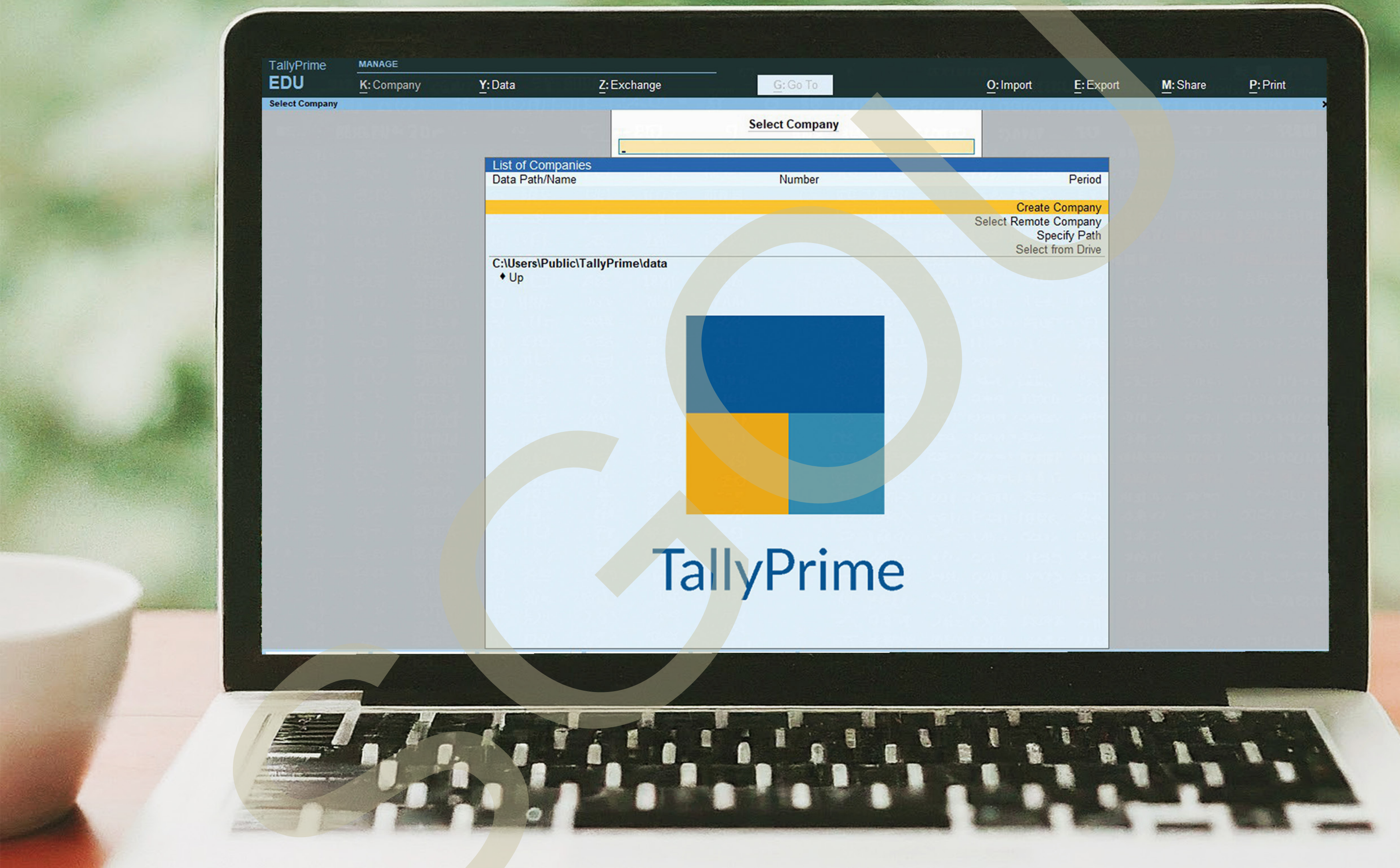
Accounting with Tally

COURSE CODE: B21EC01SE

Skill Enhancement Course
Undergraduate Programme in Economics



SELF LEARNING MATERIAL

SREENARAYANAGURU
OPEN UNIVERSITY

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The State University for Education, Training and Research in Blended Format, Kerala

SREENARAYANAGURU OPEN UNIVERSITY

Vision

To increase access of potential learners of all categories to higher education, research and training, and ensure equity through delivery of high quality processes and outcomes fostering inclusive educational empowerment for social advancement.

Mission

To be benchmarked as a model for conservation and dissemination of knowledge and skill on blended and virtual mode in education, training and research for normal, continuing, and adult learners.

Pathway

Access and Quality define Equity.

Accounting with Tally

Course Code: B21EC01SE

Semester - III

Skill Enhancement Course
Undergraduate Programme in Economics
Self Learning Material

(With Model Question Paper Sets)

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www.sgou.ac.in

ISBN 978-81-973709-0-8

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August 2024

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YouTube

MESSAGE FROM VICE CHANCELLOR

Dear learner,

I extend my heartfelt greetings and profound enthusiasm as I warmly welcome you to Sreenarayanaguru Open University. Established in September 2020 as a state-led endeavour to promote higher education through open and distance learning modes, our institution was shaped by the guiding principle that access and quality are the cornerstones of equity. We have firmly resolved to uphold the highest standards of education, setting the benchmark and charting the course.

The courses offered by the Sreenarayanaguru Open University aim to strike a quality balance, ensuring students are equipped for both personal growth and professional excellence. The University embraces the widely acclaimed “blended format,” a practical framework that harmoniously integrates Self-Learning Materials, Classroom Counseling, and Virtual modes, fostering a dynamic and enriching experience for both learners and instructors.

The university aims to offer you an engaging and thought-provoking educational journey. The undergraduate courses are compared to similar ones at other state universities in Kerala. The programme structure follows guidelines set by the University Grants Commission, which include three main subjects and a range of other academic topics. The undergraduate programme includes Skill Enhancement Courses to teach learners specific skills related to their field of study. This is an important part of the university's plan to give learners new experiences with relevant subject content. The Skill Enhancement Courses have been designed to match those offered by other premier institutions that provide skill training. The Self-Learning Material has been meticulously crafted, incorporating relevant examples to facilitate better comprehension.

Rest assured, the university’s student support services will be at your disposal throughout your academic journey, readily available to address any concerns or grievances you may encounter. We encourage you to reach out to us freely regarding any matter about your academic programme. It is our sincere wish that you achieve the utmost success.

Warm regards.
Dr. Jagathy Raj V. P. 17-08-2024

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BLOCK

Introduction to Accounting

Unit 1
Financial Accounting

Learning Outcomes

Upon the completion of this Unit, the learner will be able to;

- ◊ familiarise the basic concepts and processes of accounting, including its definition, advantages, and limitations.
- ◊ differentiate between the main branches of accounting: management accounting, cost accounting, and financial accounting.
- ◊ analyse and interpret the four basic financial statements: Income Statement, Balance Sheet, Cash Flow Statement, and Statement of Owner's Equity.
- ◊ apply the golden rules of accounting for real, personal, and nominal accounts in recording business transactions.

Prerequisites

All of you, at some point, have visited a grocery shop or a medical shop. You might have wondered how the business person maintains a record of all the transactions done during a particular period, say a year? You might have also thought why do they have to maintain a record? How is it beneficial? Is it mandatory? Now, lets think of larger business organisations. They provide goods that might range from a simple safety pin to fighter aircraft. Those in the service industry provide various services such as transportation, hospitality, or developing complex software programs. To make sound decisions, a business enterprise needs accounting information. This information is also needed by government agencies, regulatory bodies, analysts, and individuals at various points in time and at different levels. This is the essence of Financial Accounting - a crucial tool for businesses of all sizes and the stakeholders around them.

Keywords

Accounting, Accounting Process, Accounting Branches, Advantages and Limitations of Accounting, Financial Accounting, Accounting Concepts, Kinds of Accounts

Discussion

1.1.1 Accounting

Accounting is the language used to communicate the financial information of business to its stakeholders like owners, creditors, employees, government and society. Accounting came into force to support human memory by recording business transactions. We can consider accounting as an information system because it receives, processes, and converts financial data into useful information. This is a broader term that encompasses all processes of recording, classifying, and summarising financial transactions to provide information that is useful in making business decisions. It includes several specialised areas such as Financial Accounting, Managerial Accounting, Cost Accounting, Tax Accounting and Auditing.

According to American Institute of Certified Public Accounts (AICPA), "Accounting is the art of recording, classifying and summarising in a significant manner and terms of money, transactions and events which are, in part at least, of a financial character, and interpreting the result thereof."

1.1.1.1 Process of Accounting

Imagine running a business without knowing how much money you are making or spending. It would be like driving a car without a dashboard – you would have no idea how fast you are going, how much fuel you have left, or if anything is wrong with the engine. The accounting process serves as the dashboard for businesses. It provides a systematic way to record, classify, and summarise financial transactions, giving business owners and managers the information they need to make informed decisions. Whether you're managing a multinational corporation or a small family business, understanding the accounting process is essential. The process of accounting is as follows:

a. **Recording:** Recording business transactions is the first and most basic function of accounting. This is done in a book called the "Journal." Business transactions are classified into two types:

   i. ***External Transactions***: These involve the exchange of something valuable between two or more entities. Examples include purchasing raw materials from suppliers and selling goods to customers.

   ii. ***Internal transactions***: These refer to events that occur within the enterprise, such as transferring materials from the stores department to the production department or providing stationery items to different departments.

c. **Classifying:** The recorded transactions are classified based on their nature. Similar transactions are grouped together in a book called the "Ledger."

d. **Summarising:** The classified data is presented in a way that is understandable and useful to various users of accounting information, such as management, owners, creditors, and bankers. This process involves preparing an income statement to show the profit or loss of the business for a specific period and a position statement to show the assets and liabilities of the business on a specific date.

e. **Analysis and Interpretation:** The summarised financial data are analysed and interpreted so that users can make meaningful judgements about the financial position and operational results of the business.

f. **Communication:** After meaningful analysis and interpretation, accounting information needs to be communicated properly to the appropriate individuals. This is done by preparing and distributing accounting reports, such as accounting ratios, graphs, diagrams, etc.. Accounting is often referred to as the language of business because of this communication aspect.

1.1.1.2 Advantages of Accounting

a. **Decision Making Tool:** Accounting serves as a valuable tool for decision making by providing relevant financial information. For instance, a company can analyse its financial statements to determine the profitability of different product lines and make informed decisions about resource allocation and pricing strategies.

b. **Overcoming Memory Limitations:** By recording business transactions, accounting helps overcome the limitations of human memory. The books of accounts provide a reliable record of financial information, ensuring that important data is accessible at all times. For example, a company can refer to its sales records to track customer payments and outstanding balances.

c. **Comparing Profit Over Time:** Accounting allows for the comparison of profits across different years, enabling businesses to assess their progress and make informed decisions. For instance, by analysing the financial statements of previous years, a company can evaluate its growth rate and identify areas where it may need to make strategic changes.

d. **Tax Compliance:** Accounting records provide accurate information about the amount of tax levied on sales (Goods and Service Tax - GST) and the profit of the business (corporate tax). This facilitates compliance with tax regulations. For example, a company can refer to its accounting records to calculate the correct amount of GST payable and ensure timely and accurate tax reporting.

e. **Business Valuation:** Accounting enables the determination of the value of assets, liabilities, and the purchase price of a business. This information is crucial in cases where a business is sold or undergoing a merger or acquisition. For instance, potential buyers can review the financial statements of a business to assess its financial position and make informed decisions regarding its value.

f. **Legal Validation:** In the event of a dispute, accounting records can be presented as evidence in court to support and validate the arguments of a business. For example, if there is a disagreement over financial transactions or contractual obligations, presenting the account books can help clarify and resolve the dispute.

1.1.1.3 Limitations/Disadvantages of Accounting

a. **Accounting is a Post-mortem Analysis:** What happened in the business is examined through accounting; that is, the amount spent on a particular item of expenditure and the income of a particular source is recorded. But no information for controlling expenditure or increasing an income is mentioned.

b. **Only Monetary Transactions Come Under the Purview of Accounting:** Non-monetary transactions like the sincerity and hard work of employees, efficiency of management, etc. do not have a place in accounting.

c. **It does not Consider the Price Level Changes:** As per the rule of accounting, fixed assets are to be shown on the asset side of the Balance Sheet at cost less depreciation. Therefore, it never shows the current market value of the asset. Hence the Balance Sheet will not show a true and fair view of the state of affairs of the business.

d. **Based on Estimation:** Accounting is based on estimation also. For example, there are different methods for providing depreciation. A particular method can be chosen by an accountant normally unless otherwise there are some legal restrictions. In no case, the amount of depreciation charged and debited to the Profit and Loss Account is the exact amount because the exact life of an asset, its estimated scrap value, etc. cannot be predicted in advance. Accounting is based on certain principles and concepts.

1.1.1.4 Basic Accounting Terms

It is important to know a few basic terms in accounting that helps to understand the accounting process easily. Let us go through some of the important terminologies in accounting.

a. **Business Transactions**

We engage in many financial activities in our daily lives. The most common is paying money for goods purchased at shops, which represents a transaction - an event with a monetary value. Sometimes in transactions, money is exchanged simultaneously with goods and services, called cash transactions. Other times payment is postponed to a later date, called credit transactions. In the past, the barter system was used instead of cash or credit transactions, where goods and services were directly exchanged for other goods and services rather than money. Overall, transactions refer to measurable monetary exchanges, either with immediate cash payment or deferred credit payment, as opposed to direct exchange of goods and services without money as in the historical barter system.

b. Assets

If an individual owns land, that land has value and can be used by the owner to pay off debts and meet other obligations. Similarly, companies own assets such as machinery, equipment, facilities, etc. that have value and are owned by the company. These assets can be used by the company to pay expenses and satisfy other business obligations. Just as privately owned land is considered an asset to an individual because it has worth and can be utilised to cover financial responsibilities, assets owned by a company, like property and equipment, represent value that belongs to the business and can be leveraged to take care of business commitments.

Assets are resources of value owned and controlled by the business. Assets are an important part of a firm, which include cash, plant and machinery, goodwill, and other valuable things owned by a business. Assets can be transformed into cash if the business requires. We can classify assets into two, i.e., tangible assets and intangible assets. Tangible assets are those assets like machinery and furniture, which can be touched, seen, or felt. Intangible assets (assets which are not in physical form and cannot be touched, seen, or felt) like copyright, trademark, goodwill, etc..

c. Liabilities

An individual can owe money to a bank by taking out a loan. Similarly, companies can also have debts like loans, unpaid bills owed to suppliers, and other financial obligations. All of these amounts that a business owes to external parties are considered liabilities. A liability is any kind of financial debt or obligation that one business must pay to another entity or person. Just as an individual may have a liability like a bank loan, a company can also have liabilities in the form of credit that it has taken on from banks, bills owed, or other unpaid debts that the company is responsible for paying back.

d. Purchases

Suppose a company bought leather and other raw materials to manufacture shoes. Such transactions must be recorded in the books of accounts. Generally, this can be included in the purchase category. Purchase indicates the total goods purchased by the firm for manufacturing or sale.

e. Sales

Galaxy Pvt. Ltd.'s primary business is selling shoes. Once the shoes are manufactured, Galaxy must sell them to various customers. These sales transactions involve Galaxy selling their produced or purchased shoe inventory to customers in exchange for payment. In accounting, sales refer to the total amount of goods that a company sells to customers for monetary compensation. Since Galaxy's main activity is selling the shoes they produce, their revenues from selling their shoe products to customers are considered sales in their accounting records.

f. Capital

Jeff and Susan are the owners of the company called Galaxy Pvt. Ltd. We saw that they started the company by investing their savings. This initial investment made by the owners is called capital. Capital is considered as a liability (as per business entity concept) of the firm because it is the money contributed by the owners which is to be repaid at the time of winding up or closure of business.

g. Drawings

Sometimes owners of the firm withdraw cash or goods from the business for their personal needs. For instance, it Susan and Jeff withdraw cash or goods from their firm for their personal needs. This is accounted as drawings and considered as a reduction from capital most of the time.

h. Debtors

Once Galaxy Pvt. Ltd. manufactures shoes, various retail stores purchase shoes from them under agreements that allow the stores to pay for the shoes sometime after they are delivered. Since these retail stores now owe money to Galaxy for the shoe purchases, they are considered debtors to the company. Because Galaxy is allowing the stores to buy the shoes on credit and pay for them later, the stores are essentially debtors that owe payment back to Galaxy for the shoes. So, in Galaxy's accounting records, these retail stores would be tracked as debtors that have outstanding debt owed back to Galaxy resulting from the shoes purchased on credit. In every business, there are groups of people who buy goods or services and agree to make the payment in the future. Such people are called debtors. "Debtors are persons or other companies who owe something to the business." They are considered the assets of the business.

i. Creditors

Suppose Galaxy Pvt. Ltd. has purchased leather from another company called ABC Ltd. for manufacturing shoes and promised to pay the money after a week. Here ABC Ltd. will be a creditor because Galaxy Pvt. Ltd. owes money to them. In most of the firms, there are suppliers or other persons who supply goods to the business. The firms agree that their payment will be made on a future date. Such suppliers to whom the company owe the amount is called creditors. Creditors can be defined as "Persons to whom something is owed by the business."

j. Stock

Stock means the value of goods that are available for sale during a particular period. Galaxy Pvt. Ltd. has manufactured 1000 shoes, and they are ready to be sold. So, the available stock will be 1000 units. Let us consider a situation, Galaxy Pvt. Ltd. has 1000 shoes in their stock. Two new orders with the quantity of 700 and 200 shoes are received respectively. So, the firm can meet the requirements of these two orders as they have sufficient stock. The remaining unsold goods are their new stock (1000-700-200=100).

k. Income

Here is an example situation: Galaxy Pvt. Ltd. rented out a small portion of their office space to a Cafeteria so the Cafeteria could run their business of serving Galaxy employees. As part of the rental agreement, the Cafeteria pays Galaxy a fixed monthly rent payment. This rent money received by Galaxy from the Cafeteria is considered rental income for Galaxy. By renting out part of its office to the Cafeteria, Galaxy has generated a rental income stream through the regular monthly payments the Cafeteria makes in order to occupy the space. So, the rent Galaxy receives would be accounted for as income in their records. Companies can earn income from various sources such as interest, rent, dividends, and revenue generated from sales and services. Any interest, rent, or dividend payments received by a business are considered income. Additionally, revenues coming in from sales of products or services represent income for the business. All of these types of earnings that a company takes in are categorised as income, which serves to increase the overall value and worth of the business. The different forms of income allow a business to grow its assets and value.

l. Expenses

From day one, Galaxy Pvt. Ltd. has incurred various expenses such as: employee wages, purchasing stationery and supplies, and more. The money Galaxy spends on these items are considered expenses for the company. In order for a business to generate revenue, it must spend money. So any money spent in the effort of earning revenue is categorized as an expense. Some examples of common business expenses include rent, employee wages and salaries, insurance premiums, advertising costs, phone service charges, and more. Galaxy must spend money to operate on a daily basis, like paying worker wages and buying office supplies, and these costs are recorded as expenses in Galaxy's accounting.

m. Expenditure

Are expense and expenditure the same? No, both the terms are different in nature. Expenditure is the amount paid to acquire assets and maintain the earning potential of the business. Expenditure can be classified into two; capital expenditure and revenue expenditure. Capital expenditure means "the amount required for acquiring fixed assets". The revenue expenditure is the amount needed for day-to-day activities of the business or maintaining the earning capacity of the business. As Galaxy Pvt. Ltd.'s business expanded, they had trouble meeting customer demand with their existing production capacity. To increase output, they purchased new machinery to replace older equipment. The money Galaxy spent to obtain this new production machinery is considered a capital expenditure for the company. Because Galaxy invested in new long-term equipment to boost production capacity and growth, the cost of purchasing the new machinery is categorised as a capital expenditure rather than a regular operating expense.

1.1.1.5 Branches of Accounting

The main branches of accounting are management accounting, cost accounting and financial accounting.

A. Management Accounting

Management accounting provides information to internal stakeholders, primarily management, to support decision making and operational control. It involves activities such as budgeting, cost analysis, variance analysis, and performance measurement. The goal of management accounting is to help managers plan, evaluate, and monitor the financial aspects of their organisation. Unlike financial accounting, which focuses on historical data, management accounting often includes forward looking information and is more flexible in adapting to the specific needs of management.

B. Cost Accounting

Cost accounting focuses on analysing, recording, and controlling costs associated with the production of goods or services. It involves classifying and allocating costs to different cost centres, such as departments or products, to determine their profitability and efficiency. Cost accountants track costs related to direct materials, direct labour, overhead, and other cost elements. This information is used by managers to make decisions about pricing, budgeting, and cost control. Cost accounting provides insights into the cost structure of a company, allowing management to optimise resources and improve cost effectiveness.

C. Financial Accounting

This is a specific branch of accounting that focuses on preparing financial statements for external users such as investors, creditors, and regulatory agencies. Financial accounting involves the preparation and presentation of financial statements, such as Balance Sheets, Income Statements, and Cash Flow Statements. Its primary focus is to provide external stakeholders, such as investors, creditors, and regulators, with accurate and reliable information about the financial performance and position of an organisation. Financial accounting follows either Generally Accepted Accounting Principles (GAAP) or International Financial Reporting Standards (IFRS) to ensure consistency and comparability in financial reporting.

“Accounting” encompasses all of a company’s financial transactions. A well-managed accounting department will have set policies and procedures for expenses, data management, and the generation of financial reports. Whereas financial accounting is concerned specifically with the generation of these reports, that they are based on accurate information and follow GAAP.

Basic Financial Statements

Financial statements are formal records that provide a comprehensive overview of an organisation's financial activities and position. They are essential tools for communicating financial information to stockeholders, including investors, creditors, management, and regulatory bodies. There are four basic Financial Statements.

Fig 1.1.1 Financial Statements

i. Income Statement

The Income Statement, sometimes called the Profit and Loss Statement, offers a view of a company's financial performance over a specific period, typically a quarter or a year. It begins with the company's revenues, then subtracts various costs and expenses to arrive at the net profit or loss. This statement is vital for understanding a company's profitability and operational efficiency. It shows not just how much money a company made, but also how it made that money and what expenses were incurred in the process.

An income statement shows a company's net income over a certain period. It is a company's total revenue minus its total expenses.

ii. Balance Sheet

The Balance Sheet, also known as the Statement of Financial Position, provides a snapshot of a company's financial status at a specific point in time. It lists all of the company's assets, which are resources owned or controlled by the business, alongside its liabilities, which are the debts and obligations owed to others. The difference between these two figures represents the shareholders' equity, effectively showing what the company is worth. This statement is crucial for assessing a company's financial strength, liquidity, and overall stability.

A balance sheet shows what a company owns (its assets) and owes (its liabilities) on a particular date, along with its owner's equity or shareholders' equity. Assets can include:

- Cash
- Prepaid expenses
- Accounts receivable
- Notes receivable (money owed to the company within 1 year)
- Inventory
- Investments (including real estate)
- Buildings
- Machinery and equipment
- Vehicles
- Intangible assets (such as patents)

Liabilities can include:

- Accounts payable
- Loans payable
- Notes payable (money the company owes within 1 year)
- Unearned revenue (a product or service a client has paid for but the company has not yet provided)
- Deferred tax
- Current taxes
- Payroll (owed but not yet paid)
- Warranty obligations
- Mortgages

Owner's equity or shareholder's equity can include:

- Stocks (preferred and common stocks)
- Retained earnings (money to be invested back into the business)
- Comprehensive income (profit or loss in a company's investments during a specific time period)

On a balance sheet, assets and the sum of liabilities and equity must balance each other.

Assets = Liabilities + Owners' Equity

iii. Cash Flow Statement

The cash flow statement, also known as the statement of cash flows, documents in detail all of a company's cash inflows and outflows over a specific period of time. It is only concerned with cash. The Cash Flow Statement provides a detailed look at how a company generates and uses its cash. It helps stakeholders understand if a company can generate enough cash to fund its operations and growth. A cash flow statement reflects the short-term viability of a company by indicating whether the operation has enough working capital on hand to pay its employees and debts. It is divided into three main sections:

a. Cash flows from operating activities – These are the costs of a company's core business activities.

b. Cash flows from Financing activities – This is money the company receives from taking loans or issuing shares, as well as money paid in interest on loans and dividends to investors.

c. Cash flows from Investment activities – This is money that comes from buying and selling the company's investments, such as securities or fixed assets.

iv. Statement of Owner's Equity

The statement of owner's equity shows the total value of the business held by its owner or owners for a reporting period. This includes income and owner contributions, minus any expenses or owner withdrawals. While you can see total owner's equity on your balance sheet, this more detailed report can indicate the cause of increases or decreases in owner's equity. For corporations, the report is called a statement of shareholders' equity (or stockholders' equity). And it would also document share capital from issuing stocks, as well as retained earnings, which shows the accumulated profits left over after paying dividends or distributions to stockholders.

Importance of Financial Accounting

Companies engage in financial accounting for several important reasons.

a. **Creating a standard set of rules** – By delineating a standard set of rules for preparing financial statements, financial accounting creates consistency across reporting periods and different companies.

b. **Decreasing risk** – Financial accounting does this by increasing accountability. Lenders, regulatory bodies, tax authorities, and other external parties rely on financial information; financial accounting ensures that reports are prepared using acceptable methods that hold companies accountable for their performance.

c. **Providing insight to management** – Though other methods such as managerial accounting may provide better insights, financial accounting can drive strategic concepts if a company analyses its financial results and makes reactionary investment decisions.

d. **Promoting trust in financial reporting** – Independent governing bodies oversee the rules of financial accounting, making the basis of reporting independent of management and a highly reliable source of accurate information

e. **Encouraging transparency** – By setting rules and requirements, financial accounting forces companies to disclose certain information on how operations are going, and what risks the company is facing, painting an accurate picture of financial performance regardless of how well or poorly the company is doing.

Here are some individuals or organisations that may reference your financial statements:

a. **Investors** – They will need to see the numbers to decide whether the business is attractive enough to invest in.

b. **Banks** – If a company wants a loan, the bank may request certain financial statements. This will allow the company to show that they can pay the loan back on time.

c. **Auditors** – If the company is subject to an IRS audit, then government auditors are going to start their analysis with these statements.

d. **Lawyers** – If there's a lawsuit or other legal action related to a company's income or expenses, lawyers will need to be able to analyse this information.

e. **Suppliers** – Suppliers may want to view a company's financials before providing goods or services to ensure that they will be able to pay their invoices.

1.1.2 Basic Accounting Concepts

Certain basic ideas or assumptions under the theory base of accounting that provide certain working rules for the accounting activities of an organisation. There are 13 important Accounting Concepts that are to be followed by companies to prepare true and fair financial statements.

