,000
	8	Cash Sales		25,000	25,000
	12	Account Receivable_ Raheel Store Sales		13,000	13,000
	16	Drawing Cash		4,000	4,000
	19	Cash Commission		2,000	2,000
	21	Machine Account Payable_ Ali sons		10,000	10,000
	23	Cash Account Receivable_ Raheel Store		10,000	10,000
	27	Salary Cash		1,000	1,000
	29	Account Payable_ Ali Sons Cash		8,000	8,000
Total				Rs. 188,000	Rs. 188,000

Account # 102		Cash Account			Page # 880
Date	Description	Ref	Dr. Amount	Cr. Amount	Balance

Example # 8.4: Rameesha Hafeez & Co. is a boat repair yard. During August 2015, its transactions included the following. You are required to prepare General Journal, General Ledger (Running Balance) and Trial Balance.

- 03. Loan taken from Habib Bank Ltd. of Rs. 25,000. Rs. 20,000 withdrawn for business and remaining in the bank account.
- 06. Paid rent for the month of August Rs. 4,400 and accrued rent expenses was Rs. 600.
- 12. At request of Kiwi Insurance, Inc, made repairs on boat of Jon Seaways. Sent bill for Rs. 5,620 for services rendered to Kiwi Insurance Inc. (credit Repair Service Revenue).
- 18. Made repairs to boat of Mill Copper and collected in full the charge of Rs. 2,830.
- 20. Placed Advertisement in The Dawn at a cost of 165, payment to be made within 30 days.
- 25- Received a check for 5,620 from Kiwi Insurance Inc representing collection of the receivable of August 12.
- 30. Sent check to The Dawn in payment of the liability incurred on August 20.

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs.)	
			Debit	Credit

Account No. 1

Cash Account

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Account No. 2

Bank Account

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Account No. 3

Bank Loan Account

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Account No. 4

Rent Expenses Account

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Account No. 5

Rent Payable Account

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Account No. 6

Account Receivable Account

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Account No. 7 Repair Services Revenue Account Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Account No. 8 Advertising Expense Account Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Account No. 9 Advertising Expense Payable Account Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Dr. Amount (Rs.)</i>	<i>Cr. Amount (Rs.)</i>	<i>Balance (Rs.)</i>

Rameesha Hafeez & Co.

Trial Balance

As on August 2015

<i>S. No.</i>	<i>Heads of Account</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	
			<i>Debit</i>	<i>Credit</i>

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TRIAL BALANCE

- At the end of accounting period, a list of all ledger balances or totals is prepared. This list is called trial balance
- Trial balance shows the mathematical accuracy of the books of accounts. For every transaction in the double entry system, equal amount of debit and credits are recorded in the books of account
- Both sides of trial balance i.e. Debit side and credit side must be equal. If both sides are not equal, there are errors in the books of accounts

9.1 Preparation of Trial Balance

For preparation of Trial Balance, following steps are followed.

- ❖ Write down the company / business name at the top middle of paper
- ❖ Write words 'Trial Balance' below company / business name at top middle of paper
- ❖ Write words ' as on ' with date of preparation in the next line just below
- ❖ Write down balances/totals of all ledger accounts

9.2 Form of Trial Balance

There are three types of Trial Balance

9.2.1 Trial Balance with Balances

Under this method, the Trial Balance can be prepared on a loose sheet that may have five columns

- (a) Serial No.;
- (b) Heads of Account;
- (c) Reference;
- (d) Debit Balance and
- (e) Credit Balance

Farhan Saleem and company

Trial Balance

As on ...

S. No.	Heads of Account	Ref	Balance (Rs.)	
			Debit	Credit
Total				

Example # 9.1: From the following Ledger Account of Ms Anum Saleem, you are required to prepare Trial Balance as on June 30th, 2015

Cash Account

Jan. 2	10,000	Jan. 4	1,500
Jan. 2	10,000	Jan. 10	6,000
Jan. 5	8,500	Jan. 15	7,000
Jan. 20	2,200	Jan. 31	1,200
		Bal	15,000
Total	30,700	Total	30,700

Supplies Account

Jan. 4	3,500		
		Bal	3,500
Total	3,500	Total	3,500

Accounts Receivables

Jan. 5	6,000		
		Bal	6,000
Total	6,000	Total	6,000

Fee Revenue

		Jan. 5	14,500
Bal	14,500		
Total	14,500	Total	14,500

Accounts Payable

Jan. 31	1,200	Jan. 4	2,000
Bal	800		
Total	2,000	Total	2,000

Note payable

		Jan. 2	10,000
Bal	10,000		
Total	10,000	Total	10,000

Unearned Revenues

		Jan. 20	2,200
Bal	2,200		
Total	2,200	Total	2,200

Common Stock

		Jan. 2	10,000
Bal	10,000		
Total	10,000	Total	10,000

Furniture and Fitting

Jan. 10	6,000		
		Bal	6,000
Total	6,000	Total	6,000

Machinery

Jan. 15	7,000		
		Bal	7,000
Total	7,000	Total	7,000

Anum Saleem**Trial Balance**As on June 30th, 2015

S. No.	Heads of Account	Ref	Balance (Rs.)	
			Debit	Credit
1	Cash			
2	Supplies			
3	Account Receivable			
4	Fee Revenue			
5	Account Payable			
6	Note Payable			
7	Unearned Revenue			
8	Common Stock			
9	Furniture and Fitting			
10	Machinery			
	Total			

9.2.2 Trial Balance with Totals

- Under this method, the trial balance is prepared by taking the total of each side of the accounts without balancing the accounts
- This method of preparing a trial balance is not commonly used because it cannot help in preparation of financial statements

Example # 9.2: From the Ledger Account of Ms Anum Saleem in example 9.1; prepare Trial Balance with Totals

Anum Saleem
Trial Balance
As on June 30th, 2015

S. No.	Heads of Account	Ref	Total (Rs.)	
			Debit	Credit
1	Cash			
2	Supplies			
3	Account Receivable			
4	Fee Revenue			
5	Account Payable			
6	Note Payable			
7	Unearned Revenue			
8	Common Stock			
9	Furniture and Fitting			
10	Machinery			
	Total			

9.2.3 Trial Balance with Balances & Totals

Under this method, the Trial Balance is prepared by combining the first and second methods

Example # 9.3: From the example 9.1; prepare Trial Balance with Balances & Totals

Anum Saleem
Trial Balance
As on June 30th, 2015

S. No.	Heads of Account	Ref	Balances (Rs.)		Totals (Rs.)	
			Debit	Credit	Debit	Credit
1	Cash		15,000		30,700	15,700
2	Supplies		3,500		3,500	
3	Account Receivable		6,000		6,000	
4	Fee Revenue			14,500		14,500
5	Account Payable			800	1,200	2,000
6	Note Payable			10,000		10,000
7	Unearned Revenue			2,200		2,200
8	Common Stock			10,000		10,000
9	Furniture and Fitting		6,000		6,000	
10	Machinery		7,000		7,000	
	Total		Rs. 37,500	Rs. 37,500	Rs. 54,400	Rs. 54,400

Example # 9.4: Make Trial Balance from mixed transactions for Iram Shehzadi Ltd at year-end (June 30th, 2016)

Iram Shehzadi Ltd

Accounts

As on June 30th, 2016

<i>Description</i>	<i>Amount</i>	<i>Description</i>	<i>Amount</i>	<i>Description</i>	<i>Amount</i>
Account Payable	Rs. 200	Owner Equity	Rs. 300	Land	Rs. 200
Account Receivables	350	Cost of Goods Sold	820	Long-term Debts	1,300
Accrued Liabilities	150	Dep. Expense	110	Prepaid Expenses	40
Acc. Depreciation	250	Interest Expense	80	Salaries Expense	660
Building	1,400	Unearned Revenue	130	Sales Revenue	2,400
Cash	120	Interest Revenue	50	Rent Expense	400
Income Tax Expense	110	Inventories	610	Retained Earning	120

Iram Shehzadi Ltd

Trial Balance

As on June 30th, 2016

<i>S. No</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	
			<i>Dr.</i>	<i>Cr.</i>
1	Account Payable			
2	Account Receivables			
3	Accrued Liabilities			
4	Acc. Depreciation			
5	Building			
6	Cash			
7	Income Tax Expense			
8	Owner Equity			
9	Cost of Goods Sold			
10	Dep. Expense			
11	Interest Expense			
12	Unearned Revenue			
13	Interest Revenue			
14	Inventories			
15	Land			
16	Long-term Debts			
17	Prepaid Expenses			
18	Salaries Expense			
19	Sales Revenue			
20	Rent Expense			
21	Retained Earning			
Total				

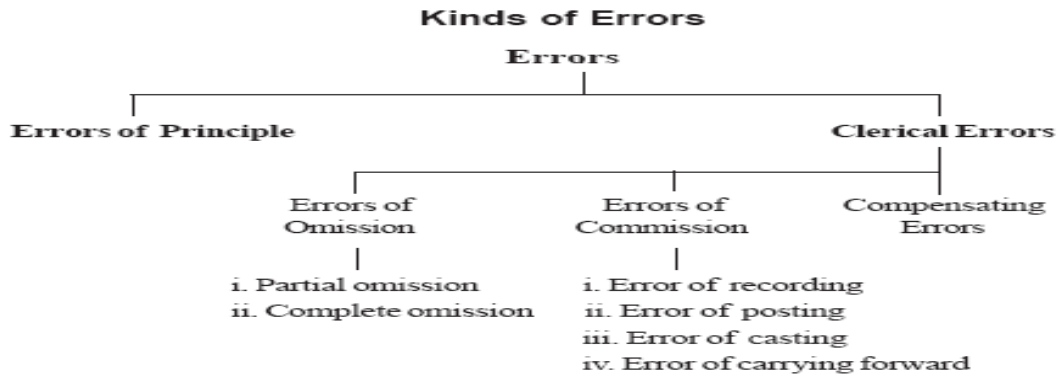
Example # 9.5: Correct following Trial Balance?

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Dr	Cr
1	Ahmed Owner's Equity			1,556
2	Ahmed Drawing		564	
3	Leasehold Premises		750	
4	Sales			2,750
5	Due from Customer			530
6	Purchases		1,259	
7	Purchases Return		264	
8	Loan from Bank			256
9	Creditors		528	
10	Trade Expenses		700	
11	Cash		226	
12	Bill Payable		100	
13	Salaries and Wages		600	
14	Stock Opening			264
15	Rent and Rates		463	
16	Sales Return			98
Total			Rs. 5,454	Rs. 5,454

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Dr	Cr
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				
12				
13				
14				
15				
16				
Total			Rs. 5,454	Rs. 5,454

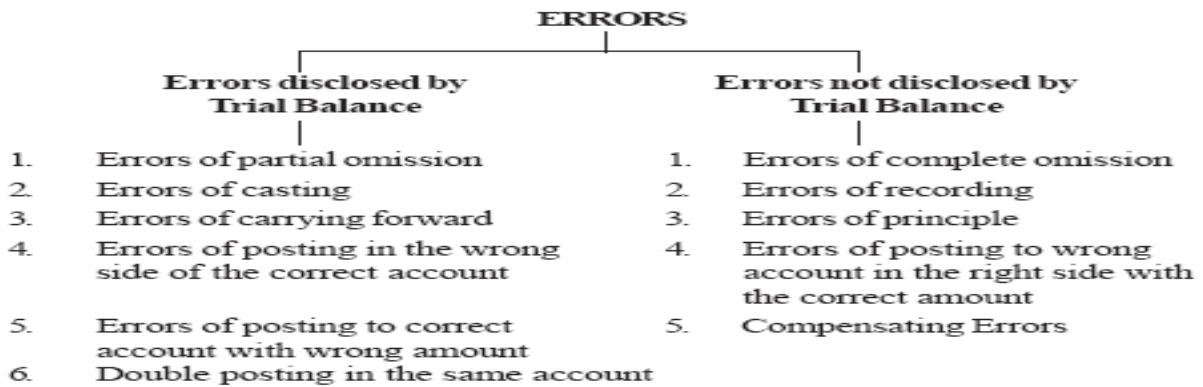
RECTIFICATION OF ERRORS

- ❖ Errors are unintentional misstatement or omission or mistake committed in book-keeping
- ❖ The mistakes may be one relating to routine or one relating to Principle
- ❖ Following are most common error encountered in accounting records



10.1 Errors in Trial Balance

Errors in trial balance are classified as errors disclosed by trial balance and errors not disclosed by trial balance



10.2 Locating Errors

Following nine steps will follow in order to locate errors

Step 1: Make sure balances in trial balance in correct sides

Step 2: Check whether the Debit and Credit sides added correctly by opposite direction

Step 3: Divide the difference by 9. If divisible by 9, so transposition error or slide error. If digits are place wrongly i.e. 5,760..... 5,670

Or

6,250 62.50 (decimal point transposition error)

Step 4: Divide the difference by 2, and check the identical amount in the bigger columns of trial balance

Step 5: Check ledger account if shows an account equal to difference

Step 6: Cross checking the amount in trial balance and ledger accounts

Step 7: Re-compute the balance of each ledger

Step 8: Check posting from journal to ledger

Step 9: Check journal entries in detail

Example # 10.1: The clerk of ABC business wrongly prepared the following Trial Balance. You are required to draw up a trial balance correctly

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Dr	Cr
1	Owner's Equity			60,000
2	Opening Stock		5,000	
3	Discount Allowed			500
4	Commission Received			700
5	Fixed Assets			60,000
6	Sales		85,000	
7	Purchases			45,000
8	Purchases Return			1,000
9	Sales Return		2,000	
10	Carriage Inward			700
11	Carriage Outward			600
12	Wages & Salaries		25,000	
13	Bill Receivables		7,000	
14	Debtors		9,000	
15	Bill Payable			7,000
16	Rent		3,000	
17	Interest Paid			2,000
18	Cash		800	
19	Creditors		6,900	
20	Ending Stock		33,800	
Total			Rs. 177,500	Rs. 177,500

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Dr	Cr
1	Owner's Equity			
2	Opening Stock			
3	Discount Allowed			
4	Commission Received			
5	Fixed Assets			
6	Sales			
7	Purchases			
8	Purchases Return			
9	Sales Return			
10	Carriage Inward			
11	Carriage Outward			
12	Wages & Salaries			
13	Bill Receivables			
14	Debtors			
15	Bill Payable			
16	Rent			
17	Interest Paid			
18	Cash			
19	Creditors			
Total				

Example # 10.2: The Make corrected Trial Balance after anticipating hidden errors

Sabeela Meer

Trial Balance

As on 31st December, 2016

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Dr	Cr
1	Owner's Equity			60,000
2	Inventory 01-01-2016		3,000	
3	Wages			500
4	Commission earned			700
5	Tangible Assets			60,000
6	Sales		85,000	
7	Purchases			45,000
8	Return Outward			1,000
9	Sales Return		2,000	
10	Carriage Inward			700
11	Fuel and Power Expense			600
12	Wages & Salaries		25,000	
13	Note Receivables		7,000	
14	Account Receivable		9,000	
15	Bill Payable			5,000
16	Rent		3,000	
17	Discount Allowed			2,000
18	Cash		800	
19	Creditors		6,900	
20	Inventory 31-12-16		33,800	
Total			Rs. 175,500	Rs. 175,500

Errors:

- (i) Credit sales of worth Rs. 4,500 was omitted to record in the book of original entry.
- (ii) Wages and Salaries account should be separate to Rs. 15,000 and 10,000 respectively.
- (iii) Drawing of worth Rs. 2,000 wrongly charged to Note Receivable Account.
- (iv) Unearned Sales of Rs. 15,000 was incorrectly credited to Sales Account.

Following accounts are used for correction and adjusting the transactions.

Sales; Account Receivable; Wages; Salaries; Drawing; Note Receivable; Unearned Sales

10.3 Rectification of Error

- An accountant can also commit errors while recording business transactions in books of accounts, in their recording, posting or balancing the accounts and so on
- These errors should be located and corrected as soon as possible so that accounts give true and fair results of the operations of the business enterprise
- There are certain errors which will disturb the Trial Balance in the sense that the Trial Balance will not agree. These errors are easy to detect and their rectification is also simple
- However, there are certain errors which are not detected through a Trial Balance. In other words, a Trial Balance would agree in spite of these errors. These errors are very difficult to detect

Example # 10.3: Rectify the following journal entries in the book of Aroosa & Brothers Co.

<i>S. No</i>	<i>Wrong Entry / Transaction</i>	<i>Correct Entry</i>	<i>Rectifying Entry</i>
<i>1</i>			
<i>2</i>			
<i>3</i>			
<i>4</i>			
<i>5</i>			
<i>6</i>			
<i>7</i>			

Example # 11.4: Pass Rectification entries for the following transactions at end April, 2016

1. A builder's bill for Rs. 4,600 for the erection of a small shed was debited to Repairs Expense Account
2. Repairs to plant amounting to Rs. 900 had been charged to Plant and Machinery Account
3. Purchase Day Book undercast by Rs. 1,000
4. Check for Rs. 750 received from Hussain Ltd. Was credit to account of Hassan Ltd
5. The total of Return Inward Book has been overcast Rs. 2,000
6. Goods to the value of Rs. 4,000 returned by X were included in closing stock, but no entry was made in the books
7. Received Rs.2,000 from Shankar debited to his account
8. The sales book undercast by Rs.1,500

General Journal

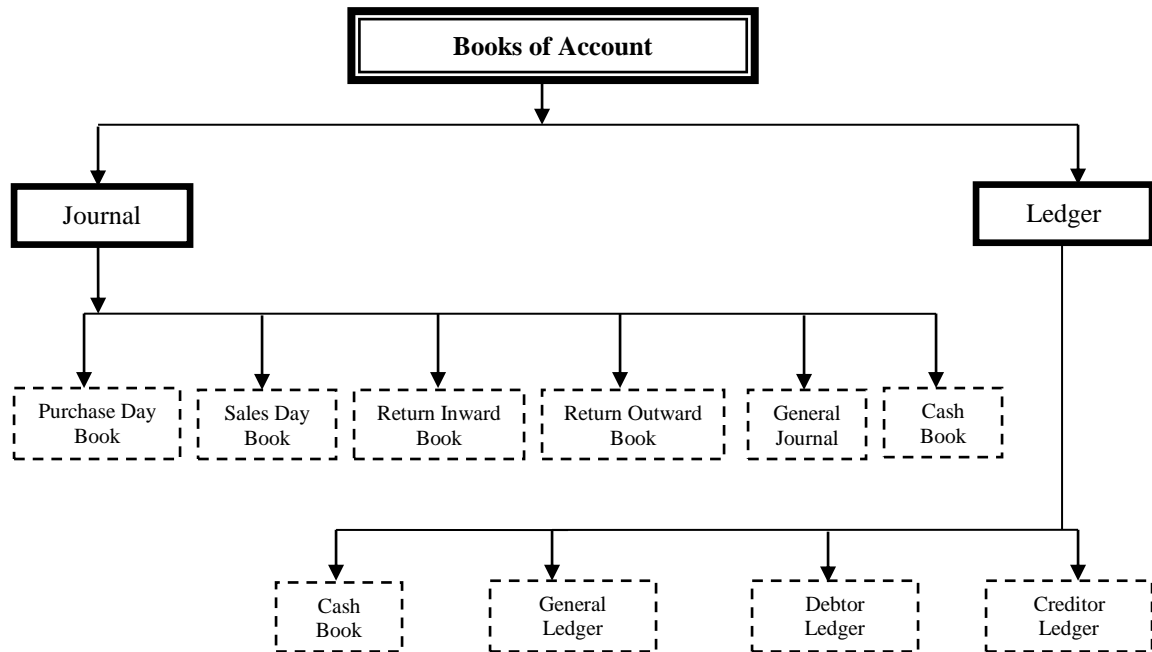
Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
2016					
<i>April</i>	1				
	2				
	3				
	4				
	5				
	6				
	7				
	8				
Total				Rs. 18,750	Rs. 18,750

Practice MCQs

www.accountancyknowledge.com/rectification-of-errors-mcqs/

BOOKS OF ACCOUNTS

- There are two main books of account, Journal and Ledger
- Journal used to record the economic transaction chronologically
- Ledger used to classifying economic activities according to nature



11.1 Subdivision of Journal

- ✓ In large business it is found inconvenient to journalize every transaction in one journal
- ✓ Therefore, the journal is sub-divided into different journals known as the subsidiary books
- ✓ The journal is divided in such a way that a separate book is used for each class of transactions. The important subsidiary books used in modern business world are the following

11.1.1 Purchases Day Book

- Purchases book or purchases day book is a book of original entry maintained to record credit purchases
- You must note that cash purchases will not be entered in purchases day book because entries in respect of cash purchases must have been entered in the cash book
- At the end of each month, the purchases book is totaled. The total shows the total amount of goods purchased on credit
- Purchases book is written up daily from the invoices received
- The invoices are consecutively numbered
- The invoice of each number is noted in the purchases book

Purchase Journal (Format)

Date	Account Credited	Invoice #	Ref	Amount
Total				

Example # 11.1: From the following transactions of a trader prepare the Purchases day book

2014

January 5	Purchased goods from Qurat Ul Ain & Co	Rs. 2,400
" 15	Purchased goods from Saba Sajjad	6,000
" 25	Purchased goods from Omer Nawaz & Co	1,500
" 30	Purchased goods from Maqbool & Co	3,000

Purchase Journal

Date	Account Credited	Invoice #	Ref	Amount
Total				

11.1.2 Sales Day Book

- A sales book is also known as sales day book in which are recorded the details of credit sales made by a businessman
- Total of sales book shows the total credit sales of goods during the period concerned
- Usually the sales book is totaled every month. The sales day book is written up daily from the copies of invoices sent out

Sales Journal (Format)

Date	Account Debited	Invoice #	Ref	Amount
Total				

Example # 11.2: From the following transactions of a trader prepare the sales day book of M. Amin

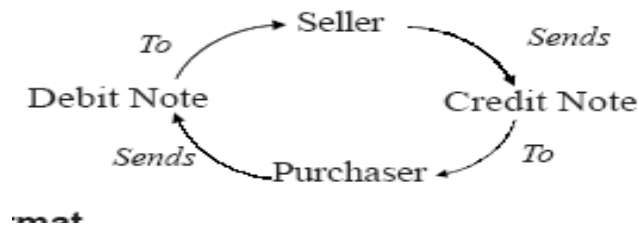
2017				
March	5	Sold goods to Ideal College		Rs. 200
"	10	Sold goods to Ahmad & Co		100
"	20	Credit sales to Ayesha Bibi		400
"	31	Sold goods to Gulbaz Khan		100

Sales Journal

Date	Account Debited	Invoice #	Ref	Amount
Total				

11.1.3 Return Inward Book

- Sales returns book is also called returns inwards book. It is used for recording goods returned to us by our customers
- Customers who return goods should be sent a credit note. It is a statement sent by a business to customer showing the amount credited to the account



Return Inward Journal (Format)