Fig 1.1.2 Accounting Concepts

1. Business Entity Concept

The business entity concept states that the business enterprise is separate from its owner. In simple terms, for accounting purposes, the business and its owners are treated separately. If an owner invests money in the business, it will be treated as a liability for the business. However, if the owner takes out some money from the business for personal use, it will be considered drawings. Therefore, assets and liabilities of a business are the business's assets and liabilities, not the owner's. Hence, the books of accounts include the accounting records from the point of view of the business instead of the owner. For example, the amount of 1,00,000 in ABC Ltd. by its owner Raj will be considered a liability to the business. The business entity concept applies to partnerships, companies, sole proprietorships, small enterprises, and large enterprises.

2. Money Measurement Concept

The money measurement concept says that a business should record only those transactions which can be expressed in monetary terms. It means that transactions like purchase and sale of goods, rent payment, expenses payment, earning of revenue, etc., will be recorded in the books of accounts of the firm. However, transactions or happenings, like the research department's creativity, machinery breakdown, etc., will not be recorded in the books of accounts of the firm. Besides, the records of transactions of a firm should not be recorded in physical units, such as 3 acre land, 20 computers, 40 chairs, etc., instead, they should be recorded in monetary terms, such as ₹13 lakh for land, ₹15 lakh for computers, and ₹2 lakh for chairs, etc., in the books of accounts.

However, there are two drawbacks of this concept in accounting. Firstly, according to this concept, the accounting of a business is limited to the recording of information that can be expressed in a monetary unit, but does not involve or record essential information that cannot be expressed in monetary units. Secondly, the concept has the limitations of the monetary unit itself.

3. Going Concern Concept

The going concern concept assumes that an organisation would continue its business operations indefinitely. It means that it is assumed that the business will run for a long period of time, and will not liquidate in the foreseeable future. It is one of the most important assumptions or concepts of accounting. It is because the going concern concept provides the firm with the basis to show its assets' value in the balance sheet.

For example, if an organisation purchases machinery for ₹1,00,000, it would not be fair to show the full amount of the machinery in one year, as the company will be getting service or production with the help of machinery for several years. Therefore, the going concern concept by assuming that the business will not liquidate in the foreseeable future states that the firm should record the machinery's value for its estimated life span. Let's say, the life span of the said machinery is 10 years. Now, the firm may charge ₹10,000 for 10 years from the profit and loss account.

4. Accounting Period Concept

The accounting period concept defines the time span at the end of which an organisation has to prepare its financial statements to determine whether they have earned profits or incurred losses during a specified time span. It also states the exact position of the firm's assets and liabilities at the end of the specified time span. This information is used by different internal and external users of the organisation for various purposes regularly. The financial statements are prepared regularly because it helps them in the decision-making process, and no firm can wait for long to know its results. The normal interval for the preparation of the financial statements is one year. This time interval of one year is known as the accounting period. According to the Companies Act, 2013 and the Income Tax Act, an organisation has to prepare its income statements annually. However, in some cases, like the retirement of a partner between the accounting period, etc., the firm can prepare interim financial statements.

5. Cost Concept

The cost concept of accounting states that an organisation should record all of its assets at their purchase price in the books of accounts. This amount also includes any transportation cost, acquisition cost, installation cost, and any other cost spent by the firm for making the asset ready to use. For example, Radha Ltd. purchased machinery for ₹60 lakh in July 2021. It has also spent a sum of ₹10,000 on transportation, ₹20,000 on its installation, and ₹15,000 on making it ready to use. The total amount at which the organisation will record the value of machinery in the books of account would be ₹60,45,000.

Therefore, the cost concept or historical cost concept states that since the company is not going to sell the assets as per the going concern concept, there is no point in revaluing the assets and showing their current value. Besides, for practical reasons also, the accountants of an organisation prefer to report the actual costs to its market values. However, the asset amount listed in the books of accounts of the firm does not indicate the value at which it can sell the asset.

6. Dual Aspect or Duality Concept

The dual aspect or duality concept is the foundation of any business. The concept describes the basis of recording business transactions in the books of accounts. According to the concept, every transaction of the business has a two-fold effect. Hence, it should record every transaction in two places. In simple words, two accounts will be affected by a single transaction. This concept can be expressed as the Accounting Equation:

Assets = Liabilities + Capital

The accounting equation states that the total of assets of an organisation is always equal to the total of its owners' and outsiders' claims. These claims or equity of the firm's owners is also known as Capital or Owner's Equity, and the outsiders' claims are known as Liabilities or Creditors' Equity. For example, Rohan started a business by investing a sum of ₹1 crore. This amount will increase the cash (asset side) of the business, and will also increase its capital by the same amount, i.e., ₹1 crore. Therefore, the effect of the transaction will be shown in two accounts, i.e., cash and capital account. The dual concept forms the base of the Double Entry System of Accounting.

7. Revenue Recognition Concept

The revenue recognition concept, also known as the realisation concept, as the name suggests, defines that an organisation should record its revenue from business only when it is realised, not when the firm has received the cash. Let us understand the concept with the help of an example. Suppose a client pays ₹5,000 in advance for a product. The company will not realise the amount of revenue until its work on the product is complete. Therefore, the firm will initially record the amount as a liability in the unearned revenue account. Once the product has shipped to the client, it will be transferred to the revenue account. Let us take another example of delayed payment. Suppose a company ships its goods amounting to ₹10,000 to its customer on the credit of 30 days. The company will realise the same as soon as the goods have been shipped even though it will receive the amount in the future.

8. Matching Concept

The matching concept states that an organisation should recognise its expenses in the same financial year if the expense is related to the revenue of that year. In simple words, if a firm is earning revenue in an accounting period, even though it incurs the expenses related to that revenue in the next accounting year, the expense will be realised in the same accounting year when the revenue has been realised by the firm. For example, if a salesman sells goods worth ₹10,00,000 in February 2022 on a 6% commission made in May 2022, the commission expense of 6% will be charged in the accounting year in which the sales have been made, i.e., 2021-2022. A company should keep in mind that the matching concept should be followed only after the realisation concept has been fulfilled.

9. Full Disclosure Concept

As the name suggests, the full disclosure concept states that an organisation should disclose all the facts regarding its financial performance. It is because the information mentioned in the financial statements is used by different internal and external users, like investors, banks, creditors, management, employees, financial institutions, etc., for making financial decisions. Hence, the concept says that all relevant and material facts or figures about an organisation must be disclosed in its financial statements. To fully ensure this concept, an organisation has to prepare its Balance Sheet and Profit & Loss Account based on the format provided by the Indian Companies Act 1956. Besides, different regulatory bodies, like SEBI, also make it compulsory for companies to completely disclose the true and fair picture of their state of affairs and profitability.

10. Consistency Concept

The consistency concept states that there should be consistency or uniformity in the accounting practices and policies followed by an organisation. It is because the accounting information provided by an organisation through its financial statements would be beneficial only when it allows its users in making a comparison between the statements of different years or with statements of other firms. However, it does not mean that the organisation cannot change its accounting policies when necessary. The firm can make required changes in its policies by properly indicating the probable effect of the changes on its financial results. For example, if a company's management wants to compare the net profit of the current year with the previous year, it can do so only when the accounting policies followed by the company in both years are the same. For example, if a company has used the SLM depreciation method in the previous year and the WDV method of depreciation in the current year; it would not be able to compare the figures.

11. Conservatism Concept

The conservatism or prudence concept believes in playing safely, while recording the transactions in the book of accounts. According to this concept, an organisation should adopt a conscious approach and should not record its profits until they are realised. However, it states that the organisation should realise any loss even if the company has not incurred it yet, or if there is a slight possibility of loss to occurring in the future. No matter how pessimist attitude this concept shows, it is essential for an organisation to deal with uncertainty and allows them to protect the interest of creditors against any unwanted distribution of its assets. For example, if an organisation feels that a certain debtor will not pay the amount in the future, it should open a Provision for Doubtful Debts Account. Similarly, an organisation should not record its increase in the market value of stock until it is sold.

12. Materiality Concept

The materiality concept suggests that an organisation should focus on material facts only. In simple words, an organisation should not waste its time on immaterial facts that do not help in determining its income for the period. In order to differentiate a fact as material or immaterial, one should consider its nature and the amount involved. Therefore, a fact will be considered material if the accountant believes that the information can influence the decisions of a user of the financial statements. For example, the original cost of stationery is insignificant to the users of financial statements. Hence they are not included in the closing stock of the statements and are shown under expenses. Similarly, suppose the company has incurred an expense on the marketing of the firm or its products. In that case, it will be shown in the financial statements as it is a material fact for the users and can change their decisions.

Objectivity Concept

The objectivity concept of accounting states that an organisation should record transactions in an objective manner. It means that the recording should be free from any kind of biasness by accountants and other people. Objectivity in the recording of transactions is possible when the transactions of the firm are supported by verifiable vouchers or documents. The purpose of the objectivity concept is that it does not let the firm’s management and accountants’ opinions impact the financial statements and provide a false image. The concept can be helpful for an organisation in creation of its goodwill. Besides, it warns the companies about the penalties if there is any sort of misinterpretation in the financial statements.

1.1.3 What is an Account?

Business transactions are numberless. The effect of transactions can be evaluated only if similar transactions are placed in a particular place. The technique used for this purpose is called an Account. It is the classified summary of all business transactions that have taken place during a particular period arranged in relation to a person, thing, expense or income. It is written in the form of 'T' having two equal sides; the left-hand side is called the debit side and the right-hand side is called credit side. Recording the effect of a transaction in the debit side of an account is called 'debiting' and recording the effect of a transaction on the credit side of an account is called 'crediting'.

In accounting, "Dr." stands for "debit," and "Cr." stands for "credit." These are abbreviations used to indicate the side of a ledger account where transactions are recorded.

Table 1.1.1

Specimen of an Account

Name of the account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount

1.1.3.1 Classification of Accounts

A company can have many different accounts depending on its transactions. Usually two approaches are followed to classify the accounts viz, English Accounting Approach and American Accounting Approach.

English Accounting Approach

Let us understand the English Approach. Accounts can be classified into three as per English approach. They are real account, personal account and nominal account.

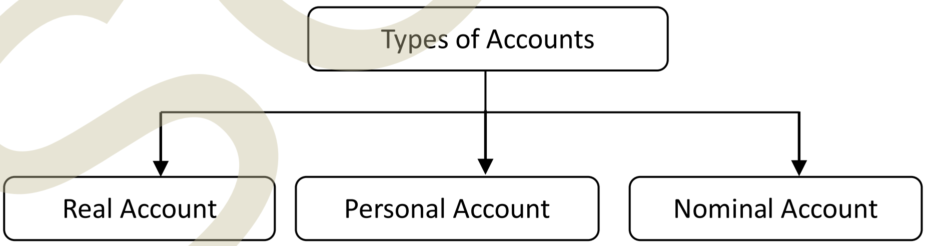

Fig 1.1.3 Types of Accounts

a. Real Account

Real accounts, usually referred to as permanent accounts, are the accounts with balances carried over from one accounting year to the next. In other words, the company's Balance Sheet's ending balance in one reporting year becomes the beginning balance of the following accounting year. Real accounts are accounts of properties, possessions, and things. Real accounts are types of accounts that deal with assets, such as machinery, cash, and furniture.

The accounting rule for the real account is;

"Debit what comes in Credit what goes out"

b. Personal Account

Personal account are related to individuals or entities with which a business has financial transactions. They represent the people, organisations, or entities involved in those transactions. Personal accounts can be further divided as:

◊ **Natural Personal Accounts:** These accounts represent specific individuals and are typically used for recording transactions with customers or suppliers. Examples include accounts of customers, suppliers, employees, and owners.

Example: If you sell goods to a customer on credit, the transaction would be recorded in a personal account called "Accounts Receivable" under the customer's name.

◊ **Artificial/Legal Entity Accounts:** These accounts represent organisations or entities such as companies, banks, or government agencies. They are used to record transactions involving these entities.

Example: If your business takes out a loan from a bank, the transaction would be recorded in a personal account called "Bank Loan" under the name of the lending bank.

◊ **Representative Personal Accounts:** These accounts include those accounts that represent natural or artificial persons such as outstanding expenses, accrued incomes etc.

The accounting rule for personal account is;

"Debit the receiver And credit the giver"

c. Nominal Account

Accounts which are neither personal nor real are called nominal accounts. These accounts are related to expenses, incomes, losses and gains. Nominal accounts are closed at the end of each accounting period to calculate the net income or net loss.

The accounting rule for the nominal account is;

"Debit all expenses and losses Credit all incomes and gains"

As a conclusion, Personal accounts record transactions related to people the company deals with, such as customers, suppliers, employees, etc. Real accounts record transactions related to assets like land, buildings, equipment, inventory, etc. that the company owns. Nominal accounts record transactions related to expenses, revenues, gains, losses (basically the income and expenses of the business). So rather than having all transactions jumbled together, separating them into these three account types allows for easier tracking and management of transactions involving people, assets, and income/expenses respectively. The number of accounts in each category will vary based on the size and activities of the specific company. But this three-way classification provides an organised structure for recording the many different types of business transactions.

American Accounting Approach

Let us understand the American Approach Accounts can be classified into five categories:

1. Assets - These accounts track tangible or intangible property owned by the company, as well as anything else of value that the company owns that has a monetary value. Examples include cash, accounts receivable, inventory, land, buildings, equipment, trademarks, and goodwill. Assets represent resources available to support business operations.
2. Liabilities - These accounts reflect debts, obligations, or other amounts owed by the company. Common examples are accounts payable, wages payable, taxes payable, loans payable, and mortgages payable. Liabilities represent claims on company assets by creditors and obligations that must be paid at some point.
3. Owners' Equity - Also called capital or net worth, these accounts reflect the residual interest or shareholders' claims on the company's assets after deducting liabilities. This includes amounts invested by shareholders plus accumulated profits.
4. Revenue - These accounts track income generated from the company's operations and other sources. Revenue arises from sales of products or services, interest, dividends, and gains on asset sales. Revenues increase owners' equity.
5. Expenses - These accounts reflect costs incurred by the company to generate revenue. Expenses reduce owners' equity. Common expenses include wages, raw materials, interest, rent, utilities, depreciation, and taxes.

Debit and Credit Rules for Different Account Types:

◊ Asset accounts normally have a debit balance. To increase an asset, debit the asset account. To decrease an asset, credit the asset account.

◊ Expense accounts normally have a debit balance. To increase an expense, debit the expense account. To decrease an expense, credit the expense account.

◊ Capital, liability, and income accounts normally have a credit balance. To increase capital, liabilities, or income, credit those accounts. To decrease capital, liabilities, or income, debit those accounts.

Summary of Debit and credit rules :

◊ Debit to increase asset and expense accounts

◊ Credit to decrease asset and expense accounts

◊ Credit to increase capital, liability, and income accounts

◊ Debit to decrease capital, liability, and income accounts

Recap

- ◊ Accounting is a systematic process of recording, classifying, and summarising financial transactions.
- ◊ The main branches of accounting are management accounting, cost accounting, and financial accounting.
- ◊ Basic financial statements include Income Statement, Balance Sheet, Cash Flow Statement, and Statement of Owner's Equity.
- ◊ There are 13 important accounting concepts, including business entity, money measurement, and going concern.
- ◊ The golden rules of accounting guide the recording of transactions for real, personal, and nominal accounts.
- ◊ Accounts are classified into real, personal, and nominal categories based on English Accounting Approach and are classified into Assets, Liabilities, Owners' Equity, Revenue and Expenses.

Objective Questions

1. What is the language of business?
2. Who uses financial statements?
3. What does GAAP stand for?
4. What concept treats business separately from its owner?
5. Which statement shows a company's financial position at a specific date?
6. What does "Dr." stand for in accounting?
7. Which accounting branch focuses on cost analysis?
8. What's the accounting equation?
9. Which concept assumes a business will continue indefinitely?
10. What type of account deals with expenses and incomes?
11. Which statement shows cash inflows and outflows?
12. What's the golden rule for real accounts?
13. Which concept emphasises consistency in accounting practices?
14. What's recorded on the left side of a T-account?
15. Which statement shows changes in owner's equity?

Answers

1. Accounting
2. Stakeholders
3. Generally Accepted Accounting Principles
4. Business entity
5. Balance Sheet
6. Debit
7. Cost accounting
8. Assets = Liabilities + Equity
9. Going concern
10. Nominal account
11. Cash Flow Statement
12. Debit what comes in
13. Consistency concept
14. Debit
15. Statement of Owner's Equity

Assignments

1. Define accounting according to AICPA.
2. What are the main processes involved in accounting?
3. List the four basic financial statements.
4. Explain the business entity concept.
5. What is the purpose of the cash flow statement?
6. Describe the matching concept in accounting.
7. What are the three golden rules of accounting?
8. How would you apply the conservatism concept when recording potential future losses for a company?
9. In what ways can the going concern concept affect the valuation of assets on a balance sheet?

10. How would you use the materiality concept to decide whether to record a small office supply purchase as an asset or an expense?
11. How might a company's choice of depreciation method affect its financial statements under the consistency concept?
12. How would you apply the revenue recognition concept to a software company that receives advance payments for annual subscriptions?

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Unit 2

Single and Double Entry Systems

Learning Outcomes

Upon the completion of this Unit, the learner will be able to;

- ◊ comprehend the differences between single-entry and double-entry accounting systems.
- ◊ learn the process of journalising transactions and posting to ledger accounts.
- ◊ develop skills in balancing and closing various types of ledger accounts.
- ◊ comprehend the importance of maintaining accurate financial records through proper accounting practices.
- ◊ apply the rules of debit and credit in recording different types of business transactions.

Prerequisites

You are running a lemonade stand on a hot summer day. As customers line up, you're busy squeezing lemons, pouring drinks, and collecting money. At the end of the day, you want to know how much you made. A notebook where you note down every sale and expense. Each time you sell a cup of lemonade, you write down the amount you received. When you buy more lemons or cups, you note down what you spent. It is like keeping a diary of your lemonade business but focused on money in and money out. This simple method is the essence of the single-entry system. It is perfect for small businesses like your lemonade stand. You don't need to be a math whiz or an accounting expert to use it. Just write down what comes in and what goes out, and at the end of the day, you can easily see if you made a profit. This straightforward approach is the reason that many small shop owners, freelancers, and even some cafes use the single-entry system.

It is a simple yet effective way to keep track of business finances without getting lost in complex accounting jargon or procedures.

In this unit let us learn the single-entry and double-entry system in detail along with journal and ledger.

Keywords

Single-entry System, Single-entry Bookkeeping, Double-entry system, Journal, Ledger

Discussion

1.2.1 What is a Single-Entry System?

Have you ever wondered about the financial management of your neighbourhood cafe? Their transactions range from revenue generated (selling various coffees and snacks) to expenses (purchasing ingredients and paying for utilities and rent). Most likely, they need an uncomplicated and effective method for documenting daily sales, purchases, and costs. Here is the relevance of the single-entry system. This system allows cafe proprietors to carefully record income and expenses without much complexity. It provides precise financial monitoring without requiring advanced accounting knowledge.

A single-entry system is a simple method of accounting where each transaction is recorded only once. It focuses mainly on the income statement, tracking cash coming in and going out of the business. This system primarily records cash receipts and disbursements, usually in a cash book that looks like an expanded check register. The cash book has columns to note different sources and uses of money, with spaces to show starting and ending balances. Unlike more complex accounting methods, the single-entry system doesn't typically keep track of assets and liabilities, which must be managed separately if needed. This straightforward approach makes it suitable for small businesses or individuals who want a basic way to monitor their finances without going into more complicated accounting practices.

Example of Single-Entry System

Let us consider a small IT services company named "Tech Innovations," using the single entry system to manage its finances. Here is a simplified example of how they might record their transactions for a month:

Service Revenue: Tech Innovations records the total cash received from clients for IT services provided in the month, say ₹1,50,000.

Equipment Purchase: The company purchases new laptops for the team costing ₹80,000 in cash, which is recorded as an outgoing payment.

Office Rent Payment: They pay the office rent in cash, ₹30,000, and note it down in their ledger.

Utility Payment: Utility bills for electricity and internet services amounting to ₹20,000 are paid in cash and recorded.

Salary Payments: Salaries paid to employees in cash, totalling ₹50,000, are also recorded.

Miscellaneous Expenses: Small cash purchases for office supplies amount to ₹5,000, noted as miscellaneous expenses.

1.2.1.1 Features of Single-Entry System

a. **Simplicity:** Designed for ease of understanding and use, requiring no formal accounting training.
b. **Cost - effective:** Low setup and maintenance costs, ideal for small business budgets.
c. **Cash Focus:** Primarily tracks cash transactions, highlighting cash flow status.
d. **Minimal Record-Keeping:** Requires fewer books and records, simplifying financial tracking.
e. **Flexibility:** Adaptable to a business's specific needs without strict rules.
f. **Limited Financial Insight:** Provides a basic overview of financial performance without detailed analytics.
g. **Increased Error Risk:** Lacks the checks and balances of double-entry systems, raising the potential for mistakes and fraud.

1.2.1.2 Advantages of Single-Entry System

a. **Ease of Maintenance:** The hallmark of the Single-entry accounting system is its simplicity. It does not require users to have an in-depth understanding of complex accounting principles. Instead, businesses can maintain their financial records with basic knowledge of cash flows. This simplicity is particularly advantageous for small business owners or entrepreneurs who may not have formal training in accounting or finance. They can easily track their transactions without getting bogged down in the complexities of more sophisticated accounting systems.
b. **Cost Efficiency:** For small businesses operating with tight budgets, the Single-entry accounting system is a cost-effective solution. It eliminates the need for expensive accounting software or the hiring of professional accountants. Since the system revolves around basic record-keeping (often limited to a single ledger or a basic accounting software package) the financial overhead associated with maintaining financial records is significantly reduced. This aspect is especially

beneficial for startups and small enterprises looking to maximise their financial resources.

c. **Time-Saving:** Given its straightforward approach, the Single-entry system saves considerable time that would otherwise be spent on detailed account management. Business owners can quickly record transactions without having to match debits and credits across multiple accounts. This efficiency allows them to dedicate more time and energy to operational concerns, customer service, and strategic planning rather than being consumed by intricate accounting tasks.

d. **Flexibility:** The system's lack of rigid structure offers businesses the flexibility to tailor their accounting practices to their specific needs. Unlike the double-entry system, which requires meticulous recording in two or more accounts for each transaction, the Single Entry System can adapt to the unique financial transactions of a business. This adaptability makes it easier for businesses to modify their accounting practices as they grow or as their financial transactions become more complex.

e. **Immediate Overview of Cash Flow:** One of the primary benefits of the Single entry system is its focus on cash transactions, providing an immediate overview of the business's cash flow. This is crucial for small businesses, where managing cash flow effectively can be the difference between success and failure. By tracking cash receipts and disbursements, business owners can quickly assess their financial health, make informed decisions about expenditures, and plan for future financial needs.

f. **Less Paperwork:** The simplicity of the Single entry accounting system means it requires fewer books and records, leading to less paperwork. This streamlined approach can make financial administration more manageable, reducing the likelihood of errors and ensuring that important financial information is readily accessible. For businesses without the resources to manage extensive paperwork, this system offers a practical solution.

1.2.1.3 Disadvantages of Single-Entry System

a. **Limited Financial Information:** The single-entry accounting system provides a basic overview of cash transactions but lacks the detailed financial information necessary for comprehensive financial analysis. It does not record assets, liabilities, and equity in detail, making it difficult to determine the overall financial health of a business beyond its immediate cash flow.

b. **Inaccuracy and Error Risks:** Without the checks and balances inherent in the double-entry system, where every transaction is recorded twice to ensure accuracy, the single-entry system is more susceptible to errors and inaccuracies. Mistakes in recording transactions can go unnoticed, leading to misleading financial information.

c. **Difficulty in Detecting Fraud:** The lack of detailed records and the absence of a systematic reconciliation process make it harder to detect fraudulent activities within the business. The single-entry system's simplicity can be exploited to hide unauthorised transactions or mismanagement of funds.

d. **Inadequate for Complex Businesses:** As businesses grow and their transactions become more complex, the single-entry system becomes increasingly inadequate. It cannot effectively handle credit transactions, inventory management, fixed assets depreciation, or loans, which are crucial aspects of a growing business's financial management needs.

e. **Challenges in Tax Preparation:** The system's lack of comprehensive financial records can pose challenges during tax preparation. Businesses might find it difficult to substantiate their income, expenses, and financial position to tax authorities, potentially leading to audits or penalties.

1.2.2 Single-Entry Bookkeeping

Single-entry bookkeeping is an accounting system used to keep track of finance or fund of a business. There is only one entry made per business transaction. Most entries record incoming or outgoing funds. Transactions are recorded in a "cash book", a journal with columns that organise transaction details like date, description, and whether it is an expense or income.

The transactions are recorded in the cash book for single-entry cash balance bookkeeping are Taxable income, Tax-deductible expenses and Cash at bank and hand. Each business transaction is listed in one column and is either positive or negative. It is possible to split revenue and expenses into separate columns, but because each such accounting transaction is still recorded on a single line, this also qualifies as single-entry bookkeeping.

Single-entry bookkeeping can be performed in accounting software, but in its simplest form, it can also be recorded in a table. The journal you use to record transactions is called a cash book.

At a minimum, a cash book records:

◊ Transaction date
◊ A brief description of the transaction
◊ Transaction value: this can be placed in either an income (credit) or expense (debit) column
◊ Balance: a running tally of cash on hand or bank

You can also add a column for notes and accurate financial records. The table's last row should show the accounting period's ending balance (at month-end or year-end, for example).

Let's say you are running a small bakery. Here's how you might use single-entry bookkeeping:

First, let's create the journal:

Here are the transactions for the given single entry bookkeeping journal:

1. July 29, 2024: Starting balance of ₹5,000.00

2. July 29, 2024: Expense of ₹200.00 for flour purchase, reducing balance to ₹4,800.00
3. July 29, 2024: Income of ₹500.00 from daily sales, increasing balance to ₹5,300.00
4. July 30, 2024: Expense of ₹150.00 for sugar and eggs purchase, reducing balance to ₹5,150.00
5. July 30, 2024: Income of ₹550.00 from daily sales, increasing balance to ₹5,700.00
6. July 31, 2024: Expense of ₹300.00 for utility bill payment, reducing balance to ₹5,400.00
7. July 31, 2024: Income of ₹600.00 from daily sales, increasing balance to ₹6,000.00
8. August 1, 2024: Expense of ₹800.00 for employee wages, reducing balance to ₹5,200.00
9. August 1, 2024: Income of ₹700.00 from daily sales, increasing balance to ₹5,900.00
10. August 2, 2024: Expense of ₹100.00 for packaging supplies, reducing balance to ₹5,800.00
11. August 2, 2024: Income of ₹800.00 from daily sales, increasing balance to ₹6,600.00

These transactions show the daily income and expenses over a five-day period, with the final balance on August 2, 2024, being ₹6,600.00.