Date	Account Credited	Credit Note #	Ref	Amount
Total				

Example # 11.3: From the following transactions of a trader prepare the sales returns book

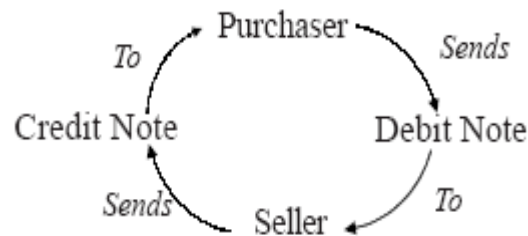
2016		
June 8	Goods returned by Sana Khalid & Co	Rs. 40
" 20	Goods returned by Ideal Traders	52

Return Inward Journal

Date		Account Credited	Credit Note #	Ref	Amount
2016					
June	8				
	20				
Total					

11.1.4 Return Outward Book

- ✓ Purchases returns book is a book in which the goods returned to suppliers are recorded. It is also called returns outward book or purchases returns day book
- ✓ Goods may be returned because they are of the wrong kind or not up to sample or because they are damaged etc.
- ✓ When the goods are returned to the suppliers, intimation is sent to them through what is known as a debit note
- ✓ These debit notes serve as vouchers for these entries. A debit note is a statement sent by a businessman to vendor, showing the amount debited to the account



Return Outward Journal (Format)

Date		Account Debited	Debit Note #	Ref	Amount
Total					

Example # 11.4: From the following transactions of a trader prepare the purchases returns day book

2016		
July 14	Karim & Sons	Rs. 135
" 27	Maria Waheed & Co	150
" 31	Saeed Bros	25

Return Outward Journal

Date	Account Debited	Debit Note #	Ref	Amount

11.1.5 Proper/ General Journal

- ❖ Journal proper is book of original entry (simple journal) in which miscellaneous credit transactions which do not fit in any other books. It is also called miscellaneous journal or General Journal
- ❖ For example purchase assets on credit, Correcting Entries, Adjusting Entries and Closing Entries etc.

Example # 11.5: Record the following transactions in the appropriate journal?

2017

March	3	Purchased goods from Ali & Co for Rs. 4,500
“	8	Sold merchandise to Naeem & Sons worth of Rs. 6,000
“	12	Purchase merchandise from B & Brothers Rs. 3,000
“	14	Credit sales of goods to Z & Co for Rs. 2,500
“	15	Naeem & Sons returned goods Rs. 1,000
“	18	Return merchandise to Ali & Co Rs. 500
“	22	Purchase Furniture from Mr. Saeed of Rs. 3,200
“	24	Returned goods to B & Brothers of Rs. 200
“	27	Purchase Machinery on account from MMM Machines Rs. 7,000
“	29	Z & Co returned merchandise of Rs. 300

Purchase Journal

Date	Account Credited	Invoice #	Ref	Amount

Sales Journal

Date		Account Debited	Invoice #	Ref	Amount

Return Inward Journal

Date		Account Credited	Credit Note #	Ref	Amount

Return Outward Journal

Date		Account Debited	Debit Note #	Ref	Amount

General Journal

Date		Account Titles and Explanation	Ref	Amount (Rs)	
				Debit	Credit

Practice MCQs

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Practice Problems with Solutions

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COMSATS University Islamabad, Abbottabad Campus

Department of Management Sciences

First Sessional Prototype

Class: BS
Subject: Accounting
Total Time Allowed: 80 Minutes
Registration #

Date:
Instructor: *Zaheer A. Swati*
Max Marks: 50

SECTION-A

(Time allowed: 20 Minutes) (Marks: 20)

Q1. Encircle the most appropriate choice (MCQs).

(Marks: 10)

1. Which of the following items should be expensed as incurred?
 - (a) Broker's fees on the purchase of a long-lived asset
 - (b) Repair of damage occurring during installation of new equipment
 - (c) Freight charges on the purchase of equipment
 - (d) Normal installation fees on the purchase of equipment
2. Accounting which recognizes an event as the transaction when cash is received or paid?
 - (a) Cash basis of accounting
 - (b) Accrual basis of accounting
 - (c) Cost accounting
 - (d) None of the above
3. Losses normally have?
 - (a) Credit balance
 - (b) Debit balance
 - (c) Not mentioned
 - (d) None of the above
4. Transactions are initially recorded in the?
 - (a) Book of Final Entry
 - (b) Accounting Equation
 - (c) T Accounts
 - (d) Book of Original Entry
5. Which of the following account will be credited in the books of XYZ Co. Ltd, if the business purchased a vehicle through cheque?
 - (a) Vehicle account
 - (b) Cash account
 - (c) Bank account
 - (d) Business account
6. The payment to a creditor will
 - (a) Increase one asset and decrease another
 - (b) Decrease an asset and decrease owner's equity
 - (c) Decrease an asset and decrease a liability
 - (d) Increase an asset and increase a liability
7. Which of the following item will be shown on debit side of debtors account?
 - (a) Discount received
 - (b) Return inwards
 - (c) Discount allowed
 - (d) Credit sales
8. Which of the following account has a normal credit balance?
 - (a) Sales
 - (b) Return outward
 - (c) Purchase return
 - (d) All of before
9. What is the treatment of ending stock in trial balance?
 - (a) Dr
 - (b) Cr
 - (c) Not considered
 - (d) Subtracted from opening stock
10. For which of the following accounts is the normal balance a debit?
 - (a) Rent Payable
 - (b) Unearned Rent Revenue
 - (c) Rent Revenue
 - (d) Prepaid Rent

Q2. On March 2017, Muhammad Saddam starts wholesaling business. Following transactions as follows (Marks: 10)

1. A Saddam started business with capital of Rs. 15,000 and Land worth Rs. 10,000
8. Bought goods from Bilal and Friends Rs. 1,000 and by cash from XYZ Co. Rs 2,000
13. Sold goods to Rehman & sons Rs. 1,500 and sale by cash Rs. 5,000
17. Gave away charity of cash Rs. 50 and merchandising worth Rs. 30
21. Paid Bilal and Friends cash Rs. 975; discount received Rs. 25
28. Received cash from Rehman & Sons Rs. 1,450; allowed him discount of Rs. 50

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs.)	
			Debit	Credit

SECTION-B

(Time allowed: 50 Minutes) (Marks: 30)

Q1: Creative Advertising, owned by Miss Abida Masood, provides advertising consulting services. During January 2017, the following events occurred: (15 Marks)

- Jan. 2 Owner contributed Rs. 50,000 and a new computer costing Rs. 20,500 to start her business
- Jan. 4 Office supplies were purchased on account for Rs. 4,000
- Jan. 10 Creative Advertising obtained 12% 5-year loan of Rs. 20,000 from the bank
- Jan. 12 Creative Advertising paid the utility bills for Rs. 2,750
- Jan. 15 Paid the Rs. 3,000 in Accounts Payable from the purchase of office supplies on Jan. 4
- Jan. 24 Advertising services completed in January were billed to clients Annie's Flowers at Rs. 18,300
- Jan. 27 Creative Advertising received Rs. 5,500 from Annie's Flowers, a client, as payment on account
- Jan. 30 Miss Abida Masood withdrew Rs. 6,000 of cash for personal use

General Journal

Date		Account Title and Explanations	Ref	Amount (Rs.)	
				Debit	Credit
2017					
Jan	2	Cash Computer Owner's Equity_ Miss Abida Masood (Started business with cash and computer)		50,000 20,500	70,500
	4	Office Supplies Account Payable (Office Supplies purchase on credit)		4,000	4,000
	10	Cash Bank Loan (Bank loan obtained)		20,000	20,000
	12	Utility Bills Cash (Utility bill paid)		2,750	2,750
	15	Account Payable Cash (Paid partial account payable)		3,000	3,000
	24	Account Receivable_ Annie's Flowers Advertising services (Bill to customer for services earned)		18,300	18,300
	27	Cash Account Receivable_ Annie's Flowers (Received cash from customer billed previously)		5,500	5,500
	30	Drawing Cash (Withdrew of cash by owner)		6,000	6,000
	Total				Rs. 130,050

Account # 1

Cash Account

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 2

Computer Account

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 3

Owner's Equity

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 4

Office Supplies

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 5

Account Payable

Page #

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 6**Bank Loan Account****Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 7**Utility Bills Account****Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 8**Account Receivable****Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 9**Drawing Account****Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Account # 10**Advertising Services Account****Page #**

<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	<i>Date</i>	<i>Description</i>	<i>Ref</i>	<i>Amount (Rs.)</i>

Creative Advertising***Trial Balance****As on January, 2017*

<i>S. No.</i>	<i>Heads of Account</i>	<i>Ref</i>	<i>Amount (Rs.)</i>	
			<i>Debit</i>	<i>Credit</i>

Q2: Make corrected Trial Balance after anticipating hidden errors for Farhat Zaib Ltd. Financial year for this company is July 1st, 2014 to June 30th, 2015

(15 Marks)

Farhat Zaib Ltd

Trial Balance

As on 30th June, 2015

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Dr	Cr
1	Purchases			35,000
2	Factory Overhead (Applied)			1,000
3	Octri and Taxes			100
4	Rebate received			500
5	Trade Mark			55,000
6	Sales		80,000	
7	Share Capital			50,000
8	Return Outward			1,600
9	Bills Owed			6,500
10	Carriage Outward			3,700
11	Inventory (1.07.2014)		10,500	
12	Motor Van		25,000	
13	Claims Receivables		1,500	
14	Sundry Debtors		9,000	
15	Return Inward		2,000	
16	Leasehold Premises		3,000	
17	Discount on Sales			2,000
18	Petty Cash		800	
19	Stock 30-06-2015		33,300	
20	Sundry Creditors		10,000	
21	Suspense Account			19,700
Total			Rs. 175,100	Rs. 175,100

Errors in Trial Balance:

- (i) Machinery bought Rs. 3,000 posted to as Trade Mark account
- (ii) Credit sales of worth Rs. 1,200 was omitted to record in the book of original entry
- (iii) Repairs to Motor Van Rs. 1,500 have been debited to Motor Van account
- (iv) Unearned Sales of Rs. 15,000 was incorrectly credited to Sales Account

Following accounts are used for correction and adjusting the transactions.

Sales; Unearned Sales, Motor Van; Sundry Debtors; Motor Van Expense; Machinery; Trade Mark

E-Books

Exercises

Past Papers

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Problems

OTQs

Workbook

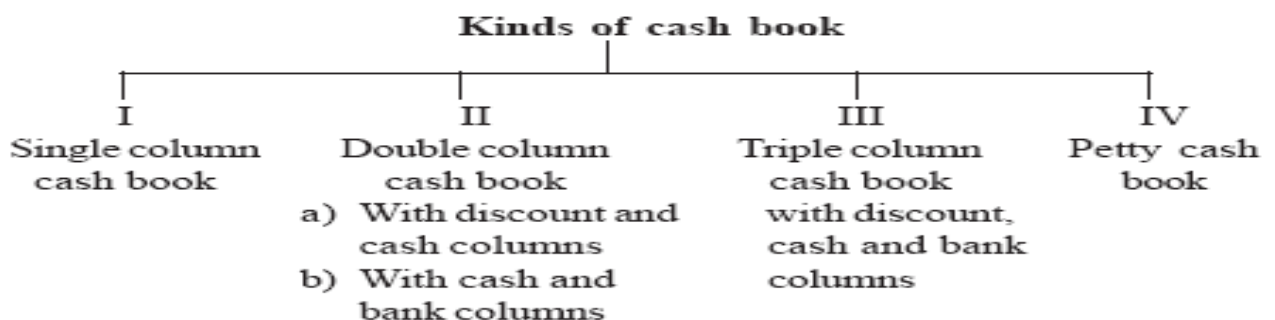
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CASH BOOK (I)

- ◆ Cash book is a book of original entry in which transactions relating only to cash receipts and payments are recorded
- ◆ When cash is received it is entered on the debit or left hand side
- ◆ Similarly, when cash is paid out it is recorded on the credit or right hand side of the cash book
- ◆ Cash Book is dual purpose book; it is Journal as well as Ledger
- ◆ It is journal as cash transactions are chronologically recorded in it. It is a ledger as it contains a classified record of all cash transactions. It Journalized Ledger
- ◆ As for as cash is concerned, consists of coins, currency, checks, money orders, and money on hand or on deposit in a bank
- ◆ Cash is reported in both the balance sheet and the statement of cash flows. The balance sheet shows the amount of cash available at a given point in time. The statement of cash flows shows the sources and uses of cash during a period of time
- ◆ Cash on hand, cash in banks, and petty cash are often combined and reported simply as Cash
- ◆ Cash is the most liquid asset and is listed first in the current assets section of the balance sheet
- ◆ Many companies use the designation “Cash and cash equivalents” in reporting cash. Cash equivalents are short-term, highly liquid investments (Marketable Security) that are both:
 1. Readily convertible to known amounts of cash, and
 2. So near their maturity that their market value is relatively insensitive to changes in interest rates
- ◆ A negative balance in the cash account should be rare. If so, it should be reported among current liabilities
- ◆ This book enables us to know the balance of cash in hand and at bank at any point of time
- ◆ Cash book consists of cash and bank accounts taken out of ledger and maintained separately
- ◆ For Every entry made in the cash book there must be a proper voucher
- ◆ Being the cash book with the balance brought forward from the preceding period or with what we start. It appears at the top of the left side as "Balance b/d" or "Capital b/d" in case of a new business
- ❖ It should be balanced at the end of a given period

12.1 Kinds of Cash Book

The type of cash book to be used by any business will depend upon its nature and requirements. It may be any one of the following



12.1.1 Single Column Cash Book (Cash Column)

- Single column cash book records only cash receipts and payments
- It has only one money column on each of the debit and credit sides of the cash book

- Cheque/Check is drawn for office use
- Cash is deposited into bank by office
- Not deposited check when deposited
- If an amount is entered on the debit side of the cash book, and the exact amount is again entered on the credit side of the cash book, it is called "contra entry"
- Such entries are marked in the cash book with the letter "C"

Example # 12.2: On January 1, 2017, Humna Faisal’s cash book showed debit balance of cash Rs. 1,500 and bank Rs. 12,500. During the month of January following business was transacted
2017

- Jan.1 Deposited cash Rs. 500 to business bank account
- " 7 Purchased office furniture for cash Rs. 700; cash sales Rs. 2,000
- " 9 Received from Mr. Shabir a cheque for Rs. 2,550 in part payment of his account and not deposited
- " 12 Paid by cheque for goods purchased to Mr. Gulzar worth Rs. 1,000
- " 18 Drew from bank for owner domestic use Rs. 200
- " 21 Sold merchandise to Zeshan Bros. for Rs. 1,500 who paid by cheque which was deposited in the bank
- " 24 Paid to Mr. Salman Rs. 900 by cheque
- " 28 Deposited into bank the cheque received from Mr. Shabir
- " 29 Paid salaries by cash Rs. 950
- " 30 Drew from bank for office use Rs. 450

Requirement: Draw up Cash Book with Cash and Bank Columns

Humna Faisal
Cash Book (Double Column)
For the month ended January, 2017

Receipts					Payments				
Date	Description	Ref	Cash	Bank	Date	Description	Ref	Cash	Bank
2017					2017				
Jan					Jan				
	Total					Total			

Practice MCQs
www.accountancyknowledge.com/cash-book-mcqs-1/

Practice Problems with Solutions
www.accountancyknowledge.com/single-column-cash-book-problems-and-solutions/

CASH BOOK (II)

13.1 Triple Column Cash Book (Cash Bank and Discount Columns)

- A triple column cash book or three column cash book is one which consists of three separate columns on the debit side as well as credit side for recording cash, bank and discount.
- The discount column on the debit side of the cash book will record discounts allowed and that on the credit side discounts received
- Discount columns in both side are not balanced only totaled

Hafsa Noor Ayub

Cash Book (Triple Column)

For the month ended

Receipts						Payments					
Date	Description	Ref	Cash	Bank	Discount	Date	Description	Ref	Cash	Bank	Discount

Example # 13.1: From the following transactions write up a three column cash book for Zakir Khan & Co 2016

- June 1 Cash in hand Rs. 2,000 and Bank Overdraft Rs. 1,500
- " 7 Received cash from Riaz & Co. Rs. 190; discount allowed Rs.10
- " 12 Sales by check Rs. 1,000
- " 15 Deposited cash Rs. 1,200 to bank account
- " 20 Paid to Waqas Shahzad Rs. 485; discount received Rs. 15
- " 25 Received check from Salman of Rs. 500 and deposited
- " 27 Paid to Hassan by bank Rs. 300
- " 28 Mr. Salman check of dated 25th has been dishonored due to technical reasons

Zakir Khan & Co

Cash Book (Triple Column)

For the month ended June, 2016

Receipts						Payments					
Date	Description	Ref	Cash	Bank	Dis	Date	Description	Ref	Cash	Bank	Dis
2016						2016					
June						June					
							Balance c/d				
	Total						Total				
July											

Example # 13.3: For the following transactions, you are required to describe side of cash book (Debit or Credit) and the column in which amount is entered (Cash, Bank or Discount)

<i>S. No</i>	<i>Transactions</i>	<i>Side of Cash Book (Debit or Credit)</i>	<i>The column in which amount is entered (Cash, Bank or Discount)</i>
1	Cash received from customer	Debit	Cash
2	Cash paid to vendor		
3	Discount allowed		
4	Check received		
5	Cash deposited in the bank	Debit (c) Credit (c)	Bank Cash
6	Discount received		
7	Cash withdrawn for office use		
8	Check received and deposited immediately	Debit	Bank
9	Salary paid by check		Bank
10	Cash sales	Debit	
11	Customer directly paid into bank		
12	Deposited check dishonored		Bank
13	Issued check dishonored		Bank
14	Favorable balance of cash in cash book		Cash
15	Bank charges	Credit	
16	Interest received from bank by company		
17	Interest on overdraft	Credit	Bank
18	Unfavorable balance of bank in cash book		
19	Amount directly received by bank as per standing instruction		
21	Rent received by check	Debit	Bank
22	Discount on purchases	Credit	
23	Payment directly made by the bank as per standing instruction		Bank
24	Discount on sales	Debit	
25	Credit sales		
26	Sales by check and check is retained in business	Debit	Cash
28	Bank balance overdraft in cash book	Credit	
29	Cash balance overdraft in cash book		Cash
30	Commission earned but not received		

BANK RECONCILIATION STATEMENT (I)

- ✘ The bank and the company maintain independent records of the company's checking account. The two balances are almost never same because of:
 - ⊗ Time lags that prevent one of the parties from recording the transaction in the same period
 - ⊗ Errors by either party in recording transactions. Bank errors are infrequent
- ✘ The cash Book and Pass Book / Bank Statement are prepared separately
- ✘ The Businessman prepares the Cash Book and the Pass Book is prepared by the Bank (here by cash book we mean two or three column cash Book)
- ✘ But as both the books are related to one person and same transactions are recorded in both the books so the balance of both the books should match i.e. the balance as per Pass Book should match to balance at bank as per cash book

	Favorable Balance	Unfavorable Balance
Cash Book		
Pass Book / Bank Statement		

- ✘ But many a times these two balances do not agree then, it becomes necessary to reconcile them by preparing a statement which is called Bank Reconciliation Statement
- ✘ A Bank Reconciliation Statement may be defined as a statement showing the items of differences between the cash Book balance and the pass book balance, prepared on any day for reconciling the two balances

14.1 Items of Difference

- ✓ A transaction relating to bank has to be recorded in both the books i.e. Cash Book and Pass Book
- ✓ But sometimes it happens that a bank transaction is recorded only in one book and not recorded simultaneously
- ✓ This causes difference in the two balances usually arises due to timing or errors

14.2 BRS Missing Approach

- In missing method first of all we dig out missing or error items (Find Missing or Error Items)
- After that find the it is missing of cash book or bank statement (Find Missing Book)
- Finally, analyze that it is missing of debit or credit (Find Missing Side)

14.2.1 Unpresented / Outstanding / Not Cashed or Uncashed Cheques:

- Cheque issued (for payments) by business but not presented for payment
- A cashier may send cheques out to suppliers, some of whom may present cheque at the bank immediately while others may keep the cheque for several days
- Cashier will have recorded all the payments in the cash book immediately when issue the cheques
- However, the bank records will only show the cheques that have actually been presented by the suppliers

14.2.2 Uncredited / Uncollected / Uncleared or Outstation Cheques:

- ✓ Check deposited (for receipts) but not collected by bank
- ✓ The firm's cashier records a receipt in the cash book as he or she prepares the bank paying-in slip
- ✓ However, the receipt may not be recorded by the bank on the bank statement for a day or so

14.2.3 Bank Charges:

- ❖ The bank charges some amount from each customer by way of incidental charges, collection charges or interest on overdraft etc. Bank debited the amount in pass book
- ❖ But customer comes to know about it only at the end of month

14.2.4 Interest Credit by Bank:

- When the bank allows interest to a customer, it credits the customer’s account
- But customer comes to know about it only at the end of month than he would pass appropriate entry

14.2.5 Direct Deposits to Bank:

- ✚ When the bank has received a direct amount on the behalf of the business
- ✚ Bank will have recorded the receipt in the business’s account at the bank but the business will be unaware

14.2.6 Direct payment by Bank:

- Bank may have deducted items from the customer’s account, but the customer may not be aware of the deduction until the bank statement arrives
- Examples of these deductions include are standing order and direct debit payments

14.2.7 Check Dishonored:

- Cheque may be dishonored due to so many reasons
- It is missing of cash book reverse impact as recorded before dishonored

14.2.8 Errors and Omissions:

- Sometimes the difference between the two balances may be accounted for by an error or omission on the part of the bank statement or in the cash book of the business
- Find the missing in order to rectify error or record omission

<i>Cash Book</i>	<i>Bank Statement</i>
Favorable	Unfavorable
Unfavorable	Favorable
<i>Cash Book (Missing)</i>	<i>Bank Statement (Missing)</i>

Example # 14.1: From the following particulars prepare a Bank Reconciliation Statement to find out the causes in two balances as on March 31st, 2017 for Abdullah Khan (Pvt.) Ltd

- i) The bank overdraft as per cash book on March 31st, 2008 was Rs. 6,000
- ii) Interest on overdraft for six months ending March 31st, 2008 Rs. 200 is debited in the Bank Statement
- iii) Bank charges for the above period also debited in the Bank Statement amounted to Rs. 50
- iv) Check issued, but not cashed, prior to 31.03.2008 amount to Rs. 1,500
- v) Check deposited into bank, but not cleared and credited before March 31st were for Rs. 2,500
- vi) Interest on investment collected by the bankers and credited in the Bank Statement amounted to Rs. 1,800

Cash Book (Bank Column Missing)

Bank Statement (Missing)

--	--

Abdullah Khan (Pvt.) Ltd

Bank Reconciliation Statement

As on March 31st, 2017

Add:		
Less:		

Example # 14.2: You are required to mention missing (Cash Book or Bank Statement & Dr /Cr)

Transactions	Missing		
	Cash Book	Bank Statement	Dr / Cr
Unpresented cheque			
Bank charges			
Interest credit by bank			
Direct deposits to bank			
Direct payment by bank			
Uncredited checks			
Uncollected checks			
Issued check dishonored			
Credit side of the Bank column in cash book cast short			
Check received entered twice in the cash book			
Outstanding check			
Deposited check dishonored			
Uncleared cheque			
Interest allowed by the bank			
Bank services charges for the month			
Bank credited interest			
Charged commission on collection of outstation check by bank			
The debit side of the cash book had been undercast			
The bank debited			
A check issued to Ahmed & Co. was not encashed			
Outstation cheque			
Interest charged by the bank			
An unpaid cheque appeared on the bank statement			
A check was credited twice in Cash book			
Bills receivable directly collected by bank			
Uncashed cheque			
Cheque issued but not cashed			
Cheque paid into bank but not cleared			
Deposits in transit			
Cheque paid in but not entered in the Cash Book			
NSF			

Practice MCQs

www.accountancyknowledge.com/bank-reconciliation-statement-mcqs-1/

Practice Problems with Solutions

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BANK RECONCILIATION STATEMENT (II)

Example # 15.1: Prepare Bank Reconciliation Statement to find out adjusted balances in both books of Zakirullah Traders on June 30th, 2015?