Single Entry Bookkeeping Journal

Date	Description	Income (₹)	Expenses (₹)	Balance (₹)
07/29/2024	Starting balance			5,000.00
07/29/2024	Flour purchase		200.00	4,800.00
07/29/2024	Daily sales	500.00		5,300.00
07/30/2024	Sugar and eggs purchase		150.00	5,150.00
07/30/2024	Daily sales	550.00		5,700.00
07/31/2024	Utility bill payment		300.00	5,400.00
07/31/2024	Daily sales	600.00		6,000.00
08/01/2024	Employee wages		800.00	5,200.00
08/01/2024	Daily sales	700.00		5,900.00
08/02/2024	Packaging supplies		100.00	5,800.00
08/02/2024	Daily sales	800.00		6,600.00

Now, let's create the ledger. In a single-entry system, the ledger is often simplified and may focus on summarising income and expenses by category:

Single Entry Bookkeeping Ledger

Income Summary

Category	Total (₹)
Daily sales	3,150.00
Total Income	3,150.00

Expense Summary:

Category	Total (₹)
Ingredients	350.00
Utilities	300.00
Wages	800.00
Supplies	100.00
Total Expenses	1,550.00

Summary:

Items	Amount (₹)
Starting Balance	5,000.00
Add: Total Income	3,150.00
Less: Total Expenses	1,550.00
Ending Balance	6,600.00
Net Profit (Ending Balance – Starting Balance)	1,600.00

1.2.3 Double Entry System

Suppose you purchased machinery for your firm by paying ₹50000. This transaction has two aspects, one is the receiving aspect and the other is the giving aspect. When you purchase the machinery, machinery came to your firm and cash is given to the supplier. That means machinery is considered the receiving aspect and cash is the giving aspect. Every transaction is accounted for a 'receiving aspect' and a 'giving aspect.' This is called the double-entry system of accounting. The double-entry accounting method requires that each business transaction be recorded in a minimum of two accounts. It also states that the total debits and credits for a transaction must be equal, or else the record is considered out of balance. These rules ensure a company's accounting equation remains properly balanced at all times.

The double-entry system is widely considered more accurate than the single-entry system due to its inherent structure and comprehensive approach to financial recording. At its core, the double-entry method requires each transaction to be recorded twice - as both a debit and a credit - ensuring that the total debits always equal the total credits.

This built-in balancing act serves as an automatic error detection mechanism, making it easier to spot mathematical mistakes or omissions. The system provides a complete representation of every financial event, capturing both aspects of each transaction and maintaining the fundamental accounting equation (Assets = Liabilities + Equity) at all times. This comprehensive approach creates a clear audit trail, making it easier to trace and verify transactions, which is crucial for accuracy and accountability.

Furthermore, the double-entry system's standardised process for recording debits and credits reduces the risk of subjective or inconsistent entries, enhancing overall accuracy. Its structure also supports enhanced internal controls, making it more difficult to manipulate records without detection. The system's ability to track all account types - assets, liabilities, equity, income, and expenses - provides a more accurate and complete picture of a business's financial state. This comprehensive view not only improves accuracy but also facilitates more in-depth financial analysis and decision-making. Additionally, the double-entry system is better equipped to handle complex transactions, ensuring that all aspects of multi-faceted financial events are properly recorded. Lastly, the system's structure makes account reconciliation easier, further contributing to its accuracy by allowing for the swift identification and correction of discrepancies. These combined features make the double-entry system a more reliable and accurate method for financial record-keeping compared to the single-entry system.

1.2.3.1 Rules of Double Entry Accounting

Double-entry accounting rules are essential guidelines that govern how transactions are recorded in the accounting system. These rules ensure that the accounting equation (Assets = Liabilities + Equity) remains balanced. Here are the fundamental rules:

For Assets:

- ◊ Increase in an asset is debited: When the value of an asset increases (e.g., receiving cash or purchasing equipment), the asset account is debited.
- ◊ Decrease in an asset is credited: When the value of an asset decreases (e.g., paying cash or selling equipment), the asset account is credited.

For Liabilities:

- ◊ Increase in liability is credited: When the company incurs a liability (e.g., taking a loan or purchasing goods on credit), the liability account is credited.
- ◊ Decrease in a liability is debited: When a liability is reduced (e.g., repaying a loan or paying off a creditor), the liability account is debited.

For Equity:

- ◊ Increase in equity (e.g., owner's investments, profits) is credited: This includes contributions from owners or earning profits.
- ◊ Decrease in equity (e.g., owner's withdrawals, losses) is debited: This includes withdrawals by owners or incurring losses.

For Revenue:

◊ Increase in revenue is credited: When the company earns revenue (e.g., sales revenue, service income), the revenue account is credited, reflecting an increase in equity.

For Expenses:

◊ Increase in expenses is debited: When the company incurs expenses (e.g., rent, utilities, salaries), the expense account is debited, reflecting a decrease in equity.

1.2.3.2 Advantages of Double Entry System

a. **Accuracy of Financial Records:** By requiring that every transaction be recorded in at least two accounts, the double entry system helps ensure that the accounting equation (Assets = Liabilities + Equity) remains balanced. This dual recording process reduces the risk of errors and omissions, leading to more accurate financial records.

b. **Error Detection and Correction:** The double-entry system facilitates the detection and correction of errors. Since the sum of debits must equal the sum of credits, any discrepancy can be traced and corrected more easily than in a single-entry system.

c. **Comprehensive Financial Overview:** This system provides a complete picture of a business's financial activities. Recording both aspects of each transaction (e.g., the source and use of funds) offers a comprehensive view of the company's financial health.

d. **Enhanced Financial Analysis and Reporting:** The detailed records maintained in the double-entry system support thorough financial analysis and reporting. This detailed financial data is crucial for making informed business decisions, preparing financial statements, and analysing trends over time.

e. **Improved Financial Management and Control:** The double entry system helps businesses manage their finances more effectively by providing detailed insights into every aspect of their financial operations. It allows for better budgeting, financial planning, and control over cash flows and expenditures.

f. **Facilitates Audit and Compliance:** The systematic and detailed nature of the double-entry accounting system simplifies the audit process. It provides auditors with clear trails of all transactions, making it easier to verify the accuracy of financial statements and ensure compliance with accounting standards and regulations.

1.2.3.3 Disadvantages of the Double Entry System

a. **Complexity:** Double-entry accounting requires understanding debits, credits, and the accounting equation, making it more complex than single-entry systems. This complexity can be daunting for those without formal accounting training.

b. **Time-Consuming:** Recording every transaction twice, as both a debit and a credit, can be time-consuming, especially for businesses with a high volume of transactions.

c. **Costly for Small Businesses:** The complexity and time requirements may necessitate hiring a professional accountant or investing in accounting software, which can be costly for small businesses or startups with limited resources.

d. **Higher Risk of Errors:** The need to make two entries for every transaction increases the risk of errors. Mistakes in recording can lead to an unbalanced ledger, requiring additional time and effort to locate and correct.

e. **Overly Detailed for Simple Operations:** For small businesses with straightforward financial transactions, double-entry accounting can provide more detail than necessary, complicating financial management without adding significant value.

1.2.4 Difference between Single-Entry System and Double-Entry System

The main differences between single-entry and double-entry accounting systems are given in the table below.

Aspect	Single-Entry System	Double-Entry System
Complexity	Simple, resembling a check book register	More complex, involving at least two accounts per transaction
Recording method	Each transaction is recorded only once	Each transaction is recorded twice (debit and credit)
Accounts tracked	Primarily tracks income and expenses	Tracks all financial aspects including assets, liabilities, and equity
Financial statements	Mainly supports income statement preparation	Supports preparation of income statement, balance sheet, and cash flow statement
Accuracy and error detection	More prone to errors, harder to detect mistakes	Built-in error detection through balanced debits and credits
Suitability	Suitable for small businesses with simple finances	Suitable for larger businesses and complex financial structures
Comprehensiveness	Provides limited financial information	Offers a complete picture of financial health
Audit trail	Limited audit trail	Provides a clear audit trail for each transaction
Accounting equation	Doesn't inherently maintain the accounting equation	Maintains the accounting equation (Assets = Liabilities + Equity)
Financial analysis	Limited capability for in-depth financial analysis	Supports comprehensive financial analysis and reporting

1.2.5 Journal

Financial data in an organisation can be extensive, making analysis difficult without proper record-keeping. To initially record transactions, firms use a journal, which is a chronological log of financial entries. Keeping this journal is crucial for organisations to systematically track their finances. Journals are created based on supporting documentation like bills, vouchers, and invoices that provide the raw data for financial transactions. The process of logging business transactions in the journal is known as journalising. Each recorded transaction in the journal is a journal entry. Below each entry, a brief narrative description of the transaction is included to provide context. This explanation of the entry is known as the narration. Narrations serve to summarise the journal entry and provide clarification on the transaction.

Table 1.2.1 Format of a Journal

W	Particulars	L.F.	Dr. Amount	Cr. Amount

1.2.5.1 Journalising Process

Recording all of a business's financial transactions in a journal as they occur is called journalising. These journal entries are logged in the journal during this process. No transaction can happen without first being noted in the journal before entering the accounting records. Nowadays, companies may keep multiple types of journals since businesses vary greatly in size and function. Journals are divided into two categories: General and Special. The most common type is the general journal, which records every transaction within a company. The general journal is more common among smaller businesses with fewer transactions. Larger trade or manufacturing companies find this record-keeping cumbersome, so they require separate, specialised journals to efficiently log certain routine transactions. The format and content of specialised journals are not subject to any standards. They are customised based on the needs, activities, and assets of the business.

1.2.5.2 Preparation of Journal

A journal has 5 columns: date, details, ledger folio, debit amount, and credit amount. The ledger folio column shows the ledger page number where the journal entry will later be transferred. Therefore, the ledger folio is left blank when initially recording the journal entry. Journal entries follow specific rules for debiting and crediting the different types of accounts involved in a transaction. Major steps in journalising, that you should remember while preparing the journal are:

1. Read the given transaction carefully and identify the accounts related to the transaction.
2. Then identify the type of accounts in the given transaction. The type of account includes personal account, real account, and nominal account.

3. Identify which account to be debited and which account to be credited based on the rules of accounts.
4. Enter the transaction date in the date column.
5. In the particulars column write the debit entry (write Dr. at the end of the debit) and in the next line write the credit entry (after leaving a little space from the left side and start with 'To') and give a narration below the entry.
6. Enter the debit amount and credit amount in the respective columns.

1.2.5.3 Importance of Journalising

1. The main purpose of journalising is to maintain accurate and organised financial records for a company. Information is entered into the journal chronologically using debits and credits, making it easy to review and catch accounting mistakes.
2. Financial statements creation by companies, which is the main goal of the accounting cycle, relies on this data. Auditors can examine the impact of transactions on a company using these records.
3. Transactions recorded chronologically in the journal allow us to get complete timely information about business transactions.
4. The journal serves as the basis for posting entries into the ledger. This makes the accountant's job easier and reduces errors.
5. Journalising is critical for shareholders and other stakeholders. Creditors, investors, shareholders, and tax authorities require full financial transparency to assess if a company is worth investing in and/or applying accounting standards to.

1.2.5.4 Points to Consider while Journalising

It is important to note the following points while recording different business transactions in to journal.

a. Journal entries can be single entries with one debit and one credit, compound entries with one debit and two or more credits, entries with multiple debits and one credit, and entries with multiple debits and credits. It's important to ensure the total debits and credits are equal in these cases.

b. If the journal spans multiple pages:

- ◊ The amounts on each page should be totalled.
- ◊ The ending balance printed at the bottom of that page.
- ◊ The same total should be brought forward at the top of the next page.

This ensures continuity across journal pages.

For Example, 20/03/2020: Sold goods for cash ₹400.

This is a cash transaction and the two aspects of these transactions are cash and goods (sales). Both these aspects come under the real account. There, cash comes in and goods go out in the form of sales. The accounting rule for the real account is "debit what comes in and credit what goes out." So, the journal entry is;

Cash A/c   Dr.   ₹400

    To Sales A/c   ₹400

Journal

Date	Particulars	L. F.	Dr. Amount	Cr. Amount
20/03/2020	Cash A/c Dr. To Sales A/c (Sold goods for cash)		400	400

Illustration

Journalise the following transactions:

01/01/2021 Started business with cash ₹95000

11/01/2021 purchased goods for ₹15000

24/01/2021 Purchased furniture for ₹30000

28/01/2021 Sold goods for cash ₹20000

30/01/2021 Paid wages for ₹15000

Hints for easy preparation: *Apply the rules of Personal Account for capital account (it is a personal account because it is an account of owners who are real persons), Apply the rule of real account for cash account, the purchase account, furniture account, sales account and apply the rule of Nominal Account for wages.*

Solution:

Journal

Date	Particulars	L. F.	Dr. Amount	Cr. Amount
01/01/2021	Cash A/c Dr. To Capital A/c (Started Business with cash)		95000	95000
11/01/2021	Purchases A/c Dr. To Cash A/c (Purchased goods for cash)		15000	15000
24/01/2021	Furniture A/c Dr. To Cash A/c (Purchased furniture for cash)		30000	30000

28/01/2021	Cash A/c Dr. To Sales A/c (Sold goods for cash)		20000	 20000
30/01/2021	Wages A/c Dr. To Cash A/c (Paid wages)		15000	 15000

Illustration:

Journalise the following:

01/01/2021 Started business with ₹100000

02/01/2021 Deposit cash to bank ₹10000

03/01/2021 Bought goods for cash ₹25000

06/01/2021 Sold goods for cash ₹10000

08/01/2021 Paid ₹1000 for telephone charges

11/01/2021 Paid ₹2500 for advertisement

24/01/2021 Bought goods from M/s Manha Co for ₹30000 on credit

25/01/2021 Sold goods to M/r Arnav Co for ₹20000 on credit

26/01/2021 Paid rent ₹3000

27/01/2021 Sold goods to DZN Co. for ₹4000 for cash

28/01/2021 Paid salaries ₹25000

30/01/2021 Withdraw from bank ₹15000 for private use

Solution:

Journal

Date	Particulars	L. F.	Dr. Amount	Cr. Amount
01/01/2021	Cash A/c Dr. To Capital A/c (Started Business with cash)		100000	 100000
02/01/2021	Bank A/c Dr. To Cash A/c (Cash deposited with Bank)		10000	 10000
03/01/2021	Purchases A/c Dr. To Cash A/c (Purchased goods for cash)		25000	 25000

06/01/2021	Cash A/c Dr. To Sales A/c (Sold goods for cash)		10000	 10000
08/01/2021	Telephone Charges A/c Dr. To Cash A/c (Paid telephone charges)		1000	 1000
11/01/2021	Advertisement A/c Dr. To Cash A/c (Paid advertisement charges)		2500	 2500
24/01/2021	Purchases A/c Dr. To M/s Manha Co. (Purchased goods on credit)		30000	 30000
25/01/2021	M/r Arnav Co. Dr. To Sales A/c (Sold goods for credit)		20000	 20000
26/01/2021	Rent A/c Dr. To Cash A/c (Paid rent)		3000	 3000
27/01/2021	Cash A/c Dr. To Sales A/c (Sold goods for cash)		4000	 4000
28/01/2021	Salaries A/c Dr. To Cash A/c (Paid Salaries)			
30/01/2021	Drawings A/c Dr. To Bank A/c (Amount is withdrawn from bank for private use)		15000	 15000

Illustration:

From the following extract of a journal find out the business transaction behind the entry.

Date	Particulars	L. F.	Dr. Amount	Cr. Amount
03/03/2022	Purchases A/c Dr. To Account Payable_Kurup & Friends A/c To Cash A/c (Purchases by credit and by cash)		3000	 1000 2000
04/03/2022	Accounts Receivables Johnson & Sons A/c Dr. Cash A/c To Sales (Purchases by cash and credit from Johnson & Sons)		1500 5000	 6500

Solution:

i. Bought goods by giving cash ₹2000 and on credit from Bilal and Friends for ₹1000

ii. Made a total sale of ₹6500 out of which ₹5000 is for cash and ₹1500 to Rahman and Sons for credit.

1.2.6 Ledger

Galaxy Pvt Ltd faced a challenge with its accounting records. While their journal entries were accurate, the sheer volume made it difficult to locate specific transaction types. To address this, the company needed to implement a system called Ledger. Galaxy needed to transfer the journal entries into the ledger, this process is called posting. Posting involves transferring journal entries into a ledger, which organises transactions by account type. This categorisation allows for easier retrieval and analysis of financial data. For instance, all cash-related transactions are grouped under the Cash account in the ledger.

The primary purpose of a ledger is to consolidate similar transactions, providing a clearer financial picture. This enables organisations to simplify data access and comprehension, enabling more efficient financial management and decision-making.

1.2.6.1 Preparation of Ledger Account

◊ A ledger account has two sides: one is a debit, which is visible on the left side of the account, and the other is a credit, which is visible on the right side of the account.

◊ All financial transactions have corresponding debit entries that are recorded on the account's debit side, and corresponding credit entries that are recorded on the account's credit side.

◊ The balance is represented by the difference between the debit and credit sides. The excess of the debit side over the credit side is represented by a debit balance, and the opposite is true for a credit balance.

The closing balance at the end of the accounting period is sent over to the succeeding year as an opening balance.

Table 1.2.2 Format of Ledger

Dr. Name of the Account Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount

Ledger accounts cover various financial aspects, such as cash, sales, purchases, and capital. Each ledger has a standardised format with debit (Dr.) and credit (Cr.) columns. These columns include fields for date, particulars, journal folio (J.F.), and amount. The

J.F. references the journal page where the original entry is found.

When transferring data from journals to ledgers, follow specific rules for each account type. For example, in the cash account, outgoing money is credited while incoming funds are debited. Apply similar principles to other account types as you post entries.

Posting is the act of moving debit and credit items from the journal to their respective ledger accounts. It's crucial to adhere to accounting principles during this process to maintain accuracy and consistency in financial records.

1.2.6.2 Rules for Posting Transactions in Ledger Accounts

- ◊ For each account, a distinct individual account is set up in the ledger book, and entries from the journal are correspondingly sent to the appropriate accounts.
- ◊ Using the terms "To," "By," "Dr," or "Cr" when posting transactions to the ledger is customary. In the particulars column with the accounts recorded on the debit side, the word "To" or "Dr" is used, whereas "By" or "Cr" is employed for the accounts put in the specific column on the credit side.
- ◊ The relevant account that was debited in the journal must likewise be debited in the ledger, but with the appropriate credit account as the reference.

We can prepare ledger accounts based on the journal. A journal entry is given below; How to post this journal entry in the ledger?

Journal

Date	Particulars	L. F.	Dr. Amount	Cr. Amount
20/03/2020	Cash A/c Dr. To Sales A/c (Sold goods for cash)		400	 400

Ledger accounts are prepared based on the journal entries. In this transaction, there are two accounts involved, a cash account and a sales account. So, when we are preparing a ledger, we need to separately open accounts for both these entries. First, the cash account should be opened, and then the sales account. All the transactions are posted in the corresponding account. If a cash account is opened, the name 'Cash account' is written at the top centre of the account. Journal entries are posted in the ledger in the order of their dates. First, open a cash account, Second, the date, Third, write the opposite transaction (the other account to be credited). Here, it is the sales account and is written as 'To sales account' on the debit side. It is customary to use the word 'To' on the debit side and 'By' on the credit side. After that, record the page number of the journal if it is given, from where the entry is taken in the journal folio column. Then enter the amount in the respective 'debit amount' column. In the next step, we should open another account, that is credit account and write the opposite entry in the credit column. Here, it is written as 'By cash,' then enter the amount in the respective credit column.

1.2.6.3 Balancing and Closing the Ledger Account

After posting all the transactions to the ledger account, Galaxy Pvt. Ltd. identified that there was a difference between the debit side total and credit side total. They started balancing the account with the help of their friend Jay, an accountant. Let us discuss the process of balancing accounts. Balance is the difference between the two sides of an account. If the debit side amount is more than the credit side amount, it is called debit balance. If the credit side amount is more than the debit side it is known as credit balance.

For balancing the account, first we should calculate the difference between the total debit amount and total credit amount. If the debit side amount is more than the credit side, the difference is written on the credit side amount column as 'By Balance c/d' (c/d means carried down). If credit total is more than debit total, then the difference is writ ten on the debit side as 'To balance c/d' in the Particulars column. The amount of balance c/d is brought forward in the opposite side of the account by entering it as balance b/d (brought down). Here, in the cash account, the amount of 'By balance c/d' is in the credit column so you write it this as balance b/d in the next year on the debit column. Remember only Real and Personal accounts are balanced whereas nominal accounts are closed at the end of the year by transferring the balance to Trading or Profit and Loss Account.

Cash Account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
20/03/2020	To Sales A/c		400	31/03/2020	By Balance c/d		400
			400				400
01/04/2020	To Balance b/d		400				

Like this, we should prepare a sales account for the entry.

Sales Account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
31/03/2020	To Balance Transferred		400	20/03/2020	By Cash A/c		400
			400				400

Illustration:

From the following particulars, prepare a journal and post them in the ledger.

05/03/2021 Started business with cash ₹250000

12/03/2021 purchased goods for ₹40000

29/03/2021 Sold goods for cash ₹35000

30/03/2021 Paid wages for ₹10000

31/03/2021 Paid rent ₹4000

Journal

Date	Particulars	L. F.	Dr. Amount	Cr. Amount
05/03/2021	Cash A/c Dr. To Capital A/c (Started Business with cash)		250000	 250000
12/03/2021	Purchases A/c Dr. To Cash A/c (Purchased goods for cash)		40000	 40000
29/03/2021	Cash A/c Dr. To Sales A/c (Sold goods for cash)		35000	 35000
30/03/2021	Wages A/c Dr. To Cash A/c (Paid)		10000	 10000
31/01/2021	RentA/c Dr. To Cash A/c (Paid rent)		4000	 4000

Ledger

Cash Account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
05/03/2021	To Capital A/c		250000	12/03/2021	By Purchases A/c		40000
29/03/2021	To Sales A/c		35000	30/03/2021	By Wages A/c		10000
				31/03/2021	By Rent A/c		4000
				31/03/2021	By Balance c/d		231000
			285000				285000
01/04/2021	To Balance b/d		231000				

Capital Account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
31/03/2021	To Balance c/d		250000	05/03/2021	By Cash A/c		250000
			250000				250000
				01/04/2021	By Balance b/d		250000

Purchases Account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
12/03/2021	To Cash A/c		40000	31/03/2021	By Balance transferred		40000
			40000				40000

Sales Account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
				29/03/2021	By Cash A/c		35000
31/03/2021	To Balance transferred		35000				
			35000				35000

Wages Account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
30/03/2021	To Cash A/c		10000				
				31/03/2021	By Balance transferred		10000
			10000				10000

Rent Account

Dr. Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
31/03/2021	To Cash A/c		4000				
				31/03/2021	By Balance transferred		4000
			4000				4000

Note: Assets and liabilities accounts are balanced whereas accounts related to expenses and income are closed to trading or Profit and Loss Account.

Recap

Single-Entry System:

- ◊ Simple method recording each transaction only once
- ◊ Primarily focuses on cash receipts and disbursements
- ◊ Suitable for small businesses with simple financial structures
- ◊ Tracks income and expenses, but not assets and liabilities comprehensively
- ◊ Uses a cash book similar to an expanded check register
- ◊ Advantages: simplicity, cost-effectiveness, time-saving
- ◊ Disadvantages: limited financial information, higher risk of errors

Double-Entry System:

- ◊ Records each transaction in at least two accounts
- ◊ Based on the principle that every transaction has equal and opposite effects
- ◊ Maintains the accounting equation: Assets = Liabilities + Equity
- ◊ More comprehensive and accurate than single-entry
- ◊ Provides detailed financial information and better error detection
- ◊ Suitable for larger businesses and complex financial structures
- ◊ Advantages: accuracy, comprehensive overview, better financial analysis
- ◊ Disadvantages: complexity, time-consuming, potentially costly for small businesses

Journalising:

- ◊ Process of recording transactions chronologically in a journal
- ◊ Each entry includes date, accounts affected, amounts, and a brief description (narration)
- ◊ Serves as the first point of entry for all financial transactions
- ◊ Follows specific rules for debiting and crediting accounts

Ledger:

- ◊ Contains individual accounts for assets, liabilities, income, and expenses
- ◊ Organizes financial information by account type
- ◊ Consists of two sides: debit (left) and credit (right)
- ◊ Ledger accounts are prepared based on journal entries through posting

Posting:

- ◊ Process of transferring journal entries to appropriate ledger accounts
- ◊ Ensures that all transactions are properly categorized and summarized
- ◊ Uses references (journal folios) to maintain a clear audit trail

Balancing Ledger Accounts:

- ◊ Process of equalising debit and credit sides of an account
- ◊ Determines the account's balance (debit or credit)
- ◊ Real and personal accounts are balanced and carried forward
- ◊ Nominal accounts are closed by transferring balances to Trading or Profit and Loss Account

Accounting Rules:

- ◊ Assets: Increase (Dr), Decrease (Cr)
- ◊ Liabilities: Increase (Cr), Decrease (Dr)
- ◊ Equity: Increase (Cr), Decrease (Dr)
- ◊ Revenue: Increase (Cr)
- ◊ Expenses: Increase (Dr)

Objective Questions

1. What is the primary focus of a single-entry accounting system?
2. In double-entry accounting, what must be equal for each transaction?
3. What is the process of transferring journal entries to ledger accounts called?
4. Which accounting system is more suitable for complex businesses?
5. What is the chronological log of financial entries called?
6. In a ledger, what does "c/d" stand for in "By Balance c/d"?
7. What type of accounts are closed at the end of the year by transferring balances to Trading or Profit and Loss Account?
8. What is the difference between the debit and credit sides of an account called?
9. Which side of the ledger account represents debits?
10. What does "J.F." stand for in a ledger account format?

11. What is the process of recording business transactions in a journal called?
12. In single-entry bookkeeping, what is the main record book called?
13. What accounting equation must remain balanced in double-entry accounting?
14. What is the brief explanation of a journal entry called?
15. What is the excess of the debit side over the credit side in an account called?