- a) Unfavorable balance as per Bank Statement Rs. 55,000, while cash book credit balance of Rs. 47,100
- b) Mark-up charged by bank Rs. 600
- c) Check of customer Basher & Company for Rs. 3,500 was dishonored and returned by bank
- d) Dividend collected by bank not recorded in the cash book amounted to Rs. 2,000
- e) Checks issued amounted to Rs. 10,000 but presented to bank for payment worth Rs. 5,800
- f) A checks deposited into the bank of worth Rs. 30,000 but Rs. 10,000 check was not collected by bank

<i>Cash Book</i>	<i>Bank Statement</i>

Zakirullah Traders
Bank Reconciliation Statement
 As on June 30th, 2015

Add:		
Less:		
Adjusted Balance		
Add:		
Less:		
Adjusted Balance		

Example # 15.2: Ms. Fiza Naseem works as a cashier for Pine & Co. Abbottabad. Her responsibilities include entering and maintaining the firm's cash book and preparing a bank reconciliation statement at the end of each month. The firm's cash book for July 2016 which she has just finished entering and balancing for the month end is shown below (Note: for the sake of clarity the cash and discount columns have been omitted from cash book.) A copy of the firm's bank statement from the Star Bank Limited dated 31st July 2016 has just been received and is also illustrated. The numerical difference between the two is; Bank statement Rs. 903.00 minus cash book Rs. 641.70 = Rs. 261.30
This is the difference which Fiza will have to 'reconcile'.

Step 1 – Tick off the items in both cash book and bank statement

Cash Book

Receipts				Payments			
Date	Description	Ref	Bank	Date	Description	Ref	Bank
2011				2011			
July	1		756.20	July	2		50.00
	3		220.00		2		130.00
	15		330.00		2		10.00
	31		63.00		8		27.50
					14		89.00
					14		49.00
					15		250.00
					26		122.00
					31		641.70
Total			1,369.20	Total			1,369.20

Bank Statement

Date	Description	Ref	Dr. Amount	Cr. Amount	Balance
2011					
July	1				756.20 (Cr)
	4			220.00	976.20
	9		50.00		926.20
	14		10.00		916.20
	16		89.00		827.20
	19			330.00	1,157.20
	24		250.00		907.20
	26		122.00		785.20
	30		49.00		736.20
	31		12.95		723.25
	31			179.75	903.00 (Cr)

Step 2 – Enter missing items which are not tick

<i>Cash Book (Bank Column Missing)</i>	<i>Bank Statement (Missing)</i>

Step 3 – Make Bank Reconciliation Statement

Pine & Co. Abbottabad
Bank Reconciliation Statement
 As on July 31st, 2016

<i>Add:</i>		
<i>Less:</i>		

Step 4 – Balance the cash book bank columns to produce an updated balance

Adjust the cash book by recording therein those items which do not appear in it but which are found in the bank statement, thus computing the correct balance of the cash book

Cash Book

Receipts				Payments			
Date	Description	Ref	Bank	Date	Description	Ref	Bank
2016				2016			
July				July			
Total				Total			
Aug				Aug			

Example # 15.3: A debit balance of Rs. 14,065 appeared in the cash book of Uzair Nawaz & Co. as on March 31st, 2017 whereas the Bank Statement showed a credit balance of Rs. 27,380 as on that date. Following discrepancies were noted:

- a) Check amounting to Rs. 9,977 had been sent to suppliers and entered in the cash book during March, but had not yet been presented to the Bank
- b) A check for Rs. 2,077 was issued by the company for purchase of merchandise and was paid by the bank but not recorded in company's book
- c) Bank deposit of March 30, for Rs. 1,570 was not shown in Bank Statement
- d) Dividend collections amounting to Rs. 7,000 were credited by bank but these were not recorded in the cash book
- e) Bank services charges for March amounting to Rs. 60 were debited by the bank but these were not recorded in the cash book
- f) The bank debited Rs. 345 for insurance premium paid on March 28, on behalf of company, but it was recorded by company as Rs. 480
- g) A check for Rs. 890 of Asif, a customer, which had been deposited in the bank incorrectly recorded in the cash book as Rs. 980

Cash Book

Bank Statement

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Uzair Nawaz & Co.
Bank Reconciliation Statement
 As on March 31st, 2017

Add:		
Less:		

Practice MCQs

www.accountancyknowledge.com/bank-reconciliation-statement-mcqs-2/

Practice Problems with Solutions

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Registration # _____

Q1. Encircle the most appropriate choice.

(Marks = 20)

1. If a company uses special journals, purchase of supplies on account should be recorded in which journal?
(a) Cash receipts journal (b) Purchases journal
(c) Cash disbursements journal (d) General journal
2. Mr. Ali buys goods on credit from Star Co. but finds that some of them are faulty. What document would Mr. Ali return to Star Co. with the faulty goods?
(a) Statement (b) Debit note (c) Sales invoice (d) Purchase invoice
3. At the end of accounting period, after all postings have been made, equality should exist between the balance of the Account Payable control account and _____?
(a) Sum of all the customer balances in the Accounts Receivable Subsidiary Ledger (b) Cash Receipts Journal
(c) Purchases Journal (d) Sum of all the creditor balances in the Accounts Payable Subsidiary Ledger
4. You received an invoice that shows credit terms of 2 / 10 and nil / 60 what does the number 10 in the credit term refers?
(a) The number of days in the credit period (b) The amount of sales discount available
(c) The number of days in the discount period (d) The amount of trade discount
5. Which one of the following affects cash book during a period?
(a) Recording depreciation expense (b) Declaration of a cash dividend
(c) Write-off of an uncollectible account receivable (d) Payment of an accounts payable
6. The discount column of a triple column cash book records?
(a) Trade discount (b) Cash discount (c) Quality discount (d) Seasonal discount
7. The Cash of a business would change as a result of?
(a) A supplier being paid by check and deposited (b) Raw materials being purchased on credit
(c) Non-current assets being purchased on credit (d) Wages being paid in cash
8. When a check is received from a customer and it is deposited into the bank for collection but ultimately returned dishonoured, the customer account will be
(a) Debited (b) Credited (c) Becomes a liability (d) None of these
9. Which of the following transactions does not decrease cash?
(a) Purchasing inventory for cash (b) Accruing operating expenses
(c) Paying trade accounts payable (d) Purchasing securities that are not cash equivalents
10. Unfavorable balance means?
(a) Credit balance in the cash book (b) Credit balance in Bank statement
(c) Debit balance in cash book (d) Debit balance in petty cash book
11. A check that bears a date latter than date of issue is called?
(a) Anti dated check (b) Post-dated check (c) Dishoured check (d) Outdated check

12. When dealing with Bank reconciliation statement while using missing method the credit side of cash book corresponds to?
(a) Debit side of cash book (b) Credit side of Bank statement
(c) Debit side of Bank statement (d) None of them
13. Uncollected checks are also known as?
(a) Outstanding checks (b) Uncleared checks (c) Outstation checks (d) Both b & c
14. Which one of the following is not missing of cash book?
(a) Mistakes in cash book (b) Outstation check
(c) Bank charges debited in bank statement? (d) Interest credited in bank statement
15. If any amount is directly deposited into the bank then?
(a) Cash book will show less balance & bank book will show more
(b) Cash book will show more balance & bank book will show less
(c) Cash book will show double balance (d) Bank book will show double balance
16. Which of the following is the reason that pass book shows more balance & cash book shows less balance?
(a) Any cheque deposited for collection but not yet collected by bank
(b) Any bank charges charged by bank but not recorded in cash book
(c) Any amount directly collected by bank on behalf of customer but not recorded in cash book
(d) Cheque issued but omitted to record in cash book
17. Petty cash may be used to pay?
(a) Salaries to staff (b) Expenses relating to post and telegrams
(c) Purchase of furniture and fittings (d) All of Above
18. In triple column cash book, cash withdrawn from bank for office use will appear in?
(a) Both sides of the cash book (b) Debit side of the cash book only
(c) Credit side of the cash book only (d) All of above
19. Which of the following best describes unpresented cheque?
(a) Cheque received on behalf of the business by the bank
(b) Cheque drawn but yet to be recorded in the bank records
(c) Cheque issued by the bank not recorded in business records
(d) Cheque received but yet to be recorded in the bank records
20. Bank has credited interest Rs. 1,200 and debited Rs. 150 for commission in the pass book. In the BRS starting with pass book balance?
(a) Rs. 1,200 will be added to and Rs. 150 will be deducted from pass book
(b) Rs. 1,200 will be deducted from and Rs. 150 will be added to pass book balance
(c) Rs. 1,350 will be added to pass book balance (d) Rs. 1,350 will be deducted from pass book

Q2. On April 1, 2010, Hassan Sajjad Store Cash Book showed debit balances of Cash Rs. 1,550 and Bank Rs. 13,575. During the month of April following business was transacted. You are required to prepare Cash Book?

(10 Marks)

2017

- April 02 Purchased Office Type-Writer for Cash Rs. 750; Cash Sales Rs. 1,315
- 07 Deposited Cash Rs. 500 to bank.
- 10 Received from A. Hussain a check for Rs. 2,550 in part payment if his account which is not deposited
- 16 Paid by check for merchandise purchased worth Rs. 1,005
- 20 Deposited into Bank the check received from A. Hussain
- 22 Received from customer a check for Rs. 775 in full settlement of his accounts
- 24 Sold merchandise to sweet Bros. for Rs 1,500 who paid by check which was deposited into bank
- 26 Paid creditor a Salman Rs. 915 by check
- 28 Deposited into Bank the check of customer of worth Rs. 775 was dated 22nd April
- 29 Paid wages by cash Rs. 500 and salary Rs. 1,000 by bank
- 30 Drew from Bank for Office use Rs. 250 and Personal use Rs. 150

Hassan Sajjad Store

Cash Book (Double Column)

For the month ended April, 2017

Receipts					Payments				
Date	Description	Ref	Cash	Bank	Date	Description	Ref	Cash	Bank
2017					2017				
April					April				
Total					Total				

Q3. From the following particulars, find out the errors in cash book and bank statement and prepare Bank Reconciliation Statement as on 31-05-2016 for Ammar Ahmed Sugar Mill Ltd. (Marks = 10)

- i.* Balance as per bank statement overdraft of Rs. 2,118
- ii.* The debit side of the cash book had been undercast by Rs. 300
- iii.* A check for Rs. 182 drawn for the payment of telephone bill had been entered in the cash book as Rs. 281 but was shown correctly in the bank statement
- iv.* A check for Rs. 210 by the customer having been deposited into bank was dishonored by the bank
- v.* A check was credited twice in Cash Book for worth Rs. 3,000
- vi.* A Dividend of worth Rs. 90 had been collected by the bank but not recorded in the cash book
- vii.* Checks Rs. 3,000 drawn in December but only 1,200 presented for payment
- viii.* Interest amounting 228 had been debited by the bank but not entered in the cash book
- ix.* A check for Rs. 2,077 was issued by the company for purchase of merchandise and was paid by the bank but not recorded in company's book.
- x.* A check for Rs. 10,500 issued to Salman & Co. for purchase of Equipment was not encashed.