Answers

1. Income statement
2. Debits and credits
3. Posting
4. Double-entry
5. Journal
6. Carried down
7. Nominal accounts
8. Balance
9. Left side
10. Journal folio
11. Journalising
12. Cash book
13. Assets = Liabilities + Equity
14. Narration
15. Debit balance

Assignments

1. What is a Single-Entry System in accounting?
2. How does the Single-Entry System differ from the Double Entry System?
3. What are the advantages of using a single-entry system?

4. What are the limitations of the Single-Entry System?
5. Can the single-entry system be used for all types of businesses?
6. What is the difference between single-entry and double-entry accounting systems?
7. Why is the double-entry system considered more accurate than single-entry?
8. What are the main components of a journal entry?
9. How does balancing a ledger account work?
10. What are the advantages and disadvantages of the single-entry system?
11. How does the double-entry system help in detecting errors?
12. What is the importance of the narration in a journal entry?
13. How does the ledger complement the journal in accounting?
14. Why are some accounts balanced while others are closed at the end of an accounting period?
15. Journalise the following transactions and post it in appropriate ledgers

    March 1. Paid wages ₹1200

    March 3. Purchased Land ₹5000

    March 5. Sold goods ₹20,000

    March 7. Paid to Lal ₹3000

    March 10. Drew from Bank ₹30000
16. Prepare ledger account for the following

Year & Date	Particulars		L.F.	Amount Dr.	Amount Cr.
2021 March 1	Cash A/c	Dr.		30000	
	To Capital A/c				30000
2	Plant A/c	Dr.		25000	
	To Cash A/c				25000
3	Purchases A/c	Dr.		40000	
	To Joy A/c				40000
7	Cash A/c	Dr.		20000	
	To Sales A/c				20000

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Unit 3

Subsidiary Books

Learning Outcomes

After completing this unit, the learner will be able to;

- ◊ understand the concept and importance of subsidiary books
- ◊ identify and differentiate between various types of subsidiary books
- ◊ record transactions in different subsidiary books, particularly the cash book.

Prerequisites

Jeff and Susan had recently opened a small bakery in their neighbourhood. At first, managing their finances seemed simple enough. They diligently recorded every transaction in their trusty journal book, feeling proud of their meticulous bookkeeping. As their bakery gained popularity, however, they found themselves spending more and more time hunched over their journal. The sheer number of cash sales, ingredient purchases, and various other transactions was becoming overwhelming.

As the number of transactions increased, Jeff and Susan found it difficult to journalise them all in a single book. They realised most of their business transactions involved cash, purchases, and sales. To reduce workload, they decided to keep separate books or registers for each transaction type. In accounting, these are known as subsidiary books. Subsidiary books simplify recording daily transactions directly. They are also called day books or special journals and are a subdivision of the general journal. In this unit, we are going to learn the subsidiary books in detail.

Keywords

Subsidiary Books, Cash Book, Purchase Book, Sales Book, Bills Receivable, Bills Payable, Journal Proper

Discussion

1.3.1 Subsidiary Books

In large organisations, the volume of transactions makes it impractical to record each business event individually. However, failing to record even minor transactions could lead to significant problems, which businesses must avoid. This is where subsidiary books become important. Subsidiary books are systems for recording transactions of a similar nature. They are subdivisions of the main Journal. These books allow for efficient organisation and management of financial records.

Subsidiary books are books that record the transactions which are similar in nature in an orderly manner. They are also known as special journals or daybooks. In big business institutions, it is not easy to record all the transactions in one journal and post them into various accounts. So, for the easy and accurate recording of all the transactions, the journal is subdivided into many subsidiary books. For every type of transaction, there is a separate book.

1.3.1.1 Types of Subsidiary Books

Eight types of subsidiary books are used for recording different types of transactions. So, let us know the types.

1. Cash Book
2. Purchase Book
3. Sales Book
4. Purchase Return Book
5. Sales Return Book
6. Bills Receivable Book
7. Bills Payable Books
8. Journal Proper

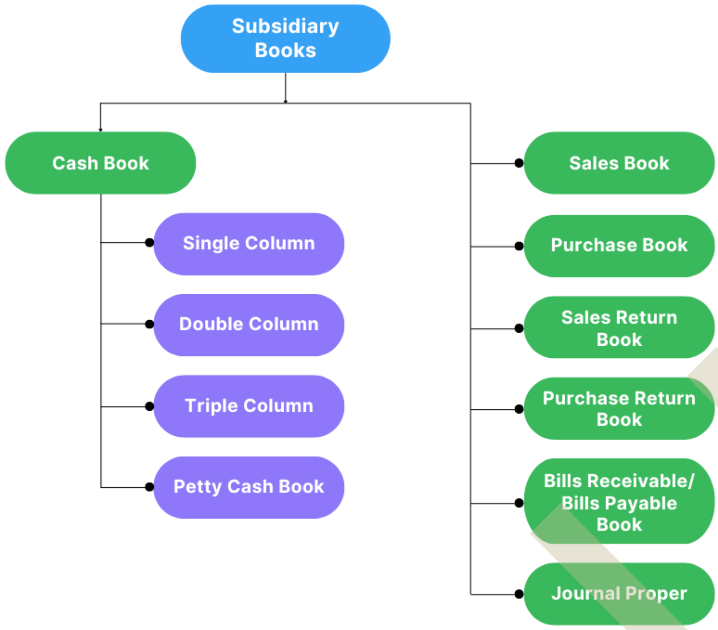

Fig 1.2.1 Types of Subsidiary Books

1. Cash Book

The first and most important subsidiary book is the cash book. It records all the transactions related to cash and bank receipts and payments. It includes sales, purchases, asset sales, expenditures, income, etc. conducted with cash or checks. Since transactions are recorded directly from source documents, the cash book is a book of original entries. The cash book lists transactions chronologically based on source documents, so it functions as a journal. However, the cash book is formatted like a ledger account, so it also serves as a ledger. In summary, the cash book acts as both a journal and a ledger for cash transactions.

Adhithy, the owner of Brew Haven, decides to implement a cash book to better manage her daily cash and bank transactions. Here is a simplified version of Brew Haven's cash book for a single day:

Brew Haven Coffee Shop - Cash Book

Date: June 1, 2024

Dr. Cr.

Receipt	Amount (₹)	Payments	Amount (₹)
To Opening Balance	500	By Coffee Bean Supplier	300
To Cash Sales	750	By Utility Bill	150
To Check from a catering job	200	By Staff Wages	400
To ATM Deposit	300	By Closing Balance	900
Total	**1750**	**Total**	**1750**

The cash book, as illustrated above, is the first and most important subsidiary book in accounting. It serves a crucial role in recording all transactions related to cash and bank receipts and payments. This includes various types of transactions such as:

i. Sales: In our example, Brew Haven recorded ₹750 in cash sales for the day.

ii. Purchases: The coffee shop paid ₹300 to their coffee bean supplier.

iii. Income: They received a ₹200 check from a catering job.

iv. Expenditures: Utility bills (₹150) and staff wages (₹400) were paid.

v. Bank transactions: An ATM deposit of ₹300 was made.

The cash book is considered a book of original entry because transactions are recorded directly from source documents such as receipts, invoices, and bank statements. In Brew Haven's case, Adhithy would enter each transaction based on the day's sales receipts, bills paid, and bank deposit slips.

The chronological listing of transactions based on these source documents means the cash book functions as a journal. However, its format resembles a ledger account with separate columns for receipts and payments, effectively serving as a ledger as well. This dual nature - acting as both a journal and a ledger - makes the cash book a unique and essential tool in accounting. It provides a clear, chronological record of all cash and bank transactions while also showing the running balance of cash on hand and in the bank.

By maintaining this cash book, Adhithy can easily track Brew Haven's daily cash flow, reconcile bank statements, and quickly access information about specific cash transactions without needing to search through a general journal or ledger.

Following are the different types of cash books;

Single-Column Cash Bsook

A single-column cash book is like a ledger account. It contains a debit side and a credit side. All Cash receipts are recorded on the debit side, and all the cash payments are recorded on the credit side of the cash book. The format of the Single Column Cash Book is given below.

Table 1.3.1
Cash book (Single Column)

Dr   Cr

Date	Particulars	L.F	Cash	Date	Particulars	L.F	Cash

Illustration:

From the following prepare a single column Cash Book in the books of James.

2020 Jan 1	Cash balance	₹20000
2	Deposited into bank	₹5000

4	Cash received from Manu, a customer deposited into the bank	₹5000
5	Paid salaries	₹2000
7	Bought a typewriter	₹2500
8	Cash withdrawn from bank	₹1200
10	Stationary purchased	₹150
11	Sold goods for cash and deposited into bank	₹7500

Solution:

Cash Book

Date	Particulars	L.F.	Amount	Date	Particulars	L.F	Amount
2020 Jan 1	To Balance b/d		20000	2020 Jan 2	By bank		5000
4	To Manu		5000	4	By bank		5000
8	To bank		1200	5	By Salary		2000
11	To sales		7500	7	By typewriter		2500
				10	By Stationary		150
				11	By Bank		7500
					By balance c/d		11550
			33700				33700

Double-Column Cash Book

Double-column Cash Book is the same as that of Single Column Cash Book; only an extra column of discount is added on both the debit and credit sides of the cash book. It records discounts allowed on the debit side and discounts received on the credit side of the cash book.

The format of the double-column cash book is given below.

Table 1.3.2

Cash book (Double Column)

Dr Cr

Date	Particulars	L.F	Discount Allowed	Cash	Date	Particulars	L.F	Discount Allowed	Cash

Illustration:

Prepare two-column Cash Books from the following information.

2020 April1	Started a business with cash	₹50000
2	Deposited into bank	₹20000
4	Purchased goods	₹4000
7	Sold goods to Sarasan	₹8000
9	Deposited into bank by Sarasan	₹7500
	Discount allowed to him	₹500
10	Purchased goods from Varghese	₹2000
12	Paid by cheque to Varghese	₹1900
	Discount allowed by him	₹100
13	Sold goods for cash	₹3000
18	Rents paid by cheque	₹400
26	Commission collected and credited by bank	₹600
30	Drew cash from the bank for office use	₹1200

Solution:

Dr. Cr.

Date	Particulars	L .F	Discount	Cash	Date	Particulars	L. F	Discount	Cash
2020					2020				
April 1	To Capital			50000	April 2	By Bank			20000
9	To Sarasan		500	7500	4	By Purchases			4000
12	To Bank			1900	9	By Bank			7500
13	To Sales			3000	12	By Varghese			1900
18	To Bank			400	18	By Rent		100	400
26	To Commission			600	26	By Bank			600
30	To Bank			1200	30	By Balance c/d			30200
			500	64600				100	64600

Working notes: Credit purchases and credit sales of goods are not recorded in the Cash Book.

Triple-column Cash Book

Triple Column Cash Book contains all the columns of a double-column cash book and also has an extra column for the bank. The format of the triple-column cash book is given below:

Table 1.3.2

Cash book (Triple Column)

Dr Cr

Date	Parti culars	L.F	Discount Allowed	Cash	Bank	Date	Parti culars	L.F	Discount Allowed	Cash	Bank

Illustrations:

Prepare a three-column Cash Book from the information given below. Mr. Johnson started a business on 1 April 2021 by introducing ₹5000. Out of this amount, ₹1000 is deposited into bank and a sum of ₹300 is paid for the furniture 2021.

April 4	Cash purchases	₹400
April 5	Sold goods for cheque and paid into bank on the same day	₹300
April 7	Purchases goods and cheque issued	₹195
April 7	Received Cheque from Kuttan ₹49 and discount allowed to him	₹1
April 8	Endorsed cheques received from Kuttan to Manu	
April 11	Cash sales	₹1400
April 13	Sold goods for cheque	₹200
April 14	Paid into bank, cheque	₹200
April 18	Deposited into bank	₹300
April 20	Drew from bank for personal use	₹100
April 22	Drew from bank for office use	₹50
April 24	Paid to Mathukutty by cheque	₹405
	Discount received from him	₹5
April 24	Interest allowed by the bank	₹16
April 25	Bank charges debited in the pass book	₹14
April 26	Received from Jayakrishnan	₹40
	Discount allowed to him	₹1
April 26	Paid for the personal expenses of the proprietor	₹10
April 27	Paid salaries by cheque	₹100
April 30	Ajith remitted to the bank directly	₹25
April 30	Received from Nadarajan, cheque and the same is sent to the bank for collection	₹409
	Discount allowed to him	₹6

Solution:

Cash Book

Dr. Cr.

Date	Particulars	L.F	Discount	Cash	Bank	Date	Particulars	L.F.	Dis coun	Cash	Bank
2021 April 1	Capital			5000		2021 April 1	Furniture			300	
1	Cash	C			1000	1	Bank	C		1000	
5	Sales				300	4	Purchases			400	
7	Kuttan		1	49		7	Purchases				195
11	Sales			1400		8	Manu			49	
13	Sales			200		14	Bank	C		200	
14	Cash	C			200	18	Bank	C		300	
18	Cash	C			300	20	Drawings				100
22	Bank	C		50		22	Cash	C			50
24	Interest				16	24	Mathukutty		5		405
26	Jayakrishnan		1	40		25	Bank charge				14
30	Ajith				25	26	Drawings			10	
30	Nadarajan		6		409	27	Salary				100
						30	Balance c/d			4480	1386
			8	6739	2250				5	6739	2250

1. Petty cash book

This journal keeps track of all daily miscellaneous cash payments for petty expenses. Cash transfers for very modest sums do occur occasionally. Petty cash transactions are a number of these transactions that happen in a single day. Stationery, mail, meals, and other expenses are a few examples of these types of transactions.

2. Sales Book

This book records all of the credit sales of products that the company makes throughout the accounting period. For recording sales deals, sales invoices serve as the foundation. Remember that asset credit transactions are recorded in the Journal Proper. It displays the names of those clients who are the business's debtors and to whom the goods are supplied on credit. The relevant sum must also be debited from the debtors' account. The format of Sales Book is given below.

Table 1.3.3
Sales Book

Date	Particulars	Outward Invoice No	L.F	Amount

Illustration:

The following transactions are to be used to prepare a sales book:

1. Sold goods to X for 600/- on 15th January 2024
2. A credit sale of 10 units to Y for 35/- per unit on 18th January 2024
3. Q bought units worth 500/- on credit on 22nd January 2024
4. Sold goods to Z for 750/- on 25th January 2024
5. A credit sale of 15 units to W for 40/- per unit on 28th January 2024

Solution:

Sales Book

Date	Particulars	Invoice Number	L.F	Amount
15/01/2024	Sold goods to X	INV-001		600/-
18/01/2024	A credit sale of 10 units to Y for 35/- per unit	INV-002		350/-
22/01/2024	Sold goods to Q on credit	INV-003		500/-
25/01/2024	Sold goods to Z	INV-004		750/-
28/01/2024	A credit sale of 15 units to W for 40/- per unit	INV-005		600/-
	Total			2800/-

3. Purchase Book

Book all credit purchases of the products utilised by the company during the accounting period are recorded in this book. Purchase invoices serve as the foundation for entering transactions into the buy book for this reason. However, credit purchases of the fixed assets are recorded in the journal proper.

Table 1.3.4
Purchase Book

Date	Particulars	Inward Invoice No	L.F	Amount

Illustration:

Prepare the Purchase book based on the transactions given below:

◊ August 20, 2022: XYZ Ltd. purchased office supplies from ABC Traders on credit. The order included stationery, printer cartridges, and filing cabinets, totalling ₹2,500. Invoice number INV-321 was issued for this transaction.

◊ August 25, 2022: XYZ Ltd. bought raw materials from DEF Suppliers on credit. The purchase included 500 kg of industrial-grade plastic pellets and 200 kg of metal sheets, amounting to ₹1,200. This was recorded on invoice

INV-322.

◊ August 28, 2022: XYZ Ltd. acquired packaging materials from GHI Wholesalers on credit. The order consisted of 1000 cardboard boxes, 500 rolls of packing tape, and 200 kg of bubble wrap, totalling ₹1,800. Invoice INV-323 was issued for this purchase.

◊ September 1, 2022: XYZ Ltd. purchased machinery parts from JKL Manufacturing on credit. The order included replacement gears, bearings, and motor components for their production line, amounting to ₹3,500. This was recorded on invoice INV-324.

◊ September 5, 2022: XYZ Ltd. bought computer equipment from MNO Electronics on credit. The purchase included 3 desktop computers, 2 laptops, and associated peripherals, totalling ₹2,700. Invoice INV-325 was issued for this transaction.

Purchase Book

Date	Particulars	Invoice Number	L.F	**Amount (₹)**
20/08/2022	ABC Traders - Office supplies	INV-321		2,500
25/08/2022	DEF Suppliers - Raw materials	INV-322		1,200
28/08/2022	GHI Wholesalers - Packaging materials	INV-323		1,800
01/09/2022	JKL Manufacturing - Machinery parts	INV-324		3,500
05/09/2022	MNO Electronics - Computer equipment	INV-325		2,700
	Total			11,700

4. Sales Return Book

This book, which is also known as the return inward book, keeps track of the products that customers return which the company originally sold. When a customer returns products to a business, the business (creditor or seller) issues the customer (the buyer or debtor) a credit note. The deal is entered into the sales return book using these notes as a foundation. As a result, the corresponding amount is credited to the debtor's account as a return inward, and the entire amount of the returned goods is posted to the sales return account's debit, column.

Table 1.3.5

Sales Return Book

Date	Particulars	Credit Note No	L.F	Details	Amount

Illustration:

The following are the transactions of Indira Electricals, Karunagappally. You are required to prepare sales returns book.

2020 September 3: Joy and Co returned 3 Table Lamps @ ₹50 per Lamp less 10% trade discount.

Sep 5: Jose Electricals 5 Table Fans @ ₹750 per Fan less 20% trade discount.

Sep 20: Kairali Electrical 5 Heaters @ ₹200 per Heater less 5% discount

Solution:

Sales Return Book

Sales Returns Book

Date	Particulars		L.F	Credit Note No.	Amount
2020 Sep 3	Joy and Company 3 Table Lamps @ ₹50 per Fan Less trade discount	 150 (15)			 135
5	Jose Electricals 5 table Fans @ ₹750 per Fan Less trade discount 20%	 3750 (750)			 3000
20	Kairali Electricals 5 Heaters @ ₹200 per Heater Less trade discount 5%	 1000 (50)			 950
					4085

5. Purchase Returns Book

It also goes by the name "Return Outward Book" and records all product returns the company makes to its vendors. The business (debtor or buyer) issues the debit note to the supplier upon receiving the returned products from the supplier (creditor or seller). Transactions are entered in the purchase return book using the debit note as a starting point. The appropriate amount is debited from the creditor's account for this reason. Additionally, the entire value of this book is added to the purchase return ledger's credit column. It should be remembered that returns for cash transactions need to be recorded in the cash book.

Table 1.3.6

Purchase Return Book

Date	Particulars	Debit Note No	L.F	Detais	Amount

Illustration:

MSM Book house Kollam gives the following information. You are required to prepare a purchase returns book

2021 March 1: Returned 10 accounting text books @ ₹50 per book less trade discount of @25% to Jeevan Books, Karunagappally.

March 10: Returned 50 books of drama to Universal Books Kollam @ ₹100 per book less 10% trade discount.

Solution:

Purchase Return Book

Date	Particulars	L.F.	Debit Note No	Amount
2020 March 1	**Jeevan Books** 10 Books on accounting @ ₹50 per book 500 Less Trade Discount 25% (125)			375
10	**Universal Books** 50 Drama Books @ ₹100 per book 5000 Less trade discount 10% (500)			4500 4875

6. Bills Receivable Book

The book kept to keep a record of bills drawn by the company is known as the bills receivable book. It is maintained when the business draws bills on behalf of its clients. The sum will be recorded as bills payable on the credit side of each party's account. At the end of the month, the total amount from the bills receivable book will be added to the debit side of the bills receivable account. It should be mentioned that the transactions related to dishonoured bills, endorsements, etc. are recorded in the journal rather than in this book. The format of Bills Receivable Book is given below.

Table 1.3.7

Bills Receivable Book

Date of Bill	Bill No	Acceptor	From	Terms	Due date	Amount

7. Bills Payable Book

All bills accepted by the company and drawn by the suppliers for payment later are recorded in the bills payable book. The sum will be recorded on the debit side of individual party's accounts. Additionally, at the end of the month, the total of these books is credited to the ledger account for bills payable.

Table 1.3.8

Bills Payable Book

Date of Bill	Bill No	Drawee	Payee	Terms	Date of Maturity	Amount

- ◊ Write the the entry for a bill payable dated 22-Jan- 2023, with bill number BP-001, where XYZ Corp is the drawee and ABC Supplies is the payee, with an amount of Rs 500 and a due date of 28-05-2023.
- ◊ Write the the entry for a bill payable dated 24-02-2023, with bill number BP-002, where ABC Supplies is the drawee and XYZ Supplies is the payee, with an amount of Rs 750 and a due date of 22-06-2023.
- ◊ Write the the entry for a bill payable dated 27-02-2023, with bill number BP-003, where DEF Corp is the drawee and ABC Supplies is the payee, with an amount of Rs 750 and a due date of 22-07-2023.

8. Journal Proper

There are certain transactions which may not come under any books of accounts such transactions are recorded in a specific book called Journal Proper. Journal proper include the journal entries like opening and closing entries, rectification and transfer entries, adjustment and transfer entries, entries for unpaid bills, miscellaneous entries, etc.

Recap

Subsidiary books are vital for managing the vast number of transactions in large organisations. These books allow companies to record transactions of a similar nature in an orderly manner, making it easier to organise and maintain accurate financial records. Each type of subsidiary book serves a specific purpose, helping businesses track their finances effectively.

Types of Subsidiary Books

- ◊ **Cash Book**
  - o Records all transactions related to cash and bank receipts and payments.
  - o It serves as both a journal and a ledger, with transactions recorded chronologically from source documents like receipts and bank statements.
- ◊ **Sales Book**
  - o Tracks all credit sales made by the company.
  - o Sales invoices serve as the foundation for entries, showing the names of customers (debtors) to whom goods are sold on credit.
- ◊ **Purchase Book**
  - o Records all credit purchases of goods used by the company.
  - o Purchase invoices are used to make entries in this book, which excludes credit purchases of fixed assets.
- ◊ **Sales Return Book**
  - o Also known as the return inward book, it tracks goods returned by customers.
  - o When goods are returned, a credit note is issued, and the amount is credited to the debtor's account.
- ◊ **Purchase Return Book**
  - o Known as the return outward book, it records goods returned by the company to its suppliers.
  - o Debit notes are issued for returns, and the amount is debited from the creditor's account.

- ◊ **Bills Receivable Book**
  - o Keeps a record of bills drawn by the company, showing amounts that will be received.
  - o The total is added to the debit side of the bills receivable account at the end of the month.
- ◊ **Bills Payable Book**
  - o Records all bills accepted by the company and drawn by suppliers for later payment.
  - o The total is credited to the ledger account for bills payable at the end of the month.
- ◊ **Journal Proper**
  - o Used for transactions that do not fit into other subsidiary books.
  - o Includes entries like opening and closing entries, adjustments, rectifications, and miscellaneous entries.

Objective Questions

1. How many main types of subsidiary books are there?
2. What type of book records all cash and bank transactions?
3. Which book records credit sales of products?
4. What is another name for the Sales Return Book?
5. What document is used as a basis for recording transactions in the purchase book?
6. What type of book records bills drawn by the company?
7. Which book records miscellaneous entries that do not fit in other books?
8. What is issued when a customer returns goods to a business?
9. What is issued when a business returns goods to a supplier?
10. How many columns does a single-column cash book have?
11. What type of cash book is used for recording daily miscellaneous expenses?

Answers

1. Eight
2. Cash book
3. Sales book
4. Return inward book
5. Purchase invoices
6. Bills receivable book
7. Journal proper
8. Credit note
9. Debit note
10. Two
11. Petty cash book

Assignments

1. Why are subsidiary books important in large organisations?
2. Explain the dual nature of the cash book in accounting.
3. What types of transactions are typically recorded in the Journal Proper?
4. How does the Purchase Return Book differ from the Sales Return Book?
5. Describe the purpose and contents of a Bills Payable Book.
6. If Brew Haven's cash book shows an opening balance of ₹500, cash sales of ₹750, and payments of ₹850, what is the closing balance?
7. A company's purchase book shows total credit purchases of ₹10,000 for the month. If the purchase returns book shows returns of ₹1,500, what is the net purchase amount?
8. Prepare a single-column cash book based on the transactions given below:

Transactions for Styles Boutique:

June 1, 2024: Started business with cash ₹5,000

June 3, 2024: Purchased inventory for ₹1,500 cash

June 5, 2024: Sold merchandise for ₹800 cash

June 7, 2024: Paid rent ₹600

June 10, 2024: Received ₹300 from a customer for a previous credit sale

June 12, 2024: Purchased office supplies for ₹150

June 15, 2024: Sold merchandise for ₹1,200 cash

June 18, 2024: Paid salaries ₹800

June 20, 2024: Received ₹500 commission for hosting a fashion show

June 25, 2024: Paid utility bill ₹200

June 28, 2024: Sold merchandise for ₹950 cash

June 30, 2024: Withdrew ₹300 for personal use

9. If a triple-column cash book shows cash receipts of ₹5,000, bank deposits of ₹3,000, and discounts allowed of ₹200, what is the total amount to be debited?

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Unit 4

Trial Balance and Final Accounts

Learning Outcomes

After Completing this unit, the learner will be able to:

- ◊ understand and prepare Trial Balance
- ◊ identify different types of accounting errors and learn methods for rectifying them.
- ◊ realise the meaning and purpose of financial statements
- ◊ prepare trading accounts and Profit and Loss Accounts
- ◊ describe assets and liabilities and learn to prepare a Balance Sheet

Prerequisites

Meet Priyanka, a college student who decided to open a small campus cafe called "Brews & Bites" during her summer break. She was excited about her new venture but quickly realised that running a business involved more than just serving coffee and snacks. As the summer progressed, Priyanka diligently recorded every transaction in her notebook. She wrote down each coffee sold, every bagel purchased, and all the money spent on supplies. By the end of August, her notebook was filled with entries, but she felt overwhelmed. How could she make sense of all these numbers? More importantly, how could she tell if her cafe was actually making money? That is when Priyanka remembered her accounting class and two important concepts: the trial balance and final accounts.

First, Priyanka tackled the trial balance. She carefully listed all her accounts - cash, inventory, sales, expenses - and totalled up the debits and credits for each. This process helped her catch a few mistakes she had made in her original entries.

When the debit and credit columns finally matched, Priyanka felt a sense of relief. The trial balance had helped her organize her financial information and ensure its basic accuracy. But Priyanka still did not know if her cafe was profitable. That is where the final accounts came in. She prepared a Trading Account to calculate her gross profit, then a Profit and Loss Account to determine her net profit. Finally, she created a Balance Sheet to get a snapshot of what her business owned and owed at the end of the summer.

Through these final accounts, Priyanka discovered that "Brews & Bites" had indeed turned a small profit. She could see which products were selling well and which expenses were eating into her earnings. The Balance Sheet showed her that while she had some cash in hand, she also owed money to a supplier for her last coffee bean order. This financial journey taught Priyanka the value of proper accounting. The trial balance had helped her organise and verify her financial data, while the final accounts gave her insights into her business's performance and financial position.

As Priyanka prepared to return to her classes, she felt more confident about her business skills. She knew that these accounting tools would be essential if she decided to reopen "Brews & Bites" next summer or start any business in the future.

In this unit let us learn the Trial Balance, Profit & Loss Account and Balance Sheet.

Keywords

Trial Balance, Trading Account, Profit & Loss Account, Balance Sheet

Discussion

1.4.1 Trial Balance

Picture a meticulous accountant at her desk surrounded by ledgers and calculators. She is piecing together a financial puzzle, ensuring every number finds its rightful place. This is the essence of preparing a trial balance - a critical step in the accounting process that brings order to the chaos of financial transactions.

The trial balance is like a financial scale, carefully balancing debits on one side and credits on the other. It is a snapshot of a company's financial health, capturing the essence of countless transactions in a single, organised document. At its core, a trial balance is a bookkeeping worksheet that compiles the balances of all ledgers into two columns: debits and credits. These columns should have equal totals, reflecting the fundamental principle of double-entry accounting where every transaction affects at least two accounts.

Companies typically prepare a trial balance at the end of each reporting period, which could be monthly, quarterly, or annually. This regular check-up serves a crucial purpose: to ensure the mathematical accuracy of the bookkeeping system. While it is not a full audit, the trial balance acts as a first line of defence against errors. It is often the initial step in an audit procedure, allowing auditors to verify the basic mathematical integrity of the books before going into more complex analyses.

Definition:

A trial balance is a financial statement that lists the balances of all general ledger accounts, both debits and credits, at a specific point in time. Its primary purpose is to confirm that the total of all debit balances equals the total of all credit balances, thereby verifying the mathematical accuracy of the bookkeeping records. This financial tool serves as a bridge between day-to-day bookkeeping and the preparation of more formal financial statements, providing a foundation for accurate financial reporting and analysis.

Following is the general format for preparing Trial Balance. Trial Balance is prepared at the end of a period on a specific date. Therefore, the caption of the Trial Balance should be mentioned like 'Trial Balance of XYZ. Ltd as on 31 March 2022'.

Table 1.4.1

Format of Trial Balance

Sl. No.	Name of Account	Dr. Amount	Cr. Amount

1.4.1.1 Steps in Preparation of Trial Balance

The steps to prepare Trial Balance using the most popular method, the balance method, are as follows;

- ◊ Step 1: Determine the balances of each ledger account, including cash book.
- ◊ Step 2: Write the name of accounts in the Particulars column. Enter the amounts (closing balance) of balance in the debit column if the account has debit balance similarly the closing balance of account having credit balance should be entered in credit side.
- ◊ Step 3: In the Ledger Folio column, enter the page number of the ledger from which the balance is derived.
- ◊ Step 4: Add the columns for debit and credit. It has to be fair. Find the errors and make the Trial Balance accord if they are not equal.

Illustration:

From the following details for ABC Ltd. for the year ended on 31/02/2021 prepare Trial Balance.

Cash in hand	57000	Bad debt	3800
Debtors	28000	Drawings	3000
General Expenses	2500	Plant and Machinery	25000
Furniture	15000	Purchases	42000
Rent	1500	Sales Returns	4500
Rate	2000	Capital	80000
Sales	52200	Interest received	2100
Dividend Received	5000	Purchased Returns	25000
Creditors	45000	Opening Stock	25000

Solution:

Trial Balance of ABC Ltd. as on 31/03/2021

Sl.No.	Name of Account	Dr. Amount (₹)	Cr. Amount (₹)
1	Opening Stock	25000	
2	Furniture	15000	
3	Drawings	3000	
4	Plant and Machinery	25000	
5	Purchases	42000	
6	Sales Returns	4500	
7	Rent	1500	
8	Rate	2000	
9	Bad debts	3800	
10	Debtors	28000	
11	Cash in Hand	57000	
12	General Expenses	2500	
13	Capital		80000
14	Interested received		2100
15	Creditors		45000
16	Sales		52200
17	Purchases Returns		25000
18	Dividend Received		5000
		209300	209300

1.4.1.2 Accounting Errors

Accounting errors are mistakes that can happen when recording financial transactions. Some errors will make the trial balance debits and credits unequal. But other errors may not affect the agreement of the trial balance. If errors are not caught, they may or may not show up in an unbalanced trial balance. However, all errors reduce the accuracy of the financial records, even if the trial balance still balances. Inaccurate information leads to poor financial analysis and decisions, regardless of the trial balance outcome. So identifying and fixing errors is key for correct accounting and clear financial reporting, not just balancing the trial balance. When an unbalanced trial balance signals a definite error, a balanced trial balance does not guarantee the accounts are error-free. Additional checks are still needed because any mistakes distort the data and harm decision-making.

Accounting errors can be classified as:

Fig 1.4.1 Accounting Errors

a. Error of Omission

An error of omission occurs when transactions are completely or partially left out of the accounting records.

Complete Omission: Imagine Galaxy Ltd is a shoe-making company, receives a ₹1,000 payment from a customer, but the accountant forgets to record it entirely. This complete omission will not affect the trial balance, as nothing was recorded.

It should have been Debit: Cash ₹1,000 and Credit: Accounts Receivable ₹1,000

Partial Omission: Galaxy Ltd buys office supplies for ₹500 on credit, but only the credit to Accounts Payable is recorded. This partial omission will cause the trial balance to be out of balance by ₹500.

Incorrect entry: Credit: Accounts Payable ₹500

The correct entry should be Debit: Office Supplies Expense ₹500 and Credit: Accounts Payable ₹500

b. Error of Commission

Errors of commission occur when transactions are recorded incorrectly.

Example: Galaxy Ltd sells goods worth ₹2,000 on credit but records it as a cash sale.

Incorrect entry: Debit: Cash ₹2,000 and Credit: Sales ₹2,000

Correct entry should be Debit: Accounts Receivable ₹2,000 and Credit: Sales ₹2,000

This error will not affect the trial balance totals, but it misrepresents the company's cash position and accounts receivable.

c. Compensating Error

Compensating errors occur when two mistakes balance each other out.

Example: Galaxy Ltd makes two errors:

1. Fails to record a ₹300 discount given to a customer
2. Forgets to log ₹300 in rental income

It should have been recorded Debit: Sales Discounts ₹300 Credit: Accounts Receivable ₹300 and Debit: Cash ₹300 Credit: Rental Income ₹300.

These errors compensate each other, leaving the trial balance in agreement. However, both sales discounts and rental income are understated by ₹300.

d. Error of principle

Errors of principle occur when transactions violate accounting principles or standards.

Example: Galaxy Ltd purchases a delivery van for ₹25,000 but records it as an expense instead of an asset.

Incorrect entry is Debit: Vehicle Expense ₹25,000 and Credit: Cash ₹25,000

Correct entry should be Debit: Vehicles (Asset) ₹25,000 and Credit: Cash ₹25,000

This error does not affect the trial balance, but it significantly misrepresents the company's financial position by understating assets and overstating expenses.

e. Duplication Error

Duplicate Error: Galaxy Ltd records a ₹1,500 utility payment twice.

The trial balance will still match, but expenses are overstated by ₹1,500 and cash is understated by ₹1,500.

In all these cases, while the trial balance might still agree, the financial statements would be inaccurate. This highlights the importance of thorough reviews and checks beyond just balancing the books to ensure accurate financial reporting.

1.4.1.3 Rectification of Errors in Accounting

When an error is identified in accounting records, it can be rectified in two ways, depending on when it is discovered:

a. Rectification of errors before preparing the Trial Balance

When an error is found before the Trial Balance is prepared, the method of correction depends on the nature of the error:

i. One-sided errors: These affect only one side (debit or credit) of an account and do not require a journal entry for correction.

Example: The rent expense of ₹500 was recorded as ₹5,000 in the Rent Expense account.

Correction: Simply change the figure in the Rent Expense account from ₹5,000 to ₹500.

ii. Two-sided errors: These affect two accounts in opposite directions and are corrected by passing journal entries.

Example: A company paid ₹2,000 for building repairs but incorrectly debited the Building account instead of the Repairs and Maintenance account.

Incorrect entry: Debit: Building ₹2,000 and Credit: Cash ₹2,000

Correction entry: Debit: Repairs and Maintenance ₹2,000 and Credit: Building ₹2,000

b. Rectification of errors after the preparation of the Trial Balance

If an error is discovered after the Trial Balance is prepared and it does not balance, the difference is temporarily placed in a Suspense Account to make the Trial Balance.

Example: The Trial Balance shows a ₹1,500 difference between debits and credits. The accountant creates a Suspense Account to balance it:

If debits are short: Debit: Suspense Account ₹1,500 and Credit: [Balance sheet total] ₹1,500

If credits are short: Debit: [Balance sheet total] ₹1,500 and Credit: Suspense Account ₹1,500

Later, when the specific error is found, it is corrected using the Suspense Account.

For instance: It was discovered that a ₹1,500 sale was recorded as ₹150 in the Sales account.

Correction entry: Debit: Suspense Account ₹1,350 and Credit: Sales Account ₹1,350

This entry corrects the Sales account and eliminates the Suspense Account balance.

In both scenarios - before or after the Trial Balance - the goal is to ensure all transactions are accurately recorded and the books are balanced. The key difference is the use of the Suspense Account as a temporary measure when errors are discovered after the Trial Balance has been prepared.

1.4.2 Final Accounts: Trading, Profit & Loss Account, Balance Sheet

Final accounts are financial statements prepared at the end of an accounting period to summarise a company's financial position and performance. They typically include:

1. Income Statement (Trading, Profit and Loss Account): Shows revenues, expenses, and profit/loss for the period.
2. Balance Sheet: Presents assets, liabilities, and owner's equity at a specific date.
3. Cash Flow Statement: Illustrates cash inflows and outflows from operating, investing, and financing activities.
4. Statement of Changes in Equity: Reflects changes in the company's equity over the period.

These accounts provide a comprehensive view of a business's financial health and are used by stakeholders like investors, creditors, and management for decision-making. They are also often required for tax purposes and regulatory compliance.

1.4.2.1 Trading Account

Raj, a poultry farmer who buys high-quality chicks from trusted suppliers. He does not immediately resell these chicks; instead, he invests time and resources to raise them. Raj provides proper housing, feeds them a balanced diet, ensures they receive necessary vaccinations, and carefully monitors their growth and health. Once the chickens are fully grown, he sells them to various customers such as local markets, restaurants, and individual consumers. This cycle of buying chicks, raising them, and selling grown chickens represents a fundamental economic activity: trade.

Raj's poultry business illustrates the concept of trade in action. At its core, trade is the process of exchanging goods and services between parties. It typically involves buying (or producing) goods or services, potentially adding value through processing, packaging, or service delivery, and then selling these goods or services to customers. In Raj's case, he buys chicks, adds value by raising them to maturity, and then sells the grown chickens. This exemplifies how trade can be defined as the economic exchange of goods and services, often with an intermediary step of value addition. Trade can occur at various scales, from local businesses like Raj's to national and international exchanges, serving as a fundamental driver of economic activity by allowing specialisation, efficient resource allocation, and the satisfaction of diverse consumer needs.

A Trading Account is a financial statement prepared by businesses involved in buying and selling goods. It is typically the first section of the Profit and Loss Account (Income Statement) for a trading business. The main purpose of a Trading Account is to determine the gross profit or gross loss from trading activities for a specific accounting period.

To illustrate, let us consider a small retail store that buys electronics from wholesalers and sells them to consumers. The store's Trading Account would show:

1. The total sales of electronics (revenue)
2. The cost of electronics purchased (purchases)
3. Any changes in inventory (opening and closing stock)
4. Direct expenses related to buying and selling these goods (like freight charges)

The Trading Account calculates the difference between the selling price of goods and their cost, including direct expenses. This difference is the gross profit (or loss if costs exceed sales).

Key components of a Trading Account include:

1. **Sales:** Sales revenue is the lifeblood of any trading business, representing the total amount earned from selling goods or services during an accounting period. For a poultry farmer like Raj, this would be the sum of all money received from selling mature chickens, whether paid in cash or on credit. It's important to note that any sales returns or discounts would typically be deducted to arrive at the net sales figure, giving a true picture of the actual revenue generated.
2. **Purchases:** Purchases form the foundation of a trading business, referring to the cost of goods bought for resale or raw materials acquired for production. In Raj's case, this would primarily be the expense of buying chicks from suppliers. This figure includes all purchases, regardless of whether they were paid for immediately or bought on credit. To get an accurate representation of the net purchases, any purchase returns or discounts received would be deducted from the total.
3. **Opening and closing stock:** Opening and closing stock are crucial elements in understanding the flow of inventory through a business. Opening stock represents the value of inventory at the beginning of the accounting period, while closing stock is the value at the end. For Raj's poultry farm, the opening stock would be the value of chickens at various growth stages he had at the start of the year, and the closing stock would be the value of chickens he has at the end. The difference between these figures helps adjust the cost of goods sold, providing a more accurate picture of the business's trading activities over the period.
4. **Direct expenses** (like carriage inward, customs duty, etc.): Direct expenses are costs that can be directly attributed to the purchase, production, or sale of goods. In Raj's poultry business, these might include feed costs, vaccination expenses, labor costs for direct care of the chickens, and utilities like electricity and water used specifically in raising the chickens. In other types of businesses, direct expenses could include things like carriage inward (the cost of transporting purchased goods to the business premises), customs duty on imported goods, factory rent for manufacturing businesses, or packaging materials used to prepare goods for sale. These expenses are crucial in determining the true cost of producing or acquiring the goods for sale.

The format typically shows sales on the credit side, while purchases, direct expenses, and opening stock appear on the debit side. The closing stock is added to the credit side.

By preparing a Trading Account, businesses can:

- ◊ Determine their gross profit or loss
- ◊ Calculate the cost of goods sold
- ◊ Assess the efficiency of their buying and selling operations
- ◊ Make informed decisions about pricing and inventory management

In essence, a Trading Account provides a focused view of a business's core trading activities, serving as a crucial tool for financial analysis and decision-making in merchandising businesses.

Table 1.4.2
Format of Trading Account

Dr   Cr

Particulars		Amount	Particulars		Amount
Opening stock		xxx	Sales	xxx	
Purchases	xxx		Less: Sales returns	xx	xxx
Less: Purchase returns	xx	xxx	Closing stock		xxx
Direct expenses					
Carriage/Cartage/Freight in inwards		xxx			
Wages/Wages and Salaries		xxx			
Customs/Dock/Octroi		xxx			
Royalty		xxx			
Gas/Electricity/Water/Fuel/Power/ Factory rent		xxx			
To Gross profit c/d		xxx	By Gross loss c/d		xxx
Total		xxxx	Total		xxxx

Illustration:

Raj operates a poultry farm. The following information relates to his business for the year ended December 31, 2023:

1. Value of chicks at the beginning of the year: ₹5,000
2. Purchases of new chicks during the year: ₹50,000
3. Sales of mature chickens: ₹150,000
4. Value of chickens in various growth stages at year-end: ₹10,000
5. Expenses incurred during the year: a. Feed: ₹30,000 b. Vaccination: ₹5,000 c. Labor for chicken care: ₹15,000 d. Electricity and Water: ₹3,000

Required: Prepare a Trading Account for Raj's Poultry Farm for the year ended December 31, 2023. Calculate the Gross Profit for the year.

Note: Present your answer in a properly formatted Trading Account, clearly showing all relevant items on the appropriate sides (Debit and Credit). Round all figures to the nearest rupee.

Solution:

Trading Account for the year ended December 31, 2023

Dr. Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
Opening Stock (Chicks)	5,000	Sales (Mature Chickens)	150,000
Purchases (New Chicks)	50,000	Closing Stock (Chickens in various growth stages)	10,000
Direct Expenses:	30,000		
Feed	5,000		
Vaccination	15,000		
Labour (for care)	3,000		
Electricity & Water	52,000		
Gross Profit (Transferred to P&L A/c)			
	160,000		**1,60,000**

1.4.2.2 Profit & Loss Account

Every business would like to know the result of the business operations conducted by them during a particular period. What do you mean by this result? Result means the amount of final profit or loss that the business generates for its owner from its operations. For instance, Raj can determine the result of buying and selling activities of his farm during the previous year, i.e., gross profit or gross loss from the Trading Account. So, do you think Raj should be content with this information as to the final profit and loss situation of the farm? The answer is no, because the Trading account only discusses the performance of the company with regard to the direct expenses and direct income. There are some other factors like indirect expenses and indirect income that need to be addressed along with their direct counterparts while determining the final profit or loss position of the company. This final profit or loss obtained is called the net profit or net loss of the company which the owner must bear. This information as to the net profit and net loss is provided by the Profit and Loss Account.

Let us take the case of Raj's poultry farm. Its core business is egg and meat production and sales. Conducting this business results in direct expenses and direct income. Apart from that, Raj will have to suffer some other expenses like insuring chickens against diseases and the farm against natural disasters and accidents, telephone charges for the farm's purpose, salaries paid for the farm's security guard, advertisement and promotional expenses of the farm and expenses for transportation of eggs to various shops for selling. These complimentary expenses are considered indirect expenses. These indirect expenses can be generally characterised as:

a. Office and administrative expenses, such as telephone, postage, office rent, salaries of office staff, legal charges, audit fees and insurance.

b. Selling and distribution expenses, such as advertisement, commission, carriage outwards (transportation cost for distributing the final products to customers) and packing charges.

c. Miscellaneous expenses like repairs, depreciation, interest on loan, bad debts and provision for bad debt.

The farm also receives revenue from certain other sources as well. For your understanding let us consider following instances.

a. A portion of the farm's building is given on rent to Raj's friend for running a shop. In this case the farm will receive revenue in the form of rent.

b. Raj had purchased the feeding material on credit. Now when Raj went to pay this amount, the supplier provides him some discount. In some cases, discounts are allowed by the creditors while settling the account. This discount is also revenue for the farm.

c. Using the revenue generated from the farm's operations, Raj made certain small investments in banks and other companies. Interest and dividends received from these investments are also revenue for the farm.

These incomes are not obtained from the main business of the farm but it also contributes to the profit of the farm. These incomes can be considered Indirect Income. Indirect Income is the income received by the company from activities other than sales of its final goods and services. Since it is generated from activities other than the operating activities of the company, it is also known as non-operating income. Some common specimens of indirect income are commission received, rent received, discount received, dividend received, etc.. Profit and Loss Account is prepared to include these factors as well and determine the net profit or net loss of the company. Profit and Loss Account is a nominal account that is prepared by incorporating the indirect expenses incurred and indirect income earned by a business, along with its gross profit or gross loss in order to ascertain the net profit or net loss of the business.

Preparation of Profit & Loss Account

Profit and Loss Account is prepared as a continuation of Trading Account. Since Profit and Loss Account is a nominal account the accounting rule of debit and credit is applicable here. "Debit all expenses and losses Credit all income and gains" This means all indirect expenses and losses will be written on the debit side and all indirect income and gains will be written on the credit side of the Profit and Loss Account.

Items to be written on the debit side of Profit and Loss Account.

a. Gross Loss – If Trading Account discloses gross loss for the business, then it should be brought down to the debit side of Profit and Loss Account.

b. Office and Administrative expenses

c. Selling and Distribution expenses

d. Miscellaneous expenses

Items to be written on the credit side of Profit and Loss Account:

a. Gross Profit – If the company earns gross profit as per Trading Account, then it will be brought down to the credit side of Profit and Loss Account.

b. Indirect Income and Gains.

Now, on balancing the Profit and Loss Account, if total credit side value exceeds the total debit side value, then the balance amount will be written on the debit side and it is termed as net profit. If the total debit side value exceeds the total credit side value, then the balance amount will be written on the credit side and it is called net loss. The net profit and net loss are the results of a business's operations for a particular period of time. So, the net profit will be added to the capital of the owner and if it is net loss then it will be reduced from the owner's capital.

Table 1.4.3
Format of Profit and Loss Account

Particulars	Amount	Particulars	Amount
To Gross loss b/d (if any)	xxx	By Gross Profit b/d (if any)	xxx
Salaries	xxx	Interest Received	xxx
Printing and Stationaries	xxx	Dividend Received	xxx
Rent, Rates and Taxes	xxx	Rent Received	xxx
Audit Fees	xxx	Commission Received	xxx
Postage and Telegram	xxx	Discount Received	xxx
Legal Charges	xxx	Any other Income	xxx
Insurance	xxx		
Telephone charges	xxx		
Bank Charges	xxx		
Advertisements	xxx		
Commission paid	xxx		
Deprecation	xxx		
Charity	xxx		
Carriage Outwards	xxx		
Travelling Expenses	xxx		
Discount Allowed	xxx		
Bad debts	xxx		
Provision for doubtful debts	xxx		
Any other expenses	xxx		
Net Profit (f any)	xxx	Not Loss (if any)	xxx
Total	xxx		xxx

Note:

a. Net profit /Net loss must be transferred to Capital account.

b. Personal expenses of the owner like income tax, and domestic and household expenses will not be written in the Profit and Loss Account.

c. From the Trial Balance given in the question, only indirect expenses and indirect incomes are entered in Profit and Loss Account.

Apprentice Premium is an indirect income received by the company for training someone. Now let us solve a simple problem that involves the preparation of Trading and Profit and Loss Account

Illustration:

From the following information on Raj's farm, prepare Trading and Profit and Loss Account for the year ended on 31 December 2020.

Particulars	Amount	Particulars	Amount
Sales	25000	Factory Expenses	200
Purchase	4000	Repairs	190
Capital	6200	Stock (01-01-2020)	1600
Salary	750	Rent	250
Machinery	15000	Drawings	1700
Furniture	3600	Advertisement	300
Sundry creditors	4600	Carriage in	300
Wages	100	Cash at bank	2600
Sundry Debtors	8560	Bills Payable	3350

The closing stock was ₹250.

Trading and Profit and Loss Account for the year ended 31 December 2020

Particulars	Amount	Particulars	Amount
Opening stock	1600	Sales	25000
Purchases	4000		
		Closing stock	250
Direct expenses			
Carriage inwards	300		
Wages	100		
Factory expenses	200		
To gross profit c/d	19050		
	25,250		25,250

		By gross profit b/d	19050
Salary	750		
Repairs	190		
Rent	250		
Advertisement	300		
Net profit transferred to capital account	17560		
	19050		19050

1.4.2.3 Balance Sheet

Imagine you own a small bakery. At the end of the year, you take stock of your business as given below:

Assets:

- ◊ Cash in bank: ₹10,000
- ◊ Baking equipment: ₹15,000
- ◊ Inventory (flour, sugar, etc.): ₹5,000 Total Assets: ₹30,000

Liabilities:

- ◊ Bank loan: ₹8,000
- ◊ Accounts payable (money owed to suppliers): ₹2,000 Total Liabilities: ₹10,000

Owner's Equity:

- ◊ Your initial investment: ₹15,000
- ◊ Retained earnings: ₹5,000 Total Owner's Equity: ₹20,000

This snapshot of your bakery's financial position is essentially a balance sheet. Now, let's define the concept:

A balance sheet is a financial statement that provides a summary of a company's or individual's financial position at a specific point in time. It is based on the accounting equation:

Assets = Liabilities + Owner's Equity

The balance sheet is divided into two main sections:

1. Assets: What the company owns or is owed
2. Liabilities and Owner's Equity: How the assets are financed

Assets represent resources with economic value that a company controls. Liabilities are the company's financial obligations or debts. Owner's equity represents the owner's investment in the business plus retained earnings. The balance sheet "balances" because the total assets must always equal the sum of liabilities and owner's equity. This provides a clear picture of a company's financial health, showing what it owns, what it owes, and the value belonging to the owners.

Balance Sheet always depicts the financial position of the business. The financial strength of a business depends on the means by which its assets are purchased, i.e., what percent of liabilities and capital are used for purchasing assets. Imparting of information about financial strength of the company is essential for the existing and potential shareholders. The information as to the position of the company in terms of assets, liabilities and capital is provided by the Balance Sheet. Since it reveals the financial position of the company, it is also known 'Position Statement'.

Items to be entered in the Balance Sheet

A. Assets

Sarah, a young entrepreneur who loves baking. She decides to start a small bakery business from her home. To begin, she uses her savings to buy a high-quality oven for ₹2,000. This oven allows her to bake delicious cakes and cookies that she sells to her neighbours and local cafes. As her business grows, Sarah realises she needs more equipment. She purchases a professional mixer for ₹500 and a refrigerator for ₹1,000 to store her ingredients and finished products. She also creates a unique recipe for a special chocolate cake that becomes very popular.

Each of these items - the oven, mixer, refrigerator, and even the recipe - are assets for Sarah's bakery business. They are things she owns that have value and help her generate income. The equipment allows her to produce more baked goods efficiently, while her recipe gives her a competitive edge in the market.

Now, let us define what an asset is:

An asset is anything of value that a person or business owns or controls, which can be used to produce positive economic value. Assets can be tangible (physical items like equipment) or intangible (non-physical items like recipes or brand reputation).

In Sarah's case: The oven, mixer, and refrigerator are tangible assets. Her special recipe is an intangible asset. These assets are valuable because they help Sarah's business operate and grow, ultimately leading to profits. Understanding assets is crucial in business and personal finance, as they form the foundation of wealth and economic potential.

◊ **Fixed Assets:**

Let us consider a farm, it acquires certain resources like land, building, machinery, furniture etc. to assist it in its operations and to be used for a long time. The farm does not intend to sell these items any time soon. These resources owned by the farm are called fixed assets of the farm. Fixed assets are acquired by the business for long-term use and it is not meant for immediate resale. Some of the common fixed assets associated with any business are land, building, furniture, plant, machinery, etc.