Cash Book

Bank Statement

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Ammar Ahmed Sugar Mill Ltd.
Bank Reconciliation Statement
 As on May 31st, 2016

Add:		
Less:		

ADJUSTMENT ENTRIES (I)

- ❖ In order to ascertain the fair and true results of a business for a particular period, it is essential that all the expenses, revenues related only to that period or year should be considered
- ❖ If Financial Statement for 2016 are prepared, then the expenses and revenues related to 2015 and 2017 should not be considered, the focus will be on 2016 incurred expenses and earned revenues
- ❖ Adjusting entries are needed to ensure that the revenue recognition and expense recognition principles are followed.
- ❖ The trial balance may not contain up-to-date and complete data for several reasons:
 - ◆ Some events are not recorded daily because it is not efficient to do so
 - ◆ Some costs are not recorded during the accounting period because these costs expire with the passage of time rather than as a result of recurring daily transactions
 - ◆ Some items may be unrecorded
- ❖ Adjusting entries are required every time a company prepares financial statements
- ❖ Every adjusting entry will include one income statement account and one balance sheet account
- ❖ Cash is not adjusted at the end of the accounting period, thus should not use cash in the adjusting process
- ❖ Adjustments are made to assign amounts of revenue or expense to the proper accounting period before finalizing the books for the fiscal period
- ❖ The records of such transactions in the book of prime entry are called adjustments. An adjustment means to make a correct record of a transaction which has not been entered or which has been entered but in an incomplete or wrong manner
- ❖ Adjusting entries can be classified as deferrals, accruals and others. Each of these classes has subcategories.

16.1 Deferrals

- ♣ To defer means to postpone or delay
- ♣ Deferrals are costs or revenues that are recognized at a date later than the point when cash was originally exchanged
- ♣ Companies make adjusting entries for deferrals to record the portion of the deferred item that was incurred as an expense or earned as revenue during the current accounting period. The two types of deferrals are prepaid expenses and unearned revenues

16.1.1 Prepaid Expenses

- Expenses paid in cash and recorded as assets until they are used or consumed. Prepaid expenses are costs that expire with the passage of time (i. e. rent and insurance) or through use (i. e. supplies)
- Expenses are paid in advance are called prepaid expenses or unexpired expenses
- Cost always has two parts one is expired and other on is unexpired. It is not unlikely that some expenses may have been paid in advance
- Companies record payments of expenses that will benefit more than one accounting
- Examples of common prepayments are insurance, supplies, advertising, and rent. In addition, companies make prepayments when they purchase buildings and equipment
 - Prepaid expenses are costs that expire either with the passage of time (e.g., rent and insurance) or through use (e.g., supplies). The expiration of these costs does not require daily entries, which would be impractical and unnecessary

Example # 16.1: For example, on September 1, 2015 full year insurance paid of Rs. 24,000. We will utilize this expense for 12 months and we have 4 months expense for 2015 and remaining for 2016. Prepaid expenses has two case on the basis of journal entry and trial balance presentation

Case 1: Expense Method

General Journal

Date		Account Titles and Explanation	Ref	Amount (Rs)	
				Debit	Credit
2015					
September	1	Insurance Expense Cash (Insurance expense recorded)		24,000	24,000

The effect of above regular entry in end of year trial balance is presented below

Trial Balance

S. No.	Heads of Account	Ref	Amount (Rs.)	
			Debit	Credit
	Insurance Expenses		24,000	

So adjusting entry at December 2015 in order to adjust the balance

Adjusting Entry

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
Dec	31				

Case 2: Asset Method

General Journal

Date		Account Titles and Explanation	Ref	Amount (Rs)	
				Debit	Credit
2015					
September	1	Prepaid Insurance Cash (Insurance expense recorded)		24,000	24,000

The effect of above regular entry in end of year trial balance is presented below

Trial Balance

S. No.	Heads of Account	Ref	Amount (Rs.)	
			Debit	Credit
	Prepaid Insurance		24,000	

So adjusting entry at December 2015 in order to adjust the balance

Adjusting Entry

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
Dec	31				

16.1.2 Unearned revenues

- Income received in advance but has not been earned in accounting period is called unearned revenue
- There are some items of income statement such as interest, rent, discount etc. etc. which might have been received in advance for which the services in full has not been given so for
- Companies record cash received before revenue is earned by increasing (crediting)

Example # 16.2: Rent received for four year in January 01, 2016 of Rs. 80,000. At the end of 2016 accounting period only one year rent is recognized as revenue and remaining liability for next accounting year

Case 1: Revenue Method

General Journal

Date		Account Titles and Explanation	Ref	Amount (Rs)	
				Debit	Credit
2016					
January	1	Cash		80,000	
		Rent Revenue			80,000
		(Rent revenue recorded)			

The effect of above regular entry in end of year trial balance is presented below

Trial Balance

S. No.	Heads of Account	Ref	Amount (Rs.)	
			Debit	Credit
	Rent			80,000

So adjusting entry at December 2016 in order to adjust the balance

Adjusting Entry

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
Dec	31				

Case 2: Liability Method

General Journal

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
Jan	1	Cash Unearned Rent (Unearned rent recorded)		80,000	80,000

The effect of above regular entry in end of year trial balance is presented below

Trial Balance

S. No.	Heads of Account	Ref	Amount (Rs.)	
			Debit	Credit
	Un earned Rent			80,000

So adjusting entry at December 2016 in order to adjust the balance

Adjusting Entry

Date		Account Titles and Explanation	Ref	Amount (Rs)	
				Debit	Credit
2016					
December	31				

- Deferred..... Expenses..... Assets Unexpired costs or prepayments
- Deferred..... RevenueLiability Unearned or Cash received in advance of performing services or selling goods

16.2 Accruals

- ◆ The second category of adjusting entries is accruals
- ◆ Prior to an accrual adjustment, the revenue account (and the related asset account) or the expense account (and the related liability account) are understated
- ◆ Thus, the adjusting entry for accruals will increase both a balance sheet and an income statement account
- ◆ Accruals fall into two categories—Accrued Revenues and Accrued Expenses

16.2.1 Accrued Revenue or Receivable Revenue

- Revenue earned but not yet received in cash in accounting year
- Revenues earned but not yet recorded at the statement date are accrued revenues
- Accrued revenues may accumulate (accrue) with the passing of time, as in the case of interest revenue. These are unrecorded because the earning of interest does not involve daily transactions
- Companies do not record interest revenue on a daily basis because it is often impractical to do so

Example # 16.3: Rs. 100,000 fixed deposits amount in bank in July 01, 2015 and contract is to earn 10% per annum at the end of contract year. So in this case we will receive Rs. 10,000 at June 2016, but we have earned interest of six months in this period 2015, so pass adjusted entry

Adjusting Entry

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
Dec	31				

16.2.2 Accrued Expenses or Outstanding Expenses or Expenses Payable

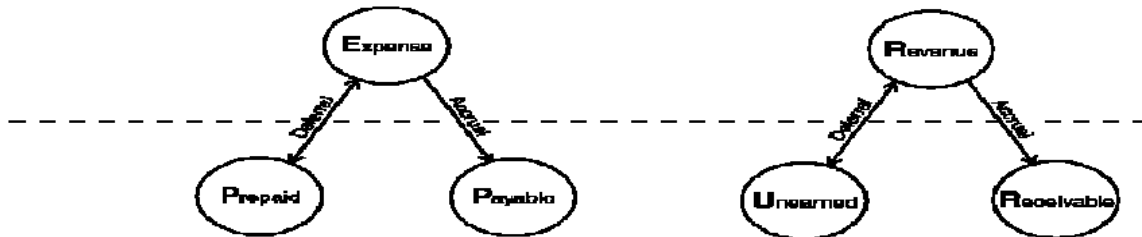
- Expenses incurred but have not been actually paid are called outstanding expenses
- For example, salary for December is generally paid till the 2nd and 3rd January next
- When books of account are closed and Financial Statements are prepared the amount of staff salary for December is treated as an “Outstanding Salaries”. It will become liability of business as on the closing date
- Expenses incurred but not yet paid or recorded at the statement date are called accrued expenses. Interest, taxes, and salaries are common examples of accrued expenses

Example # 16.4: At December 31, 2016, Abdul Basit Anwaar Ltd. expects to pay employees’ salaries of Rs. 8,400 as a result of work performed since the last pay day

Adjusting Entry

Date	Account Titles and Explanation	Ref	Amount (Rs)	
			Debit	Credit
2016				
Dec 31				

- Accrued Revenue Assets Unrecorded revenues (revenues earned, but cash not yet received)
- Accrued Expenses..... Liability..... Unrecorded expenses (expenses incurred, but cash not yet been paid)



Practice MCQs

www.accountancyknowledge.com/adjusting-entries-mcqs-1/

Practice Problems with Solutions

www.accountancyknowledge.com/adjusting-entries-problems-and-solutions/

ADJUSTMENT ENTRIES (II)

Review of Deferred and Accrual Adjustment

<i>Type of Adjustment</i>	<i>Accounts Before Adjustment</i>	<i>Adjusting Entry</i>
Prepaid expenses	Assets overstated Expenses understated	Dr. Expenses Cr. Assets
Unearned revenues	Liabilities overstated Revenues understated	Dr. Liabilities Cr. Revenues
Accrued revenues	Assets understated Revenues understated	Dr. Assets Cr. Revenues
Accrued expenses	Expenses understated Liabilities understated	Dr. Expenses Cr. Liabilities

17.1 Depreciation Expenses

- ◆ The third category of adjusting entries is related to other adjustments
- ◆ It includes depreciation and Accounting for bad debts
- ◆ Depreciation is the process of allocating the cost of tangible fixed assets over its estimated life
- ◆ Initially the cost of the assets including installation cost is debited to the particular assets
- ◆ In each accounting year/period a portion of the cost expires and needs adjustment for showing correct profit for the period and correct value of the asset

Example # 17.1: On January 1, 2015, Company acquired machinery (a depreciable asset) at a total cost of Rs. 152,000. The estimated salvage value of the asset is Rs. 2,000 and its estimated useful life is five years. Record yearly depreciation

Case 1: Cost Method

Adjusting Entry

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
Dec 31				

Case 2: Written Down Method

Adjusting Entry

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit
Dec	31				

17.2 Accounting for Bad Debts

- ❖ For achieving the maximum sales, goods are often sold to known customers on credit
- ❖ Since of these customers fails to pay their debts due to insolvency or any other factor
- ❖ These debts which cannot be recovered are called bad debts. It is a loss/expense to the business so, an adjustment is needed
- ❖ Determining the amount of accounts receivable to report is difficult because some receivables will become uncollectible
- ❖ It should be noted here that no adjustment is required for any bad debt which is appearing already in the Trial Balance. The bad debt appearing in the trial balance shows as expense in the income statement only
- ❖ Two methods are used in accounting for uncollectible accounts are Direct Write-off Method and Allowance Method