◊ **Current Assets:**

The farm will have certain resources available that can be easily converted to cash within one year. These resources are called current assets of the farm. Current assets are assets that are in the form of cash or that can be easily converted to cash within short period. Current Assets include:

a. **Cash in Hand** – Cash available with the farm at a particular date. This cash might be obtained from various sources, such as owner's capital, loan taken from bank, income from sale of chicken eggs etc. Cash in hand is the total amount of accessible cash available with the business at their disposal.

b. **Cash at Bank** – It is the amount of money held at the bank by the farm in the form of current account (cash can be withdrawn anytime) or other deposit accounts (gets interest for the deposited cash and cash can be withdrawn easily). The farm will be able to withdraw this money use it for their requirements as and when required. So, cash at bank is the amount of money kept at the bank by a business which is available at their disposal.

c. **Bills Receivable** – One hotel has purchased large quantities of chicken and eggs from the farm without making immediate cash payments. The farm needs some kind proof for this transaction. Raj for the safety of the farm, prepares a bill stating the amount and the time by which the hotel should pay back the specified cash to the farm. This bill should be accepted by the hotel for the purchase to take place. This bill is known as bills receivable. Normally, the payment period stated in the bills receivable is less than a year thereby making it a current asset. So, bills receivable is a legal agreement stating that a customer agrees to make a full payment of what they owe to a company at a future date.

d. **Sundry Debtors** – Some individuals residing near the farm used to purchase eggs and meat from the farm on credit. They used to pay the money to the farm usually during the first week of every month when they get their salaries. The farm does not raise the bills receivable on their account as the amount to be paid back is less and because of the faith the farm has over them. But the farm keeps a record of these individuals and the amount they owe to the farm. The farm groups all these individuals under the common heading as Sundry debtors. Sundry debtors in general are persons who receive goods from a business on credit and are liable to pay back the amount in the immediate future.

e. **Short Term Investments** – From the profit the farm generates, the owner decided to make some investments in treasury bills issued by the government. For the money invested the government will provide Treasury bill as proof to the owner. The Treasury bill also specifies the interest rate, the government agrees to pay to owner's farm for the invested money. Usually, the maturity period of Treasury bills is less than a year, which means owner will get back the originally invested amount within this period. This Treasury bill is a form of short-term investment. Short term investments in general are temporary investments that can be converted to cash within one year period.

f. **Closing Stock** – The farm might be having some newly purchased chickens, some half grown chickens, some fully grown chickens, eggs, etc. that are unsold at the end of the accounting period. The value of these semi-finished and finished products available with the farm at the end of the accounting period is called closing stock of the farm.

g. **Prepaid Expense** – Prepaid expenses mean paying in advance for things you will need later. For Raj's farm, they may pay in advance for things like chicken feed or medicine. The farm should record these payments as current assets on their books and slowly use them up over time. It helps the farm plan and make sure they have what they need.

h. **Outstanding or Accrued Income** – When the farm receives revenue from renting out its outhouse, but the tenant requests extra time to make payment, this is known as outstanding or accumulated income. Rent that was meant to be paid this month is now paid the next month. The farm has earned the money, but it still has not been received.

◊ **Intangible Assets**

The farm has earned a great reputation in the community. People trust the farm because it always delivers products on time and replaces any faulty eggs. This positive word-of-mouth has attracted more customers, increasing the farm's profits. This trust and reputation are called goodwill, which is an intangible asset. Intangible assets, like goodwill, do not have physical form but bring long-term value to a business.

B. Liabilities

We have discussed in detail about liabilities with illustration of the farm in the beginning of this chapter. Now we will classify the liabilities in a way to be written on a Balance Sheet:

◊ **Fixed Liabilities or Long-Term Liabilities**

Suppose, the farm took a bank loan to buy incubators for hatching eggs. This loan is a liability for the farm, which they do not have to repay it right away. It has a maturity period of up to 10 years. Such debts that need to be repaid after one year or more are called long-term liabilities. Examples include long-term loans, debentures, and public deposits.

◊ **Current Liabilities**

The farm will have certain other obligations like making payment to suppliers of chicks in cases where the chicks were purchased on credit. The farm is liable to settle these obligations as soon as possible. These debts can be called as current liabilities of the farm. Current liabilities in general are debts to be repaid by the business within one year. Current liabilities include:

a. **Bank Overdraft**: When the farm needed more money for a purchase, their bank account balance was zero. Thankfully, SBI, the bank they have a good relationship with, allowed them to continue using the account even with no money. This extra amount drawn from the bank with permission is called a bank overdraft. The farm has to pay back this amount to the bank soon, making it a current liability. Overdraft lets businesses withdraw money even with a zero balance.

b. **Bills Payable:** The farm bought feeding material on credit from the supplier. To guarantee the transaction, the supplier prepares a bill stating the amount and when the farm should make the payment. This bill, which makes the farm responsible for paying the supplier, is called bills payable. Usually, the repayment period mentioned in the bill is less than a year, making it a current liability. Bills payable is a legal agreement for the farm to pay the owed amount in the future.

c. **Sundry Creditors**: The farm had purchased a new variant of feeding material from a supplier who is his friend. The purchase was made on credit. The owner promised to pay the amount back after a few months and since the supplier was owner's friend no bill was drawn as guarantee. For the farm, this is a liability that needs to be settled immediately. The farm keeps a record of this obligation and the amount it owes to the supplier. Similar kinds of liabilities of the farm will be grouped together and placed under the common heading of Sundry Creditors. Sundry Creditors can be defined as persons to whom a company owes money when goods or services are purchased on credit.

d. **Outstanding Expenses**: The workers at the farm, who are from other states, asked to receive their wages in bulk to save for their visits to home. As a result, their wages are not paid monthly though it is due every month. These unpaid wages are called outstanding expenses. They are expenses that are due but not yet paid and are considered current liabilities. Common outstanding expenses include unpaid salary, wages, and rent.

C. Capital/Owner's Equity

Let us consider a small bakery with the following financial information:

◊ Total Assets: ₹1,00,000

◊ Total Liabilities: ₹60,000

In this case, the Capital/Owner's Equity would be calculated as:

Capital/Owner's Equity = Total Assets - Total Liabilities

Capital/Owner's Equity = ₹1,00,000 - ₹60,000 = ₹40,000

This means that the owners have invested ₹40,000 into the business, and this represents their claim on the net assets of the bakery.

Capital or Owner's Equity represents the net worth or the residual claim of the owners or shareholders of a business. It is the difference between the total assets (what the business owns) and the total liabilities (what the business owes to others).

Preparation of Balance Sheet

Now with the concepts you have learned so far in this chapter, we look at the general steps to be followed in the preparation of Balance Sheet.

- ◊ Real accounts and Personal accounts which are not entered in the Trading and Profit and Loss account are entered in the Balance Sheet.
- ◊ Balance Sheet is not an account but it is a statement and as a result it does not have debit side and credit side.
- ◊ Balance Sheet has two sides: Asset side and Liability side.
- ◊ Assets are written on the right side of the Balance Sheet and Liabilities and Capital are written on the left side of the Balance Sheet.
- ◊ Balance Sheet is a detailed depiction of the Accounting Equation. So, as per the accounting equation, the Asset side and Liability side of the Balance Sheet must be equal.
- ◊ Assets and Liabilities are arranged in the Balance Sheet according to the principle of Grouping and Marshalling.

Grouping or Marshalling of Assets and Liabilities

According to the Companies Act 2013, Balance Sheets must be prepared in a standard format using the method of grouping or marshalling. In the above mentioned farm's Balance Sheet, individuals who owe money for purchases are presented together under "Sundry Debtors" instead of listing them individually which is an example of grouping. Marshalling is the arrangement of assets and liabilities in a specific order. For the farm, current assets are listed first, followed by fixed assets and intangible assets. On the liability side, current liabilities come first, followed by fixed liabilities and capital. This order is known as the order of liquidity, reflecting the farm's ability to convert assets to cash and settle debts promptly. Sole proprietorships and partnerships commonly follow this practice in Balance Sheet preparation. Assets and liabilities can be marshalled in order of permanence also. Order of permanence arranges assets and liabilities based on their permanency within the business. Intangible assets are listed first, followed by fixed assets and current assets. On the liability side, owner's capital comes first, followed by long term liabilities and current liabilities. Corporate businesses typically follow the order of permanence in their Balance Sheets.

The Final Accounts, we are dealing here are that of Sole Proprietors, so we will be preparing the Balance Sheet according to the order of liquidity. As we have learned in detail about the preparation of Balance Sheet, we will look into the general format of Balance Sheet as per the order of liquidity and order of permanence separately.

Table 1.4.4

Balance Sheet in the Order of Liquidity

Liabilities		Amount	Asset	Amount
Bank Overdraft		Xxx	Cash In Hand	xxx
Sundry Creditors		xxx	Cash At Bank	xxx
Bills Payable		xxx	Short term investments	xxx
Outstanding Expenses		xxx	Bills Receivable	xxx
Loans		xxx	Sundry Debtors	xxx
Capital:	xxx		Closing Stock	xxx
Add: Net profit	xxx		Prepaid Expenses	xxx
Add: Interest on Capital	xxx		Furniture	xxx
	xxx		Machinery	xxx
Less: Drawings	xxx		Land and building	xxx
		xxx	Goodwill	xxx
		xxxx		xxxx

Table 1.4.5

Balance Sheet in the order of permanence.

Liabilities		Amount	Asset	Amount
Capital :	xxx		Goodwill	xxx
Add: Net profit	xxx		Land And Building	xxx
Add: Interest on Capital	xxx		Plant And Machinery	xxx
	xxx		Furniture And Fittings	xxx
Less: drawings	xxx	xxx	Prepaid Expenses	xxx
Loans			Closing Stock	xxx
Bills Payable		xxx	Bills Receivable	xxx
Outstanding Expenses		xxx	Sundry Debtors	xxx
Sundry Creditors		xxx	Short term investments	xxx
Bank Overdraft		xxx	Cash at Bank	xxx
		xxx	Cash in Hand	xxx
		xxxx		xxxx

Since the concept behind the preparation of Final Accounts is discussed, we can solve a simple problem involving the preparation of Final Accounts.

Illustration:

From the following information on Raj's Farm, prepare Trading and Profit and Loss account for the year ended 31 December 2020 and a Balance Sheet as on that date.

Particulars	Amount (₹)	Particulars	Amount (₹)
Sales	25000	Factory Expenses	200
Purchase	4000	Repairs	190
Capital	6200	Stock (01-01-2020)	1600
Salary	750	Rent	250
Machinery	15000	Drawings	1700
Furniture	3600	Advertisement	300
Sundry creditors	4600	Carriage inwards	300
Wages	100	Cash at bank	2600
Sundry Debtors	8560	Bills Payable	3350

The closing stock was ₹250.

Trading and Profit and Loss Account for the year ended 31 December 2020

Particulars	Amount (₹)	Particulars	Amount (₹)
Opening stock	1600	Sales	25000
Purchases	4000	Closing stock	250
Direct expenses			
Carriage inwards	300		
Wages	100		
Factory expenses	200		
To gross profit c/d	19050		
Total	25250	Total	25250
Salary	750	By gross profit b/d	19050
Repairs	190		
Rent	250		
Advertisement	300		
Net profit transferred to capital account	17560		
Total	19050	Total	19050

Balance Sheet as on 31 December 2022

Liabilities		Amount	Asset	Amount
Bills Payable		3350	Cash at bank	2600
Sundry Creditors		4600	Closing Stock	250
			Sundry debtors	8560
			Furniture	3600
Capital	6200		Machinery	15000
Add: Net profit	17560			
	23760			
Less: Drawings	1700	22060		
		30010		30010

Recap

- ◊ Trial Balance is a financial statement listing balances of all general ledger accounts and it verifies mathematical accuracy of bookkeeping records
- ◊ Errors can occur that do not affect trial balance agreement
- ◊ Common errors include errors of omission, commission, compensating errors, and errors of principle
- ◊ Errors are rectified differently before vs. after preparing trial balance
- ◊ Final accounts include Trading Account, Profit & Loss Account, and Balance Sheet
- ◊ Trading Account shows gross profit/loss from buying and selling activities
- ◊ Profit & Loss Account incorporates indirect expenses/income to show net profit/loss
- ◊ Balance Sheet provides snapshot of assets, liabilities and owner's equity
- ◊ Assets include fixed assets, current assets, and intangible assets
- ◊ Liabilities include long-term and current liabilities
- ◊ Balance Sheet follows accounting equation: Assets = Liabilities + Owner's Equity
- ◊ Two orders used: liquidity (for sole proprietorships/partnerships) and permanence (for corporations)

Objective Questions

1. What is the financial statement that verifies the mathematical accuracy of books?
2. What type of error occurs when two mistakes balance each other?
3. Which account shows the gross profit from trading?
4. What do we call resources owned by a business for long-term use?
5. What term describes debts to be repaid within one year?
6. What is the term for extra amount drawn from a bank with permission?
7. What do we call the positive reputation of a business?
8. What is the term for arranging items in a specific order in a Balance Sheet?
9. What order is followed in the Balance Sheet of sole proprietorships?
10. What is the equation behind a Balance Sheet?
11. On which side of the Balance Sheet are assets shown?
12. Which account shows the net profit or loss?
13. What do we call expenses that are due but not yet paid?
14. What term describes assets without physical form?
15. Who are the persons owing money to a business for credit purchases?

Answers

1. Trial Balance
2. Compensating error
3. Trading Account
4. Fixed assets
5. Current liabilities
6. Bank overdraft
7. Goodwill
8. Marshalling
9. Liquidity

10. Accounting equation
11. Right side
12. Profit & Loss Account
13. Outstanding expenses
14. Intangible assets
15. Debtors

Assignments

1. What is the purpose of preparing a Trial Balance?
2. How does a Trading Account differ from a Profit & Loss Account?
3. Define current assets and give three examples.
4. What is the difference between fixed liabilities and current liabilities?
5. Explain the concept of grouping and marshalling in Balance Sheet preparation.
6. What are the main components of a Balance Sheet?
7. Prepare a Trial Balance from the following information

   XYZ Company had the following transactions during the year ended December 31, 2022:

   Received ₹25,000 cash from the owners as initial investment.

   Purchased equipment for ₹80,000 on credit.

   Acquired inventory worth ₹35,000 by paying in cash.

   Sold goods with a cost of ₹120,000 for ₹180,000 on credit.

   Paid ₹30,000 towards accounts payable.

   Incurred ₹35,000 in salaries expense.

   Incurred ₹12,000 in rent expense.

   Incurred ₹8,000 in utilities expense.

   Recorded accumulated depreciation of ₹20,000 on the equipment.

   Took out a loan of ₹45,000 from the bank.

Given the above transactions, prepare the Trial Balance for XYZ Company as of December 31, 2022.

8. From the following Trial Balance, prepare Trading Account, Profit & Loss Account for the year ended March 31, 2023, and Balance Sheet as on that date:

Trial Balance for ABC Company as of December 31, 2023

Account	Debit	Credit
Cash	₹85,000	
Land	₹100,000	
Office Equipment	₹30,000	
Accounts Receivable	₹80,000	
Inventory	₹40,000	
Accounts Payable		₹20,000
Notes Payable		₹60,000
Capital Stock		₹50,000
Sales		₹80,000
Cost of Goods Sold	₹40,000	
Salaries Expense	₹25,000	
Rent Expense	₹10,000	
Utilities Expense	₹5,000	
Total	₹415,000	₹415,000

9. Explain the different types of accounting errors and methods to rectify them. Provide examples for each type of error.

Suggested Reading

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1. Warren, C. S., Reeve, J. M., & Duchac, J. E. (2023). *Financial & Managerial Accounting*. Cengage Learning.
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2

BLOCK

Computerised Accounting - Tally

Unit 1

Tally

Learning Outcomes

Upon the completion of this Unit, the learner will be able to;

- ◊ create awareness on the basic concepts in Tally
- ◊ realise the importance of computerised accounting through the software
- ◊ get a broad idea about the creation and loading of company and the recording of inventory
- ◊ know the Group and ledger formation methods

Prerequisites

Priyanka, is a young entrepreneur who just opened her first coffee shop. At first, she tried to keep track of her business finances using pen and paper. Every night, she had to sit down with a stack of receipts, trying to figure out her sales, expenses, and profits. It was time-consuming and frustrating. One day, Priyanka's friend Tom visited the coffee shop. He noticed Priyanka looking stressed as she struggled with her books. Tom, who ran a successful bakery, smiled and said, "Priyanka, let me tell you about something that changed my business life - computerised accounting!" Tom explained how he used a software called Tally to manage his bakery's finances. "It is like having a super-smart assistant," he said. "Tally helps me record every sale, track my inventory, and even prepare financial reports with just a few clicks." Intrigued, Priyanka decided to give it a try. She installed Tally on her computer and was amazed at how user-friendly it was. She created her coffee shop as a "company" in Tally, set up different ledgers for various expenses like coffee beans, milk, and staff wages, and started entering her daily transactions.

To her surprise, what used to take hours now took minutes. Tally automatically calculated her profits, showed her which products were selling best, and even reminded her when it was time to reorder supplies. Priyanka could now see at a glance how her business was doing. As months passed, Priyanka's coffee shop flourished. With Tally handling the number-crunching, she had more time to focus on creating new coffee blends and chatting with customers. When tax season came around, Priyanka was not worried at all. Tally had all her financial information organised and ready. Priyanka realised that computerised accounting with Tally was not just about making her life easier. It was a powerful tool that gave her insights into her business, helped her make smarter decisions, and ultimately contributed to her success. As she sipped her morning coffee and looked at her neatly organised Tally reports, Priyanka smiled, thinking about how far she had come from those stressful nights with her paper ledgers. In this unit let us learn the basic aspects of computerised accounting using Tally software.

Keywords

Startup Tally, Creation of Company, Alteration of a company, Deleting a company, Shut a company

Discussion

2.1.1 Computerised Accounting

A busy restaurant kitchen during the dinner rush - Chefs are cooking, waiters are rushing orders, and customers are eagerly waiting for their meals. The restaurant owner trying to keep track of all the ingredients used, meals sold, staff hours worked, and money earned - all with just a pen and paper. It would be chaos, right? This is where computerised accounting comes in. It is like having a super-efficient assistant that keeps track of every financial detail, allowing the owner to focus on running the restaurant.

Computerised accounting is the modern way of recording, organising, and analysing financial information using specialised software. Instead of writing in ledgers or filling out spreadsheets by hand, businesses use programs that automate many accounting tasks. These systems can record transactions, calculate totals, generate reports, and even help with complex processes like payroll or tax preparation. Computerised accounting can be defined as the process of using specialised software to record, store, and analyse financial data in a systematic and automated manner, enabling businesses to manage their finances more efficiently and accurately.

2.1.1.1 Benefits of Computerised Accounting

Accuracy: Computerised accounting systems significantly reduce human errors. For instance, imagine a small retail store manually tallying up hundreds of sales transactions each day. Even a small mistake could throw off the entire balance sheet. With computerised accounting, each sale is automatically recorded and calculated, minimizing the risk of errors.

Example: A local grocery store switched to a computerised system and found that their end-of-day balances matched their actual cash and card receipts much more consistently, eliminating the hours spent trying to find small discrepancies.

Time Savings: Automated processes save enormous amounts of time. Tasks that once took hours or even days can now be completed in minutes.

Example: A freelance photographer used to spend every Sunday afternoon manually entering receipts and invoices. After adopting accounting software, he/she now spends just 15 minutes a day quickly reviewing and categorising transactions, freeing up her weekends for actual photography.

Real-Time Financial Information: Computerised systems provide up-to-date financial data at the click of a button, allowing for better decision-making.

Example: A restaurant owner can check his food costs versus revenue in real-time, allowing him to quickly adjust menu prices or supplier orders if he notices costs creeping up.

Improved Financial Analysis: Advanced reporting tools offer deeper insights into a company's financial health.

Example: A small manufacturing company used their accounting software to generate a report showing profitability by product line. They discovered that one of their least-produced items was actually their most profitable, leading them to restructure their production priorities.

Better Inventory Management: For businesses dealing with physical goods, computerised accounting can integrate with inventory systems. *Example*: A bookstore owner can see exactly how many copies of each title are in stock, what is on order, and how quickly different books are selling, all within her accounting software.

Easier Tax Compliance: Computerised systems can automatically categorise transactions and generate tax reports, simplifying tax preparation. *Example*: A self-employed consultant dreaded tax season until he/she started using accounting software. Now, he/she can generate a tax summary report with all her income and deductible expenses categorised correctly, saving her hours of work and reducing her anxiety about potential audits.

Improved Audit Trails: Computerised systems maintain detailed records of all financial transactions, which is crucial for auditing purposes. *Example*: When a mid-sized company was audited, they were able to quickly provide detailed transaction histories for specific accounts, complete with dates, amounts, and related documents, all generated from their accounting software.

Multi-User Access: Many systems allow multiple users to access the data simultaneously, improving collaboration. *Example*: In a small marketing agency, the account managers can enter billable hours, the finance manager can process invoices, and the CEO can review overall financial performance, all at the same time from different locations.

Cost-Effective in the Long Run: While there may be initial setup costs, computerised accounting often saves money over time through increased efficiency and reduced errors. *Example*: A growing e-commerce business found that after implementing accounting software, they no longer needed to hire an extra part-time bookkeeper to keep up with their increasing transaction volume, saving them thousands in annual wages.

Integration with Other Systems: Many accounting systems can integrate with other business software, creating a more streamlined operation. *Example*: A small manufacturing company integrated its accounting software with their e-commerce platform and inventory management system. Now, when a sale is made online, it automatically updates its inventory levels and financial records without any manual input.

Enhanced Security: Computerised systems often have better security measures than traditional paper-based systems. *Example*: A local non-profit organisation uses accounting software with role-based access control. This means volunteers can enter donations received, but only the treasurer can view full financial reports or process payments, reducing the risk of fraud or data breaches.

Scalability: As a business grows, computerised accounting systems can easily scale to handle increased transaction volumes and complexity. *Example*: A startup that began with just two founders grew to a team of 50 within two years. Their cloud-based accounting software seamlessly scaled with them, handling the increased complexity of multiple departments, project-based accounting, and a much higher volume of transactions.

In conclusion, computerised accounting offers numerous benefits that can significantly improve a business's financial management and overall operations. From increased accuracy and efficiency to deeper financial insights and better decision-making capabilities, these systems have become an essential tool for businesses of all sizes in the modern economy.

2.1.2 Tally Software

Tally, in its current form, is a comprehensive business management software suite. The latest version, TallyPrime, is designed to cater to various aspects of business management, especially for small and medium-sized enterprises. Tally Solutions is a Bangalore-based company that was co-founded by Shyam Sunder Goenka and Bharat Goenka in the year 1986. This father-son duo came up with this software to help manage the financial transactions in their own company and then given its efficiency launched it for the world. The first version of Tally was called Peutronics Financial Accountant and it only offered basic accounting features. Later the software is updated with new versions. Now, Tally Solutions had more than 1 million customers. Bharat Goenka won the Padma Shri Award in the field of Trade and Industry for all his hard work in developing this world-renowned software.

Tally software versions with years

Tally 3.0	Founded in the year 1990 and it offered basic accounting features.
Tally 3.12	Developed in the year 1992 and it offered similar features to the previous version.
Tally 4	Developed in the year 1992 and it supported Microsoft DOS.
Tally 4.5	Developed in the year 1994 and it offered enhanced performance than the previous versions.
Tally 5.4	Developed in the year 1996 and it offered a graphic interface version.
Tally 6.3	Developed in the year 2001. It was compatible with Windows and offered features to calculate VAT.
Tally 7.2	Developed in the year 2005 with more enhanced features.
Tally 8.1	Developed in the year 2006 with features for managing payroll and point of sale.
Tally 9	Developed in the same year 2006 with features for TDS calculation, E-TDS filing, and FBT among other features.
Tally ERP 9	Developed in the year 2009. It could help with GST calculations, had a multi-user login feature, could generate invoices, and could also be remotely accessed from various office locations.
Tally Prime	Developed in the year 2020 with easier navigation, user experience, and multi-tasking features TallyPrime was first introduced in 2020, replacing the previous Tally. ERP 9 version. Since then, Tally Solutions has been releasing regular updates rather than completely new versions. Here is the timeline: ◊ TallyPrime Release 1.0 - December 2020 ◊ This was the initial release of TallyPrime ◊ TallyPrime Release 2.0 - July 2021 ◊ This update brought significant improvements and new features. ◊ TallyPrime Release 2.1 - November 2021 ◊ This version included further enhancements and bug fixes. ◊ TallyPrime Release 3.0 - August 2022 ◊ TallyPrime Release 4.1 – March, 2024 ◊ TallyPrimeEDU and TallyPrimeGold

Tally is very user friendly and popular Accounting Software that runs on Microsoft Windows. It can even maintain your Accounts, Inventory and Statutory Compliances. It is a comprehensive accounting and inventory management system designed to help businesses manage their financial transactions, inventory, and compliance requirements. It is widely used by small and medium-sized enterprises (SMEs) in India and other countries.

Some key features of Tally include:

1. Accounting: Financial accounting, journal entries, ledger management, and trial balance.
2. Inventory: Management of stock, inventory tracking, and reporting.
3. Taxation: Compliance with various tax laws, including GST (Goods and Services Tax).
4. Reporting: Generation of financial statements, such as balance sheets and profit & loss accounts.
5. Payroll: Management of employee payroll and related statutory compliance.

Tally offers various versions, including Tally Prime, Tally ERP 9, and Tally on Cloud in order to cater to different business needs.

2.1.2 Working with Tally Software

To start using Tally software, follow these steps:

1. Launch Tally: Open the Tally software on your computer by double-clicking on the Tally icon or searching for it in your start menu.
2. Create a Company: Once Tally is open, click on the "Create a Company" button to set up your business information. Fill in the required details such as company name, address, and financial year.
3. Set up Your Financial Year: Choose your financial year and set up your accounting periods. This will help Tally organise your financial data.
4. Create a Ledger: Create a ledger to classify and record your financial transactions. You can create ledgers for assets, liabilities, equity, income, and expenses.
5. Start Recording Transactions: Begin recording your financial transactions such as sales, purchases, receipts, and payments. You can use Tally's voucher entry feature to easily record transactions.
6. Explore Tally's Features: Familiarise yourself with Tally's features such as invoicing, inventory management, and financial reporting.

Now let us understand these steps in detail.

2.1.2.1 Launch Tally

Open the Tally software on your computer by double-clicking on the Tally icon or searching for it in your start menu. You can see the following window (fig 2.1.1) when-ever you open the Tally Software.

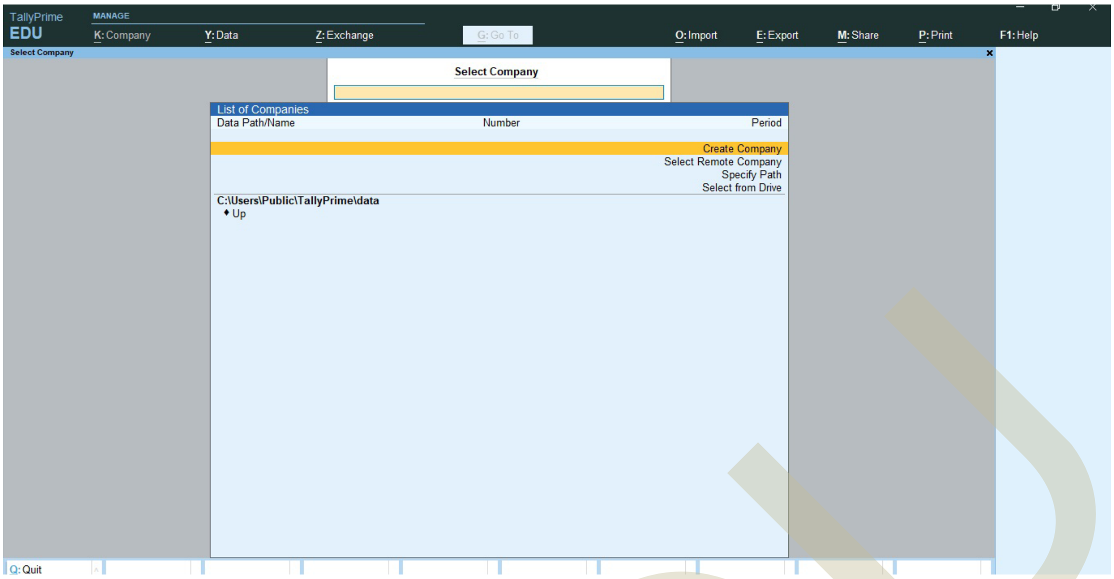

Fig 2.1.1 Tally Starter Platform

2.1.2.2 Quitting Tally

Step 1: Close all open screens

Press Ctrl + W to close the current screen

Repeat this step until all screens are closed

Step 2: Exit Tally

Press Alt + F4 to exit Tally

Alternatively, you can click on the "File" menu and select "Exit"

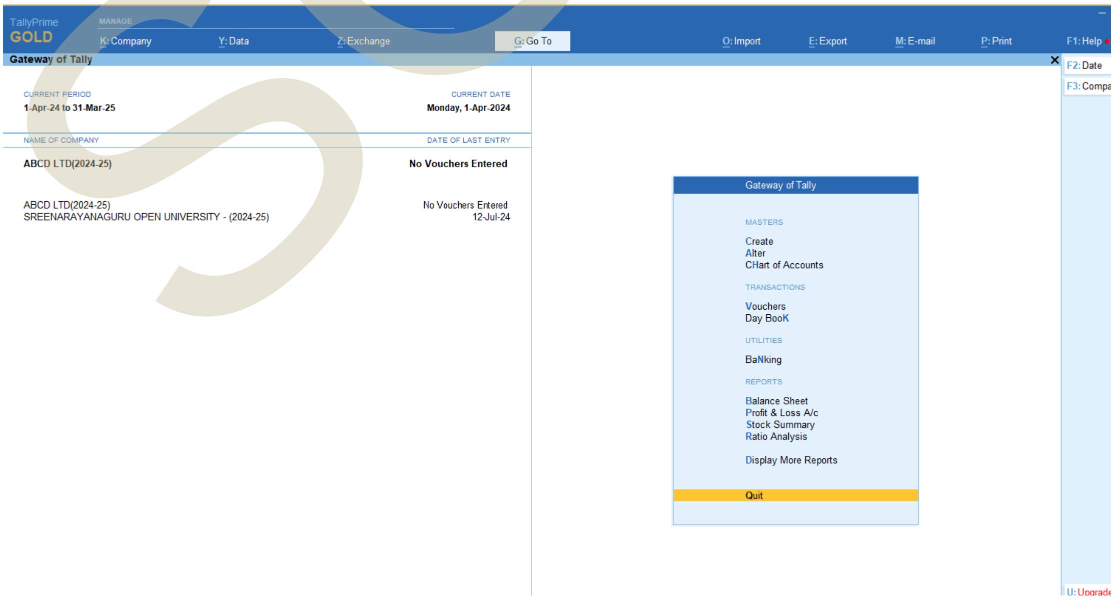

Fig 2.1.2 Quitting Tally

Step 3: Confirm Exit

A confirmation message will appear asking if you want to quit Tally.

Click "Yes" to confirm

Alternatively, you can also use the shortcut key Ctrl + Q to quit Tally directly.

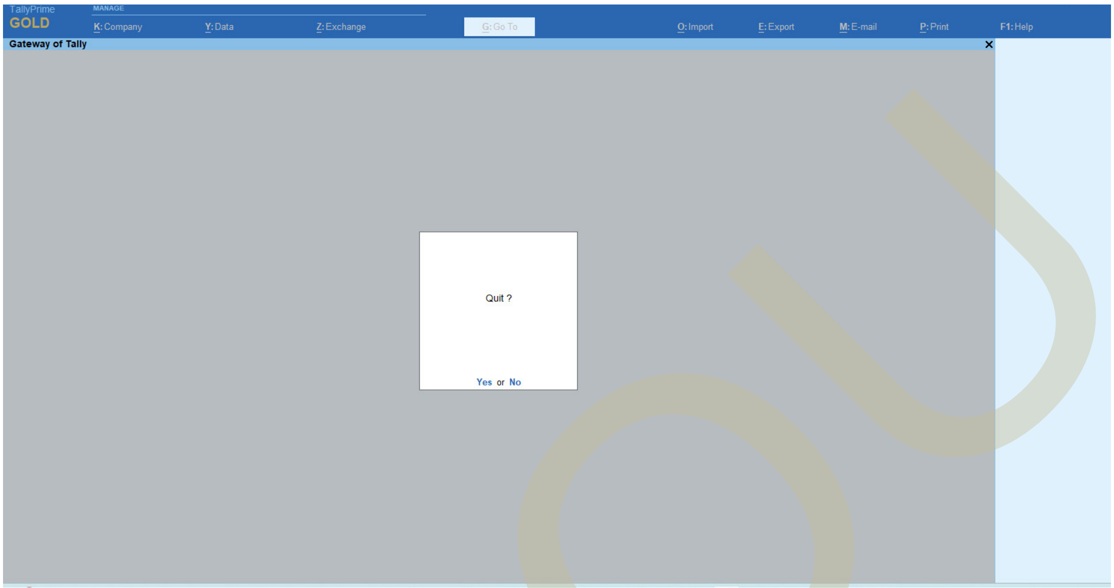

Fig 2.1.3 Confirmation window for quitting Tally

2.1.2.3 Creation of a Company in Tally

A company is a formal business entity formed by a group of individuals to engage in a specific commercial or industrial enterprise. It is characterised by its legal recognition as a separate entity from its owners, known as shareholders or members. Companies are typically created to generate profit through the production or sale of goods and services. They can vary greatly in size, structure, and purpose, ranging from small sole proprietorships to large multinational corporations. Key features of a company include limited liability for its owners, perpetual succession (continuing to exist despite changes in ownership), and the ability to raise capital through the issuance of stocks or bonds.

In Tally, to maintain and process data, you must open a Company and create Accounts. You should learn the following accounting concepts to start Tally.

a. Assets: Resources owned by a business that have economic value and are expected to provide future benefits. Examples include cash, inventory, equipment, and accounts receivable.

b. Liabilities: Financial obligations or debts owed by a business to external parties. These can include loans, accounts payable, and accrued expenses.

c. Capital: Also known as owner's equity, it represents the owner's investment in the business plus accumulated profits. It is the residual interest in the assets after deducting liabilities.

d. Debit: An accounting entry that increases asset or expense accounts and decreases liability, revenue, or equity accounts. It is recorded on the left side of a T-account.

e. Credit: An accounting entry that increases liability, revenue, or equity accounts and decreases asset or expense accounts. It is recorded on the right side of a T-account.

f. Double Entry Accounting: A fundamental accounting principle where every financial transaction is recorded in at least two accounts. For each debit entry, there must be a corresponding credit entry, ensuring that the accounting equation (Assets = Liabilities + Capital) always remains balanced.

Let us learn the creation of company in TallyPrime

To create a company;

Step 1: Double click on the Tally Icon > Create Company

Or

Go to Gateway of Tally > Alt+F3 > Create Company.

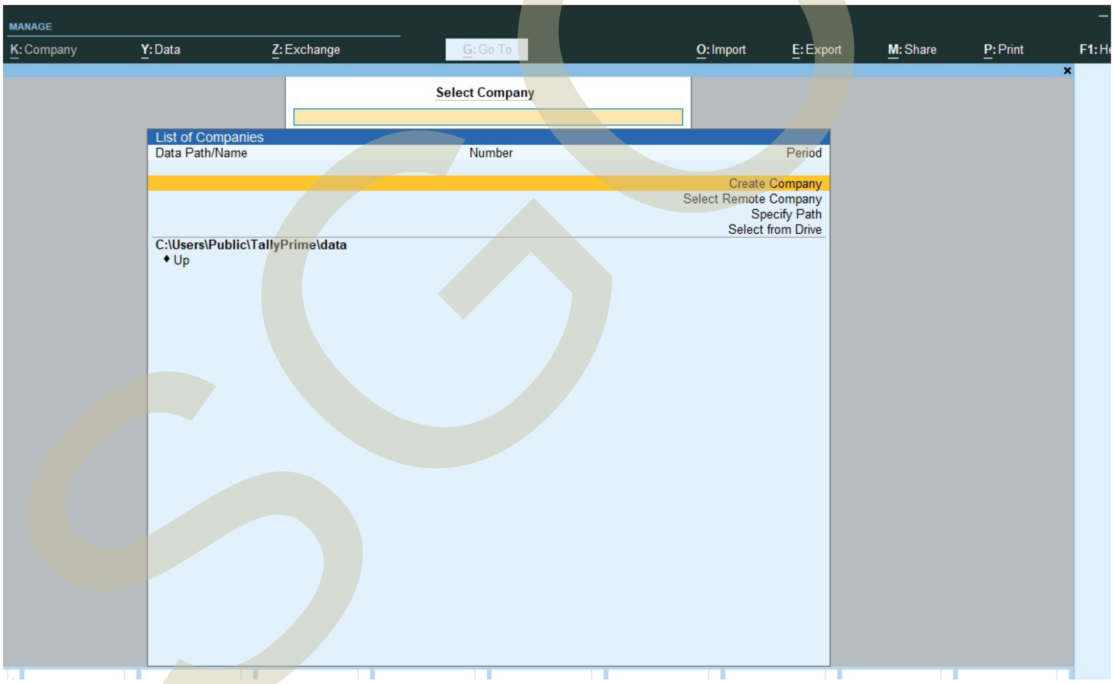

Fig 2.1.4 Go To window

Step 2: Click on Create Company.

Step 3: Fill the details

Use Enter key to go downwards. Use Tab to navigate between fields. Use Enter key to save and move to the next field. Accept > Yes.

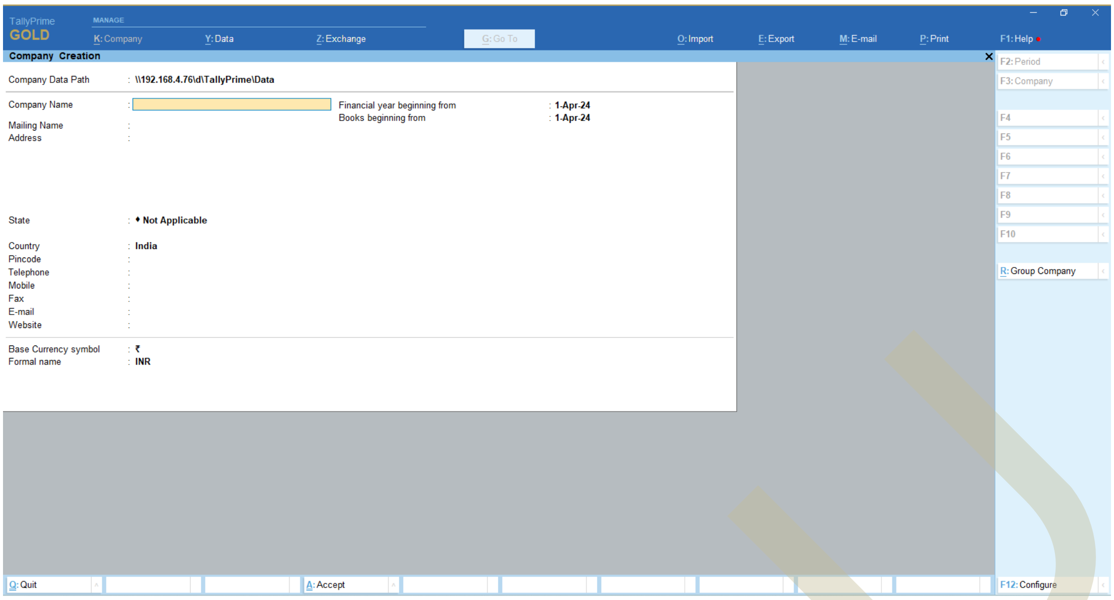

Fig 2.1.5 Fill Details of Company

2.1.2.4 Set up Financial Year

As part of filling details, the details of the financial year should also be given.

Press Alt + F2 to open the "Financial Year" screen

Select the financial year start and end dates

If you want to get the transaction details of a day, press F2.

Use Ctrl + S to save

2.1.2.5 Set up Currency

Press F3 to open the "Currency" screen

Select the currency and symbol

Use Ctrl + S to save

2.1.2.6 Set up Units

Press F4 to open the "Units" screen

Select the unit of measurement

Use Ctrl + S to save

2.1.2.7 Save Company

Press Ctrl + S to save the company details

Then you can see an Accept message. Answer as yes. See the Screenshot given below. All those are default. You can see this in the following Screenshot.

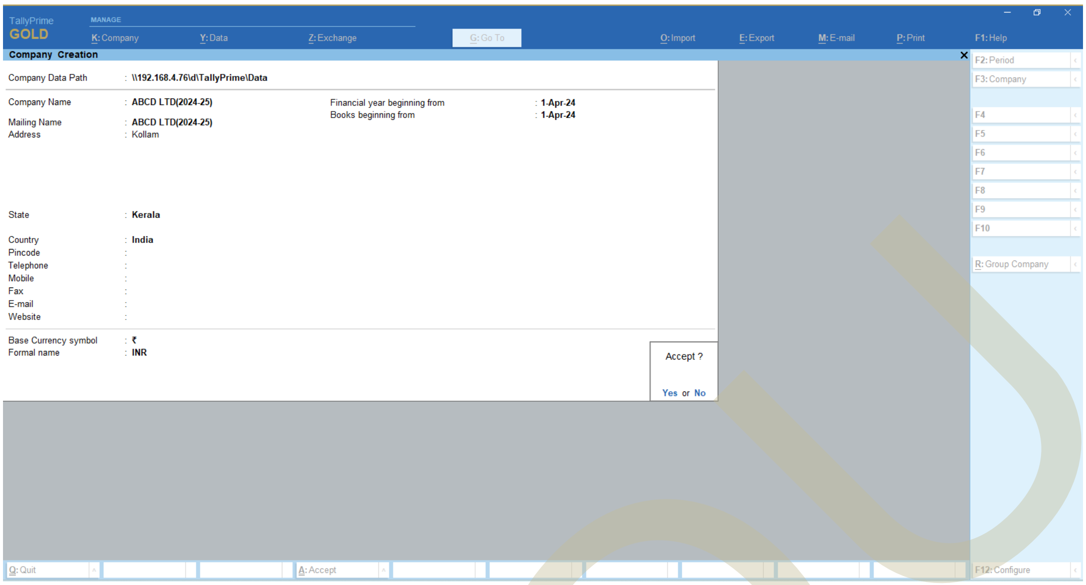

Fig 2.1.6 Confirmation window for creating Company

You will see a confirmation message "Company created successfully"

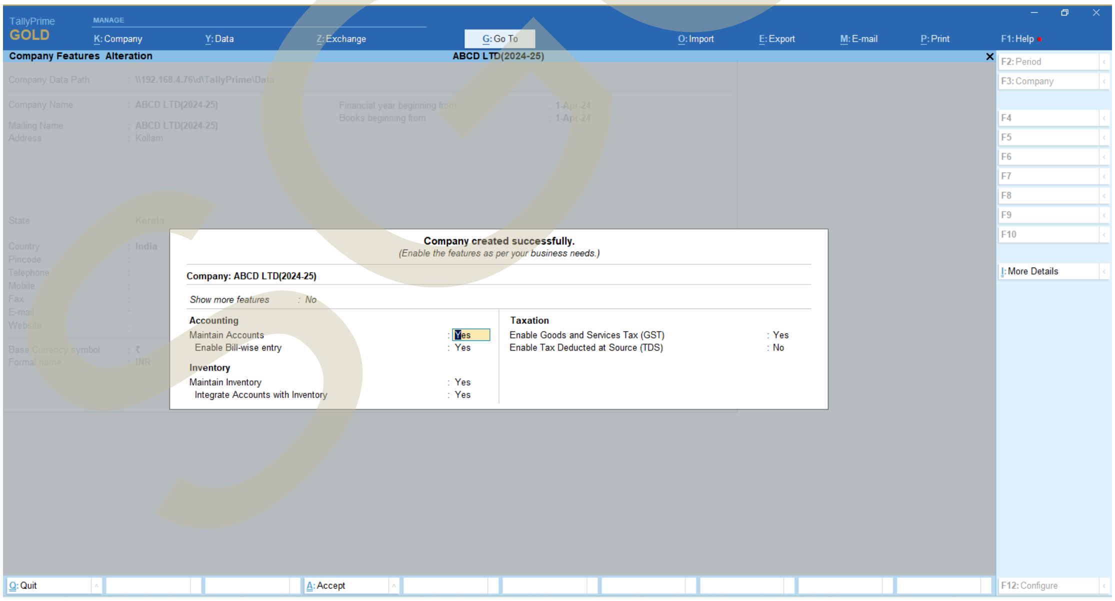

Fig 2.1.7 Company created successfully

2.1.3 Alteration, deleting, and shutting a company

2.1.3.1 Alter a company

To alter the details of the company, you have to click on the Alter Menu. Then you change the details with respect to the company. Such details include Company name, Address, Financial year, Currency, Tax registration details (e.g., GST, VAT), Accounting features (e.g., inventory, payroll), Company logo, Company website, Company email and Other company-related information.

Altering a company in Tally allows you to:

- ◊ Update company information due to changes in business operations or structure
- ◊ Correct errors or inaccuracies in the company details
- ◊ Reflect changes in company name, address, or other details due to rebranding or restructuring
- ◊ Modify accounting features or settings to suit changing business needs

Step 1: To select and alter a company, Go To window > Click on 'Alter Company'

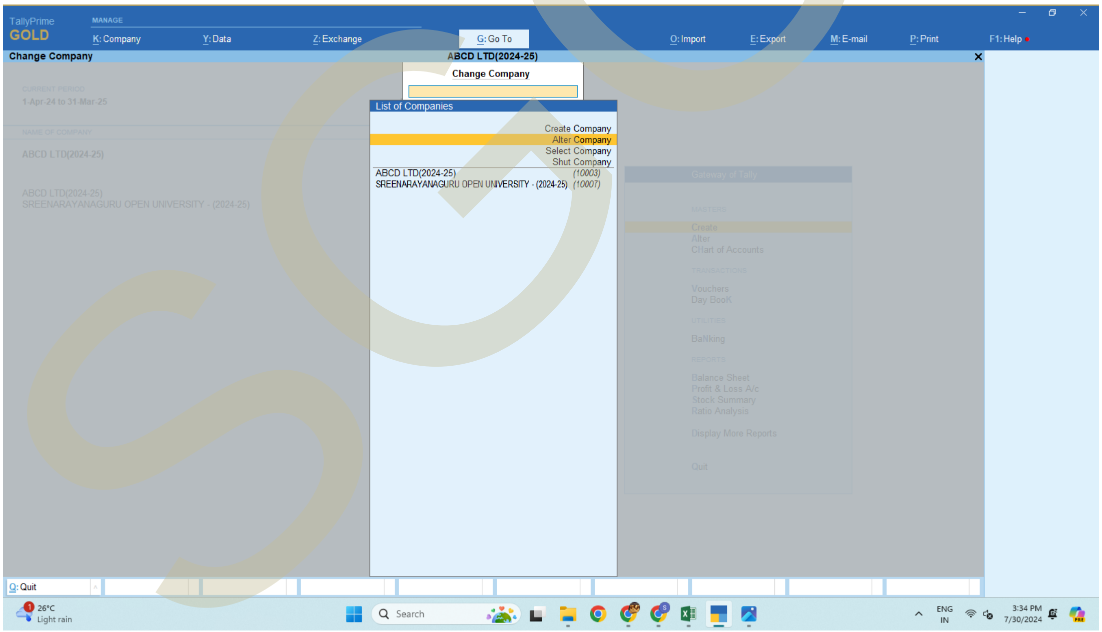

Fig 2.1.8 Select 'Alter company'

Step 2: In the newly opened 'Alter' window, view the list of company details and select the desired company.

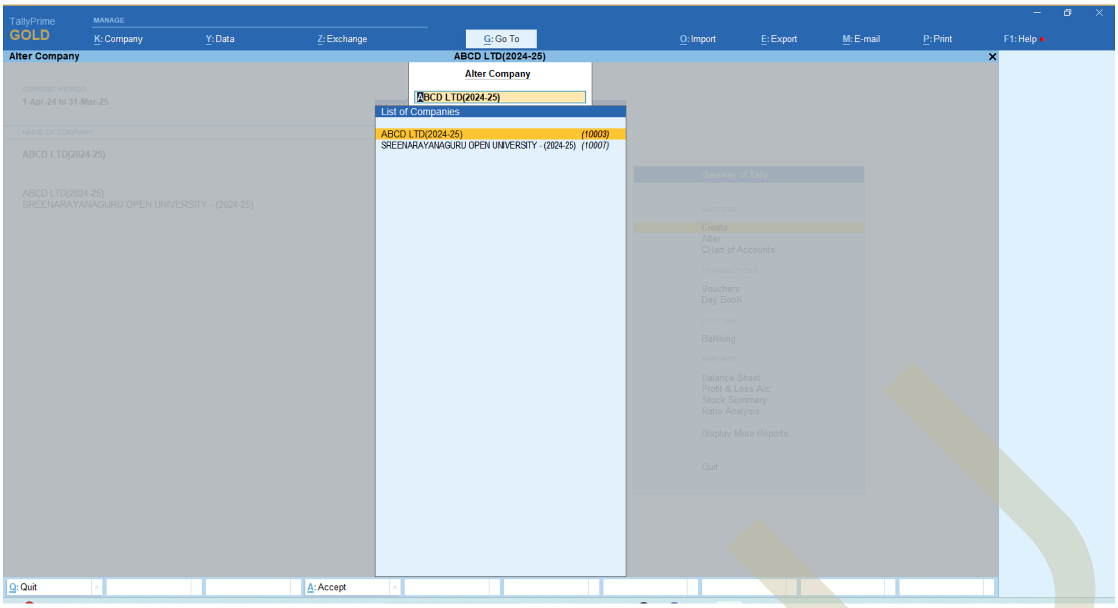

Fig 2.1.9 View the List of company

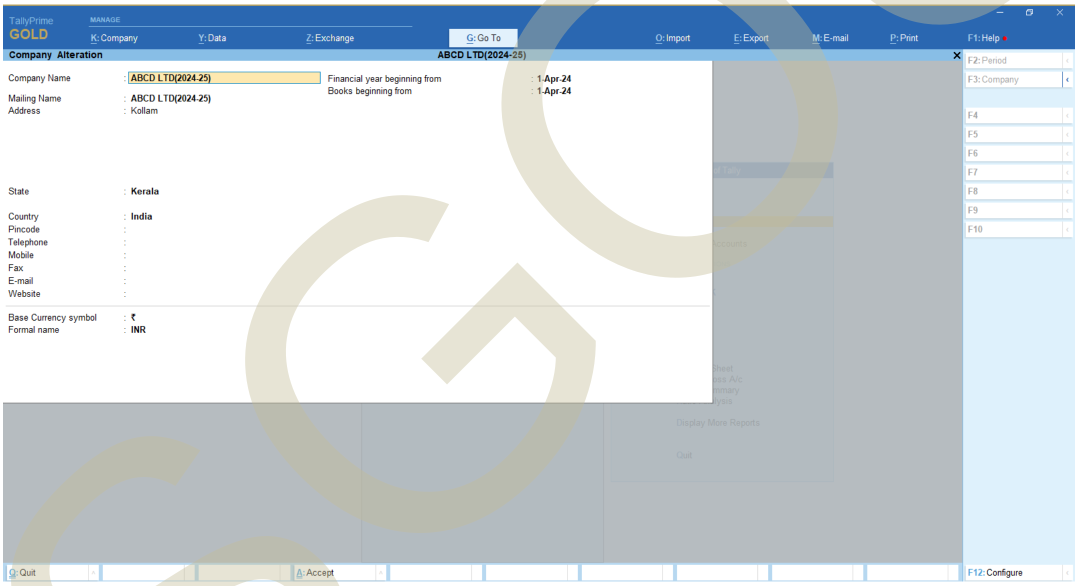

Fig 2.1.10 Make Alteration

Step 3: A confirmation message will appear asking for acceptance.