17.2.1 Direct Write-off Method

- When a specific account is determined to be uncollectible, the loss is charged to Bad Debts Expense
- Bad debts expense will show only actual losses from uncollectible
- Using the direct write-off method, entries to record write-offs are often made in a period following sales rather than in the period in which the sales were made. Therefore, there is no matching of expenses with the revenue
- Use of the direct write-off method can reduce the usefulness of both the income statement and balance sheet
- Unless bad debt losses are insignificant, the direct write-off method is not acceptable for financial reporting purposes

Example # 17.2: Based on an analysis the bad debts expense adjustment for the year 2016 is Rs. 1,000 for Ali and Sons

Adjusting Entry

Date		Account Title and Explanations	Ref	Amount (Rs)	
				Debit	Credit

17.2.2 Allowance or Provision Method

- The allowance method of accounting for bad debts involves estimating uncollectible accounts at the end of each period
- It provides better matching of expenses and revenues on the income statement and ensures that receivables are stated at their cash (net) realizable value on the balance sheet
- Cash (net) realizable value is the net amount of cash expected to be received. It excludes amounts that the company estimates it will not collect
- Receivables are therefore reduced by estimated uncollectible amounts on the balance sheet through use of the allowance method
- The allowance method is required for financial reporting purposes when bad debts are material
- Three essential features of the allowance method are:
 - Companies estimated uncollectible accounts receivable and match them against revenues in the same accounting period in which the revenues are recorded
 - Company are record estimated uncollectible as an increase (a debit) to Bad Debts Expense and an increase (a credit) to Allowance for Doubtful Accounts (a contra asset account) through an adjusting entry at the end of each period
 - Companies debit actual uncollectible to Allowance for Doubtful Accounts and credit them to Accounts Receivable at the time the specific account is written off as uncollectible

17.2.2.1 Recording Estimated Uncollectible:

- Allowance for Doubtful Accounts shows the estimated amount of claims on customers that are expected to become uncollectible in the future
- The credit balance in the allowance account will absorb the specific write-offs when they occur
- Allowance for Doubtful Accounts is not closed at the end of the fiscal year
- Bad Debts Expense is reported in the income statement as an operating expense (usually a selling expense)

17.2.2.2 Recording the Write-Off

- Each write-off should be approved in writing by authorized management personnel
- Under the allowance method, every bad debt write-off is debited to the allowance account (not to Bad Debt Expense) and credited to the appropriate Account Receivable
- A write-off affects only balance sheet accounts. Cash realizable value in the balance sheet, therefore, remains the same

17.2.2.3 Recovery of an Uncollectible Account

- When a customer pays after the account has been written off, two entries are required:
 - (1) The entry made in writing off the account is reversed to reinstate the customer's account
 - (2) The collection is journalized in the usual manner
- The recovery of a bad debt, like the write-off of a bad debt, affects only balance sheet accounts

Example # 17.3: Assume Abbottabad Furniture has credit sales of Rs. 1,200,000 in 2011, of which Rs. 200,000 remains uncollected at December 31st 2016. The credit manager estimates that Rs. 12,000 of these sales will prove uncollectible. Pass the adjusting entry to record the estimated uncollectible

Estimation of Uncollectable

Date	Account Title and Explanations	Ref	Amount	
			Debit	Credit
2016				
Dec 31				

Assume that the vice-president of finance on March 1, 2017, authorizes a write-off of Rs. 500 balance owed by R. A. Sons. Pass the adjusting entry to record the write-off

Bad Debts Write-Off

Date	Account Title and Explanations	Ref	Amount	
			Debit	Credit
2017				
March 1				

When R. A. Sons pays Rs. 500, two journal entries are required to record the collection:

Recovery of Bad Debts

Date	Account Title and Explanations	Ref	Amount	
			Debit	Credit

- ◆ Frequently the allowance is estimated as a percentage of the outstanding receivables
 - Management establishes a percentage relationship between the amount of receivables and expected losses from uncollectible accounts
 - Companies often prepare a schedule in which customer balances are classified by the length of time they have been unpaid
 - Because of its emphasis on time, this schedule is often called an aging schedule and the analysis of it is often called aging the accounts receivable

SUMMARY OF ADJUSTING ENTRIES

Adjusting Entry	Account to be DEBITED	Account to be CREDITED
PREPAID EXPENSES:		
Asset Method	Expense	Prepaid expense
Expense method	Prepaid expense	Expense
UNEARNED REVENUES:		
Liability Method	Unearned Revenue	Revenue
Revenue method	Revenue	Unearned Revenue
ACCRUED EXPENSES		
	Expense	Payable
ACCRUED REVENUES		
	Receivable	Revenue
DEPRECIATION		
	Depreciation Expense	Accumulated depreciation
DOUBTFUL ACCOUNTS		
	Bad debts Expense	Allowance for Bad Debts

Example # 17.4: For each of the following cases, prepare the adjusting entries at the end of December, 2011

- a. One-third of the fee related to Rs. 60,000 cash received in advance is performed this period
- b. Wages of Rs. 9,000 are earned by workers but not paid as of December 31, 2011
- c. The prepaid Insurance account had a Rs. 5,000 balance on December 31, 2011. An analysis of insurance policies shows that Rs. 2,200 of unexpired insurance benefits remains at December 31, 2012
- d. The company has earned (but not recorded) Rs. 750 of interest from investments in CDs for the year ended December 31, 2011. The interest revenue will be received on January 10, 2012
- e. The company has a bank loan and has incurred (but not recorded) interest expenses of Rs. 3,500 for the year ended December 31, 2011. The company must pay the interest on January 2, 2012
- f. Record the bad debt expense for December that estimates total uncollectible accounts at Rs. 1,400
- g. Depreciation on the company's equipment is Rs. 3,000 by WDM

Adjusting Entries

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
<i>2011</i>				
<i>Dec</i>				
	Total			

Practice MCQs

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ADJUSTED TRIAL BALANCE

18.1 Adjusted Trial Balance

- ❖ A list that contains all the accounts and their balances after adjustments have been made is called adjusted trial balance
- ❖ Adjusted trial balance = Trial balance plus or minus adjustments
- ❖ The adjusted trial balance is prepared after all adjusting entries have been journalized and posted
- ❖ The adjusted trial balance shows the balances of all accounts, including those that have been adjusted, at the end of the accounting period
- ❖ The purpose of the adjusted trial balance is to prove the equality of the total debit balances and total credit balances in the ledger after all adjustments
- ❖ The two columns of the adjusted trial balance should equal each other in the same way that the trial balance does
- ❖ Financial Statements can be prepared directly from the adjusted trial balance

Sadiqa Huma
Adjusted Trial Balance
As on ...

S. No.	Heads of Account	Ref	Amount (Rs.)	
			Debit	Credit
Total				

Example # 18.1: Prepare Adjusted Trial Balance for the year ending 31st December 2016 from the Trial Balance and adjustments of Mishal Company given below:

Mishal Company
Trial Balance
As on December 31st, 2016

Description	Debit	Credit
Drawings	14,000	
Capital Account		80,000
Supplies	55,000	
Purchases	485,000	
Sales		610,000
Sundry Debtors	80,000	
Sundry Creditors		60,500
Sales Returns	5,000	
Carriage Inwards	6,000	
Salaries	28,000	
Rent, Rates, Taxes	15,000	
Insurance Expense	4,000	
Machinery	50,000	
Furniture	5,000	
Cash in hand	3,500	
Total	Rs. 750,500	Rs. 750,500

Adjustments:

1. Rent received includes a deposit of Rs. 1,000 refundable to shop-keeper when the premises are vacated (Credit Unearned rent).
2. Out Standing Salary of manager on December 31, 2015 is Rs. 1,500.
3. Inventory in the shop on December 31, is Rs. 60,000.
4. Insurance Expense for the period July 1, 2015 to June 30, 2016.

Solution 1: Corrected Trial Balance*AR Khan Co (Pvt.) Ltd.*

Trial Balance

As on 31st December, 2015

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Debit	Credit
1	Return outward			
2	Furniture			
3	Salaries			
4	Account Payables			
5	Bank			
6	Carriage Inward			
7	Rent Received			
8	Discount Allowed			
9	Purchases			
10	Bill Payable			
11	Account Receivables			
12	Carriage Outward			
13	Owner Equity			
14	Machinery			
15	Return Inward			
16	Discount Received			
17	Insurance Expenses			
18	Sales			
19	Building			
Total				

10				
11				
12				
13				
14				
15				
16				
17				
18				
19				
20				
21				
22				
23				
Total				

Practice MCQs

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FINANCIAL STATEMENTS (INFORMAL)

Financial statements are end results of financial accounting. It consists of Income Statement, Statement of Owner Equity and Balance Sheet.

19.1 Income Statement

- ✓ An Income Statement presents the results of a company's operations for a given reporting period
- ✓ It is called flow statement or period of time statement
- ✓ The Income Statement presents the Revenues earned and Expenses incurred by an entity during a specific time period
- ✓ Resultant figure known as Net Income/Profit (Excess of revenue over expenses) or Net Loss (Excess of expenses over revenue)
- ✓ Accounting period or year is the period of time covered by an Income Statement. It is usually one year. It can either be calendar year (Jan to Dec) or fiscal year (July to June)
- ✓ Income Statement includes revenue, expenses and net profit or loss which carry forward to statement of owner equity

Idrees Sultan

Income Statement

For the Period / Year ended

<i>Expenses</i>	<i>Debit</i>	<i>Revenue</i>	<i>Credit</i>
Total		Total	

19.2 Statement of Owner Equity

- This is a statement, which shows the financial interest or claim of the owner
- Financial interest of the owner represents residual claim against assets of the business
- It includes initial investment plus any further investment and dividend or profit and less withdrawal or/and loss and closing balance which carry forward to balance sheet

Saifullah Mir

Statement of Owner Equity

For the Period / Year ended

<i>Description</i>	<i>Debit</i>	<i>Description</i>	<i>Credit</i>
Total		Total	

19.3 Balance Sheet

- It shows financial position or condition at a specific point in time
- Sometime balance sheet is known a statement of financial position or statement of condition
- A Financial Statement that summarizes a company's Assets, Liabilities and Owner Equity called Balance Sheet
- These three balance sheet segments give investors an idea as to what the company owns and owes, as well as the amount invested by the shareholders. The Balance Sheet must follow the following formula:

$$\text{Assets} = \text{Liabilities} + \text{Shareholders' Equity}$$

Obaid Ur Rehman

Balance Sheet

As on

<i>Assets</i>	<i>Debit</i>	<i>Equities</i>	<i>Credit</i>
Total		Total	

Example # 19.1: Following are the Adjusted Trial Balance related to Naeem & CO (Pvt.) Limited. Prepare Financial Statements (Income Statement, Statement of Owner Equity and Balance Sheet) for the year ended 31st March, 2017

Naeem & CO (Pvt.) Ltd.

Adjusted Trial Balance

For the Period Ended 31st March, 2017

(Million Rupees)

S. No	Heads of Accounts	Debit	Credit
1	Owner Equity		1,551
2	Drawings	560	
3	Machinery	1,850	
4	Sales		5,850
5	Account Receivables	530	
6	Purchases	1,260	
7	Wages	364	
8	Bank Loan		356
9	Account Payable		528
10	Taxes	220	
11	Cash in Hand	226	
12	Note Payable		680
13	Inventory	264	
14	Accumulated Depreciation _Machinery		350

15	Repair	61	
16	Land	2,000	
17	Financial Charges	25	
18	Commission		35
19	Discount	94	
20	Rent	46	
21	Building	1,200	
22	Deprecation of Machinery	50	
23	Note Receivable	600	
Total		Rs. 9,350	Rs. 9,350

Solution:

Naeem & CO (Pvt.) Ltd.

Income Statement

For the Period Ended 31st March, 2017

(Million Rupees)

Description	Amount	Description	Amount
Total		Total	

Naeem & CO (Pvt.) Ltd.

Statement of Owner Equity

For the Period Ended 31st March, 2017

(Million Rupees)

Description	Amount	Description	Amount
Total		Total	

Naeem & CO (Pvt.) Ltd.*Balance Sheet*For the Period Ended 31st March, 2017*(Million Rupees)*

Assets	Amount	Equities	Amount
Current Assets:		Current Liabilities	
		Non Current Liabilities	
Non Current Assets:			
		Owner Equity:	
Total		Total	

Example # 19.2: Prepare corrected Trial Balance, Adjustment Entries, Adjusted Trial Balance, Income Statement, Statement of Owner Equity and Balance Sheet (Informal 3 Financial Statements).

Purwa Shakeel (Pvt.) Ltd.*Uncorrected Trial Balance*As on 31st December, 2016

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Debit	Credit
1	Salary		3,200	
2	Return Inward		1,500	
3	Rent Expense			29,000
4	Sundry Debtors			41,500
5	Loan from Ahmed Ali			60,000
6	Cash in hand		9,000	
7	Cash at Bank			3,000
8	Return Outward		10,000	
9	Sundry Creditors			17,000
10	Interest Expense		1,200	
11	Capital Owner Equity			32,500
12	Sales			75,800
13	Purchases		92,500	
14	Suspense Account		115,800	
15	Furniture		20,000	
16	Insurance Expenses			2,400
17	Commission (Cr)		8,000	
Total			Rs. 261,200	Rs. 261,200

Adjustments:

1. Salary due to his shop assistants on December 31, 2016 is Rs. 800.
2. Rent includes Rs. 25,000 deposited as security (Debit Prepaid Rent).
3. Loan from Mr. Ahmed Ali taken on July 01, 2016 carries simple interest at the rate of 10%.
4. Inventory in the shop on December 31, 2016 is Rs. 35,000.
5. Insurance Expense for the period September 1, 2016 to August 31, 2017.

Solution 1 : Correction of Trial Balance***Purwa Shakeel (Pvt.) Ltd.******Trial Balance******As on 31st December, 2016***

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Debit	Credit
1	Salary			
2	Return Inward			
3	Rent Expense			
4	Sundry Debtors			
5	Loan from Ahmed Ali			
6	Cash in hand			
7	Cash at Bank			
8	Return Outward			
9	Sundry Creditors			
10	Interest Expense			
11	Capital Owner Equity			
12	Sales			
13	Purchases			
14	Furniture			
15	Insurance Expenses			
16	Commission (Cr)			
Total				

Solution 3: Adjustments Trial Balance

*Purwa Shakeel (Pvt.) Ltd.**Adjusted Trial Balance*As on 31st December, 2016

S. No	Heads of Accounts	Ref	Amount (Rs.)	
			Debit	Credit
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				
12				
13				
14				
15				
16				
17				
18				
19				
20				
21				
<i>Total</i>				

Solution 4: Income Statement (Informal)

Purwa Shakeel (Pvt.) Ltd.
Income Statement
 For the Year ended 31st December, 2016

<i>Expenses</i>	<i>Debit</i>	<i>Revenue</i>	<i>Credit</i>
Total		Total	

Solution 5: Statement of Owner Equity (Informal)

Purwa Shakeel (Pvt.) Ltd.
Statement of Owner Equity
 For the Year ended 31st December, 2016

<i>Description</i>	<i>Debit</i>	<i>Description</i>	<i>Credit</i>
Total		Total	

Solution 6: Balance Sheet (Informal)

Purwa Shakeel (Pvt.) Ltd.
Balance Sheet
 As on 31st December, 2016

<i>Assets</i>	<i>Debit</i>	<i>Equities</i>	<i>Credit</i>
Total		Total	

Practice MCQs

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CLOSING AND WORKSHEET

- ❖ As previously stated, revenue increase owner's equity and expenses and withdrawals (Drawings) by owner decrease owner's equity, all accounts relating to expense, revenues and drawing are called temporary accounts
- ❖ Assets (real accounts) and liabilities and Owner equity (Personal accounts) are permanent accounts
- ❖ At the end of financial period, temporary accounts (revenue and expenses) are closing by opening a new temporary account called Income Summary Account
- ❖ When revenue and expenses accounts have been closed than we need to close last nominal account i.e. Income Summary with Owner Equity account. Drawings are also closed with Owner Equity account
- ❖ The balances of Permanent accounts continue to exist beyond the current accounting period. The process of transferring the balances of the temporary accounts into owner's equity permanent account is called closing the accounts
- ❖ The journal entries made for the purpose of closing the temporary accounts are called closing entries
- ❖ It is common practice to close the accounts only once a year at the end of accounting period

20.1 Closing Entries for Revenue Accounts

- Revenue accounts have credit balances. Closing the revenue accounts are, therefore, mean transferring its credit balance to the Income Summary account
- This transfer is accomplished by a journal entry debiting the revenue accounts in an amount equal to its credit balance, with an offsetting credit to the Income Summary account
- The debit portion of this entry returns the balances of the revenue accounts to zero; the credit portion transfers to the former balances of the revenue accounts into the Income Summary account

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Revenue Accounts		*****	
	Income Summary			*****
	(Revenues closed with Income Summary account)			

20.2 Closing for Expense Accounts

- ♣ Expense Accounts have debit balances. Closing an expense account means transferring its debit balance to the Income Summary account.
- ♣ The Journal entry to close an expense account, therefore, consists of a credit to the expense account in an amount equal to its debit balance, with an offsetting debit to the Income Summary

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Income Summary		*****	
	Expenses Accounts			*****
	(Expenses closed with Income Summary account)			

20.3 Closing Income Summary Account

- ❖ After closing revenue and expenses with Income Summary Account, next step is to close Income Summary account, because it is also nominal account and must close at the end of each account period
- ❖ If Income Summary account has credit balance means it is profit and if Income Summary account reflects debit balance suggested lose by business operation
- ❖ Income Summary account will closed against permanent account of Owner Equity

For Profit

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Income Summary		*****	
	Owner's Equity			*****
	(Income Summary Profit closed with Owner's Equity)			

For Loss

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Owner's Equity		*****	
	Income Summary			*****
	(Income Summary Loss closed with Owner's Equity)			

20.4 Closing the Owner's Drawing Account

- ✓ Withdrawals of cash or other assets by owner are not considered as an expense of the business and, therefore, are not a factor in determining the income for the period ended
- ✓ Since drawing account is not closed by the Income Summary account but directly to Owner equity account
- ✓ For closing drawing, the closing entry as

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs)	
			Debit	Credit
	Owner Equity		*****	
	Drawing			*****
	(Drawing closed with Owner Equity account)			

20.5 Summary of the Closing Entries

Let us now summarize the process of closing the accounts

1. Close the various Revenue accounts by transferring their balances into the Income Summary account
2. Close the various Expense accounts by transferring its balances in to the Income Summary account
3. Close the Income Summary account by transferring its balance into the Owner equity account
4. Close the owner's drawing account into the Owner equity account. (The balance of the Owner equity account in the ledger will now be the same as the amount of owner's equity appearing in the Balance Sheet)

Example # 20.1: The following Adjusted Trial Balance was extracted from the books of Anees & Sons on 31st December, 2015. From this you are required to pass closing entries

Particulars	Debit	Credit
	Rs.	Rs.
Cash	5,000	
Accounts receivable	9,000	
Merchandise inventory on 1.1.2015	6,000	
Plant and machinery	74,000	
Land and building	80,000	
Furniture and fixtures	2,600	
Owner's equity		136,000
Accounts payable		3,800
Purchases	10,000	
Salary payable		2,800
Sales		70,000
Rent expense	4,600	
Drawing	2,000	
Insurance prepaid	3,400	
Advertising expense	4,000	
Salaries expense	12,000	
Total	Rs. 212,600	Rs. 212,600

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs.)	
			Debit	Credit
2015				

Total				

20.6 Post-Closing Trial Balance

After the revenue and expense accounts have been closed, it is desirable to prepare post closing trial balance. This trial balance has same total as appears in Balance Sheet

Example # 20.2: Prepare post closing trial balance for example # 20.1 after closing

Anees Fida Swati
Post Closing Trial Balance
 As on 31st December, 2015

Heads of Accounts	Debit Rs.	Credit Rs.
Total		

20.7 Worksheet

- A worksheet often refers to a loose piece of paper used by accountant for showing informal accounting statements
- A worksheet is not a permanent accounting record
- A valuable tool useful to help summarize and move data from the trial balance to the informal financial statements is a work sheet

Example # 20.3: COMSATS' Consulting Services (CCS) was established in 1999. The company adjusts and closes its accounts at the end of the current accounting period. At December 31st, 2016 the balances in the ledger accounts prior to making adjusting entries. You are required to pass adjusting, closing entries and worksheet.

COMSATS' Consulting Services (CCS)

Trial Balance

As on December 31st, 2016

S #	Chart of Accounts	Ref	Dr	Cr
1	Cash		\$ 12,540	
2	Prepaid Office Rent		3,300	
3	Prepaid Dues and Subscriptions		960	
4	Supplies		1,300	
5	Equipment		20,000	
6	Accumulated Depreciation _ Equipment			\$ 1,200
7	Note Payable			5,000
8	Unearned Consulting Fee			35,650
9	Owner Equity			17,040
10	Drawings		27,000	
11	Consulting Fee earned			90,860
12	Salaries Expenses		66,900	
13	Telephone Expenses		2,550	
14	Rent Expenses		11,000	
15	Miscellaneous Expenses		4,200	
Total			Rs. 149,750	Rs. 149,750

Other Data

- (a) In December 1st, 2016, the company signed a new rental agreement and paid three months' rent in advance at a rate of Rs. 1,100 per month. This advance payment was debited to the Prepaid Rent account
- (b) The useful life of the equipment has been estimated at 10 years from date of acquisition. NO depreciation expense has been recorded for the current year
- (c) Dues and Subscriptions expired during the period in total amount of Rs. 710
- (d) Consulting Services valued at Rs. 32,550 were rendered during the account year for clients who had made payment in advance
- (e) Salaries earned by employees but not yet paid amounted to Rs. 2,200 at December
- (f) An estimate of supplies on hand was made at December 31. The estimated cost of the unused supplies was Rs. 450
- (g) Accrued interest on Note Payable amounted to Rs. 100 at year-end (Set up accounts for Interest Expense and for Interest Payable)

General Journal

Date	Account Title and Explanations	Ref	Amount (Rs.)	
			Debit	Credit
2016				
Dec				
Total				

COMSATS' Consulting Services (CCS)

Work Sheet

For the Period ended Dec 31st, 2016

1	2	3	4	5	6	7	8	9	10	11	12	13	14
S.No	Chart of Accounts	Trial Balance		Adjustments		Adj. Trial Balance		Income Statement		Statement of O.E		Balance Sheet	
		Dr	Cr	Dr	Cr	Dr	Cr	Expenses	Revenues	Dr	Cr	Assets	Equities
1													
2													
3													
4													
5													
6													
7													
8													
9													
10													
11													
12													
13													
14													
15													
16													
17													
18													
19													
20													
21													
22													
23													
Total													

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