Click "Yes" to confirm

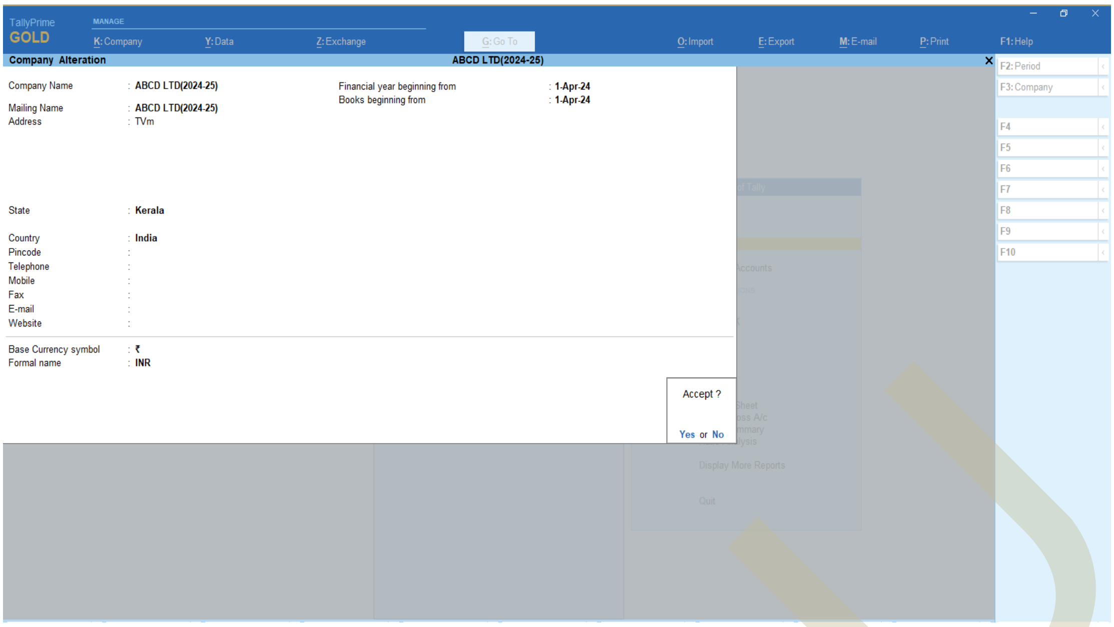

Fig 2.1.11 Confirmation message for alteration of company

2.1.3.2 Delete/ Shut a company

Deleting or shutting a company in Tally means permanently removing the company and all its associated data, transactions, and records from the Tally database. This action is irreversible and cannot be undone. When a company is deleted, all its related information, including financial transactions, accounts, ledgers, inventory, and payroll data, will be erased. Additionally, any links or relationships with other companies or entities within Tally will also be severed. Deleting a company in Tally should be done with caution and only when absolutely necessary, as it will result in the permanent loss of all data related to that company. It is essential to take a backup of your Tally data before deleting a company to ensure that you have a copy of the data, if needed.

This option allows you to delete an existing company. To delete a company, you have to load the company first.

- ◊ Select F3: Cmp Info. (ALT+F3) from the Gateway of Tally to proceed to the Company Information menu
- ◊ Select ‘shut company’ and press Enter.

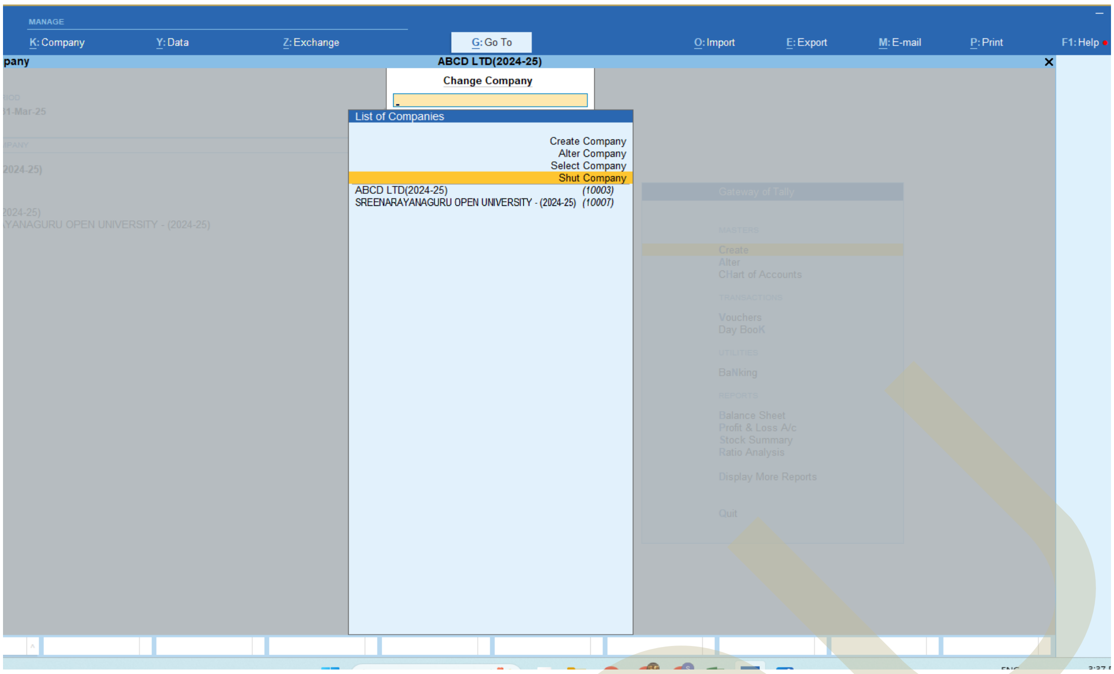

Fig 2.1.12 Select Shut company

- ◊ Select the company to be deleted or shut. The Company Alteration screen is displayed.
- ◊ Use Alt + D to delete. Tally Prime will prompt for a confirmation on deleting the company

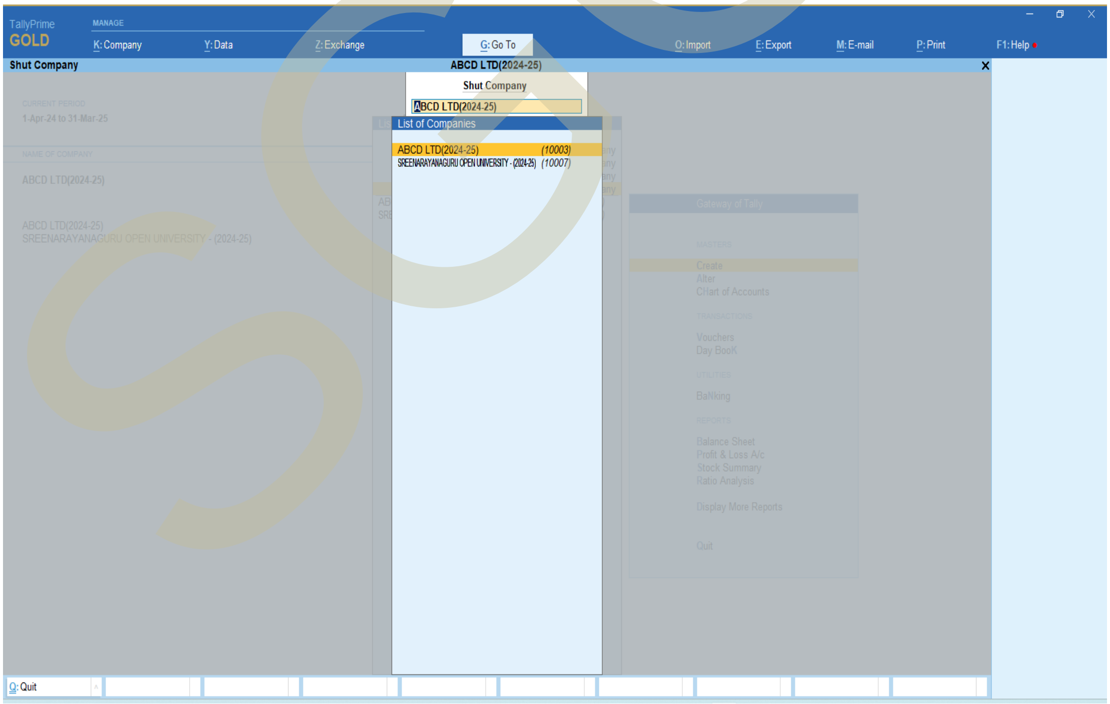

Fig 2.1.13 Window for deleting or shutting down company

- ◊ Press 'Enter' to delete the company

A confirmation message will appear asking for acceptance.

Click "Yes" to confirm

Note: Deletion of a company is irreversible. The company is permanently deleted from the system.

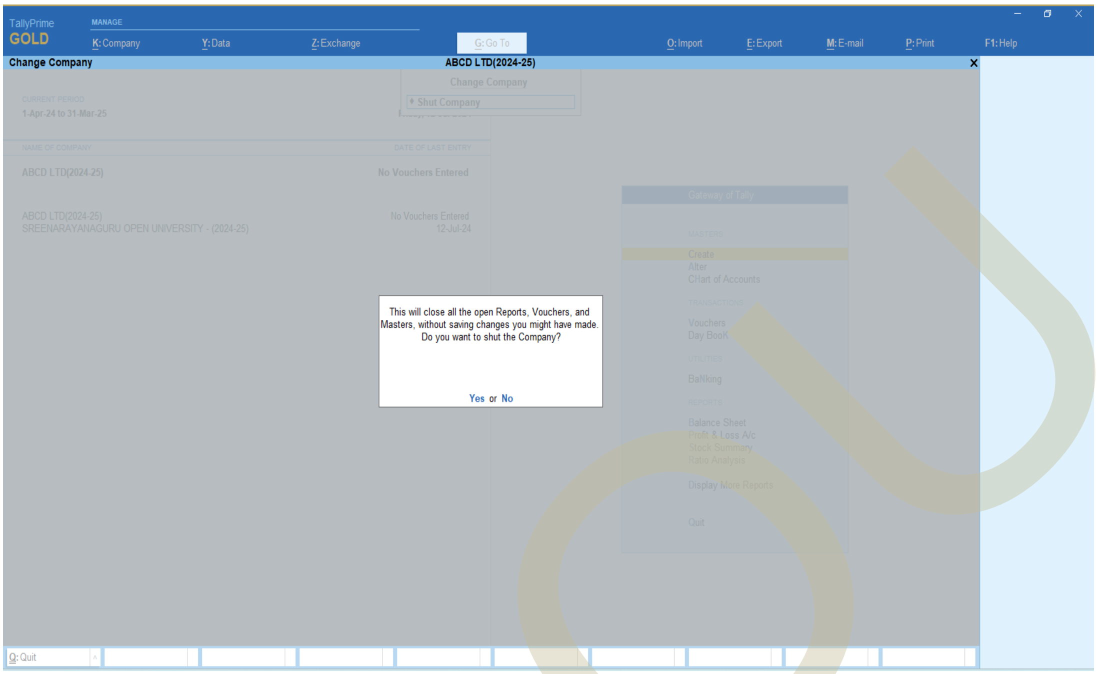

Fig 2.1.14 Confirmation message for acceptance

Recap

- ◊ Computerised accounting uses specialised software to record, organise, and analyse financial information.
- ◊ Benefits of computerised accounting include improved accuracy, time savings, real-time financial information, and better financial analysis.
- ◊ Tally is a popular accounting software developed by Tally Solutions, founded in 1986 by Shyam Sunder Goenka and Bharat Goenka.
- ◊ Tally has evolved through various versions, with TallyPrime being the latest, introduced in 2020.
- ◊ Key features of Tally include accounting, inventory management, taxation compliance, reporting, and payroll management.
- ◊ To use Tally, users need to launch the software, create a company, set up the financial year, create ledgers, and start recording transactions.

◊ The process of creating a company in Tally involves entering company details, setting up the financial year, currency, and units.

◊ Users can alter, delete, or shut a company in Tally as needed, with proper caution for irreversible actions like deletion.

Objective Questions

1. Who co-founded Tally Solutions?
2. In which year was Tally Solutions founded?
3. What is the latest version of Tally called?
4. What award did Bharat Goenka receive for his work on Tally?
5. What key does one press to open the "Financial Year" screen in Tally?
6. What shortcut is used to save company details in Tally?
7. What accounting principle does Tally use for recording transactions?
8. What key combination is used to delete a company in Tally?
9. What is the process of temporarily closing a company's operations in Tally called?

Answers

1. Goenka duo
2. 1986
3. TallyPrime
4. Padma Shri
5. F2
6. Ctrl + S
7. Double Entry
8. Alt + D
9. Shutting company

Assignments

1. What is computerised accounting?
2. List five benefits of using computerised accounting systems.
3. What are the main features of Tally software?
4. Explain the process of creating a company in Tally.
5. What is the significance of the double entry accounting system in Tally?
6. A small retail store owner wants to implement Tally for their business. What steps should they follow to set up their company in Tally and start recording transactions?
7. You're an accountant using Tally for a client's business. The client has changed their company name and address. How would you update this information in Tally?
8. A manufacturing company uses Tally for inventory management. How can they use Tally to track their raw materials, work-in-progress, and finished goods inventory?
9. Your company has ceased operations and you need to close the financial records in Tally. What is the process to shut a company in Tally, and what precautions should you take before doing so?

Suggested Reading

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7. Tally Education Private Ltd. (2021). *TallyPrime: Level 1*. The Official Book from Tally, Bengaluru: Sahaj Enterprise
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Unit 2

Grouping of Accounts

Learning Outcomes

Upon the completion of this Unit, the learner will be able to:

- ◊ comprehend the concept and importance of Groups in TallyPrime for categorising ledgers.
- ◊ create, alter, and delete Groups in TallyPrime.
- ◊ figure out the predefined account groups and their classifications in TallyPrime.

Prerequisites

A small business owner named Raj, who runs a growing electronics store. As his business expands, he finds himself drowning in a sea of financial data - sales, purchases, expenses all jumbled together. One day, while discussing his challenges with a friend, he learns about TallyPrime and its concept of 'Groups'. Intrigued, Raj explores TallyPrime and discovers that Groups are like virtual filing cabinets for financial data. Just as he organises his inventory by product types, TallyPrime allows him to categorise financial information logically. With 28 predefined groups and the ability to create custom ones, Raj realises he can now easily track sales, manage expenses, and get a clear picture of his business's financial health.

As we go deep into this unit, we will examine how Groups in TallyPrime, like in Raj's case, can transform financial management for businesses of all sizes. Whether you are an aspiring entrepreneur, an accounting student, or looking to enhance your business skills, understanding Groups in TallyPrime will equip you with a powerful tool for success in the modern business world.

Keywords

Groups, Ledgers, Chart of Accounts, Primary Groups, Subgroups, Predefined account groups, Display of Groups, Alter Groups

Discussion

2.2.1 Groups in TallyPrime

In any business, it is important to categorise similar ledgers based on their nature, type, or usage under an accounting head. In TallyPrime, such accounting heads are known as Groups. You can create, alter, and delete Groups in TallyPrime along with copying Groups from one company to another. Furthermore, in TallyPrime, you can view the created Groups with all the transactions in multiple reports. Groups help you organise the ledger accounts and view the financial statements with proper accounting heads. It can be classified between Assets, Liabilities, Expenses, and Incomes. Any Groups created under Assets and Liabilities form a part of the Balance Sheet whereas Groups under Expenses and Incomes are part of the Profit & Loss Account.

In TallyPrime, there are 28 predefined groups, of which 15 are Primary and 13 are Subgroups. Along with the predefined groups, you can create new Groups to accommodate your business needs. After creating the Groups, if you want to alter the Group for an existing ledger then you can do that as well. Suppose you have created wages under the group Direct Expense, and you want to change the Group to Indirect Expense. You can alter the ledger account and change the Group for that ledger. TallyPrime also allows you to delete unused or unwanted Groups, if any. All these changes and deletions of Groups can be tracked if you have enabled the Edit Log option. Suppose you have multiple companies and want to maintain a similar group structure and uniformity across the companies. In that case, you can copy Groups from one company to another either one at a time or all at once.

Apart from these, you can configure advanced options for Groups and make the Groups behave as sub-ledgers. With all these options, it becomes absolutely necessary to view the groups on a single page. TallyPrime provides solutions to that need as well by displaying reports such as Group Summary and Group Voucher.

2.2.2 Predefined Account Groups

There are certain account groups which are predefined in Tally to help users classify and organise their accounts in a logical and consistent manner. There are 28 predefined groups in TallyPrime. These groups are part of the Chart of Accounts for most organisations. For example, Sales Accounts are a predefined group. All sales ledgers can be classified into this group.

Out of the 28 predefined groups, 15 are primary groups of which nine Primary groups appear in the Balance Sheet that are capital in nature and six Primary groups appear under Profit & Loss A/c, which are revenue in nature and 13 are subgroups which are shown below. You can create any number of primary groups and subgroups but Primary groups in TallyPrime cannot be deleted.

Primary Groups	Appear under the head	Subgroups	Appear under the head
Branch/Division	Balance Sheet	Bank Accounts	Current Assets
Capital A/c	Balance Sheet	Bank OD A/c	Loans (Liability)
Current Assets	Balance Sheet	Cash in hand	Current Assets
Current Liabilities	Balance Sheet	Deposits (Assets)	Current Assets
Direct Expenses	Profit & Loss A/c	Duties ad Taxes	Current Liabilities
Direct Incomes	Profit & Loss A/c	Loans & Advances (Asset)	Current Assets
Fixed Assets	Balance Sheet	Provisions	Current Liabilities
Indirect Expenses	Profit & Loss A/c	Reserves & Surplus	Capital Account
Indirect Income	Profit & Loss A/c	Secured Loans	Loans (Liability
Investments	Profit & Loss A/c	Stock in hand	Current Assets
Loans (Liability)	Balance Sheet	Sundry Creditors	Current Liabilities
Misc. Expenses (Asset)	Balance Sheet	Sundry Debtors	Current Assets
Purchase Accounts	Profit & Loss A/c	Unsecured Loans	Loans (Liability
Sales Accounts	Profit & Loss A/c		
Suspense A/c	Balance Sheet		

2.2.3 Default Group

1. Capital Account

A Capital Account is a group under which the Owner's capital, Partner's capital, and similar ledger accounts are created to record the amount contributed by the owner or partner to start the business. In the case of companies, this account is shown as shareholder's equity. It also records the retained earnings. In TallyPrime, Groups created under Capital Account record the Capital of the company. The ledgers that belong to Capital Accounts are Share Capital, Partners' Capital A/c, Proprietor's Capital Account, and so on.

2. Reserves and Surplus [Retained Earnings]

Reserves are the amount set aside by the owner to use in the future for buying fixed assets, company expansion, legal requirements, or any investment. The funds are kept aside so that the cash or bank is not used for any of these expenses. On the other hand, a Surplus is an excess of income after all expenses are met. This Group contains ledgers like Capital Reserve, General Reserve, Reserve for Depreciation, and so on.

3. Current Assets

A Current Asset is an asset that a company can easily sell and convert into liquid cash. The Current Assets help to meet the daily business expenses and help to maintain the working capital of the business. There are many subgroups created under this group, like Bank or Cash accounts, Deposits, Loans & Advances, Sundry Debtors, and even stocks.

- ◊ **Bank Accounts:** This subgroup shows all the Bank accounts like Current accounts, savings accounts, short-term deposit accounts, and so on.
- ◊ **Cash-in hand:** In TallyPrime, Cash A/c is a predefined ledger created under this group. You can open more than one cash account, if needed. An account under the Cash-in-Hand group or Bank Accounts/Bank OCC A/c group is printed as a separate Cash Book in the traditional Cash Book format and does not form part of the Ledger.
- ◊ **Deposits (Asset):** Deposits contain Fixed Deposits, Security Deposits, or any deposit made by the company (not received by the company, which is a liability) that the company will get back after its maturity or at the end of the service.
- ◊ **Loans & Advances (Asset):** This records all loans given by the company and advances of a non-trading nature (for example advance against salaries). We do not recommend you to open Advances to Supplier account under this Group. For further details, please refer to the section on Common Errors.
- ◊ **Stock-in-Hand:** This group contains accounts like Raw Materials, Work-in-Progress, and Finished Goods. The balance control depends on whether you have selected the Integrated Account-cum-Inventory option while creating the company. Refer to the Company creation section under the Set Up Your Company topic for more details.

Let us consider these options:

- ◊ **Integrated Accounts with Inventory:** This option has a significant effect on the Balance Sheet and Profit & Loss A/c. When set to Yes, it pulls the stock/inventory balance figures from the inventory records and allows you to drill down to the stock registers from the balance sheet. You are not allowed to directly change the closing balance of an account under this group. You are allowed to pass transactions in Inventory records, and the account balances are automatically reflected in the Balance Sheet as Closing Stock.
- ◊ **Non-integrated Accounts with Inventory:** If Integrate Accounts with Inventory option is set to No, it ignores the inventory book figures and picks up manually entered closing stock balances from the ledger account created. This provides the facility to maintain accounts separately and inventory separately. You are not allowed to pass transactions if your accounts fall under this Group. It allows you to hold opening and closing balances only. Since no vouchers can be passed for these accounts, they are the only accounts for which the closing balances can be directly altered (this can be done with due diligence by a responsible person).

Sundry Debtors: Sundry Debtors are grouped with the persons or company who have bought the goods or services on credit and is liable to pay the business in the future.

4. Current Liabilities

Current Liabilities are obligations that must be paid as soon as they become due. The Current Liabilities are paid by liquidating the Current Assets. Hence, it is important to keep a check on the liability and ensure that the business has sufficient money to pay the liability as and when it becomes due. Accounts like Outstanding Liabilities, Statutory Liabilities, and other minor liabilities can be created directly under this group. Sub-groups under Current Liabilities are Duties and Taxes, Provisions, and Sundry Creditors.

◊ **Duties & Taxes:** Duties & Taxes contain all tax accounts like GST, VAT, CENVAT, Excise, Sales, and other trade taxes and the total liability (or asset in case of advances paid) and the break-up of individual items.

◊ **Provisions:** Accounts like Provision for Taxation, Provision for Depreciation, and so on are recorded under Provisions.

◊ **Sundry Creditors:** Sundry Creditors are grouped with the persons or companies from whom the goods or services are purchased on credit and are liable to receive from the business in the future.

5. Investments

Group your investment accounts like Investments in Shares, Bonds, Govt. securities, long-term Bank deposit accounts, and so on. This allows you to view the total investments made by the company.

6. Loans (Liability)

Loans that a company has borrowed are typically long-term loans.

◊ **Bank OD Accounts [Bank OCC Accounts]**: TallyPrime provides you with distinct types of Bank Accounts. This is used to record the company's overdraft accounts with banks; for example, Bill Discounted A/c's and Hypothecation A/c's, etc.

An account under Bank OCC A/c group is printed as a separate Cash Book in the traditional Cash Book format and does not form part of the ledger.

◊ **Secured Loans:** Term loans or other long/medium term loans obtained against the security of some asset do not verify the existence of the security. Typical accounts are Debentures, Term Loans, and so on.

◊ **Unsecured Loans:** Loans obtained without any security. Example: Loans from Directors/partners or outside parties.

7. Suspense Account

In modern accounting, many large corporations use a Suspense Ledger to track the money paid or recovered, the nature of which is not yet known. The most common example is money paid for Traveling Advance whose details will be known only upon submission of the Travelling Allowance bill. Some companies may prefer to open such accounts under Suspense Account.

The Suspense Account is a Balance Sheet item. Any expense account, even if it has 'suspense' in its name, should be opened under the Revenue group like Indirect Expenses and not under the Suspense Account group.

8. Miscellaneous Expenses (Asset)

This group is typically used for legal disclosure requirements such as Schedule VI of the Indian Companies Act. It should cover incorporation and pre-operative expenses. Companies would write off a permissible portion of the account every year. A balance remains to an extent that cannot be written off in Profit & Loss Account. TallyPrime does not show a loss, carried forward in the Profit & Loss Account, under this group. The balance of the Profit & Loss Account is displayed separately in the Balance Sheet.

9. Branch/Divisions

This maintains ledger accounts for all your company's branches, divisions, affiliates, sister concerns, subsidiaries, and so on. TallyPrime permits Sales and Purchase transactions to take place with accounts opened here. Remember, these are their accounts in your books, not their books of accounts. Just treat them like any other party account. If you wish to maintain the books of a branch or division on your computer, you must open a separate company. TallyPrime allows the maintenance of multiple company accounts.

10. Sales Account

You can classify your sales accounts based on different types of sales.

For example: Domestic Sales, Export Sales

You can even open an account as Sales Returns under the group Domestic Sales to view your net sales after returns (or the returns may be directly passed through Journal against the specific Sales account).

> Do not create customer accounts under this group. For more details, refer to the section on Common Errors.

11. Purchase Account

This is similar to sales accounts, except for the type of transactions.

12. Direct Income [Income Direct]

These are non-trade income accounts that affect Gross Profit. All trade income accounts fall under Sales Accounts. You may also use this group for accounts like Servicing, Contract Charges that follow sales of equipment.

For a professional services company, you may not use the Sales Account group at all. Instead, open accounts like Professional Fees under this group.

13. Indirect Income [Income Indirect]

These are miscellaneous non-sale income accounts; for example, Rent Received and Interest Received.

14. Direct Expenses [Expenses Direct]

These are Manufacturing or direct trading expenses. These accounts determine the Gross Profit of the company.

15. Indirect Expenses [Expenses Indirect]

This group includes all administrative, selling, or non-direct expenses.

Profit & Loss A/c is a reserved primary account in TallyPrime. You can use this account to pass adjustment entries through journal vouchers. For example, transfer of profit or loss account to Capital or Reserve account.

2.2.3.1 Common and Possible Errors in Grouping and Account Classification

Debtor/Creditor classification: Accounts of parties with whom your company is trading should be opened under any of the following groups in TallyPrime (or sub-groups under them):

◊ Sundry Debtors
◊ Sundry Creditors
◊ Branch/Divisions

Sales and Purchase account groups are meant for revenue accounts and are reflected in the Profit & Loss A/c. If you open party accounts under these groups, it becomes difficult to pass sales or purchase voucher transactions.

For example, in a sales voucher transaction entry, you must debit an account, which can be a sundry debtor, branch/division, or even a sundry creditor. Moreover, other facilities like bill-wise allocation and tracking will not be available unless the accounts belong to one of these groups in TallyPrime.

2.2.3.2 Opening two accounts for a same party

In TallyPrime you can classify debtors, creditors, and branch/divisions at your convenience. This helps you in the process of keeping the accounts of a particular group together during display and analysis. Use the classification depending on the most natural group for the party.

For example, parties from whom you buy frequently can be placed under Sundry Creditors, as that is the natural place to look for their account. TallyPrime does not restrict the accounts from having obverse balances. Thus, a Sundry Debtor can have a credit balance depending on the state of his account.

Therefore, you need not open two accounts for the same party – one under Sundry Debtors and another under Sundry Creditors. TallyPrime restricts the opening of two identical ledger accounts. In such cases, you may decide to mark one account as “A & Co – S/Dr” and another as “A & Co – S/Cr”. This will allow you to have two accounts of the same party under two groups, but you will lose the advantage of analysing the net position at a single instance. It is always better to maintain a single account to obtain the best benefits.

Simply adhering to the reserved groups may be sufficient for many organisations. For greater diversity, TallyPrime allows you to create your own groups, either as sub-groups or Primary groups. Groups can be sub-classified to practically an unlimited level, giving you a virtual accounting tree. At the lowest level, of course, it would be the ledger account.

While it is necessary to assign every ledger to a group/sub-group, it is not essential to have your own sub-classification of accounts; you may simply use the reserved groups for grouping your ledger accounts.

2.2.4 Create Groups

You can use multiple ways to create Groups in TallyPrime. You can create a Group on the fly when you are creating a ledger. Otherwise, you can create a Group first, and then record the transaction for the party. As in the case of ledgers, you can import or synchronise the list of Groups, if needed.

Go to Gateway of Tally > Create > Group or Alt+G (Go To) > Create Master > Group.

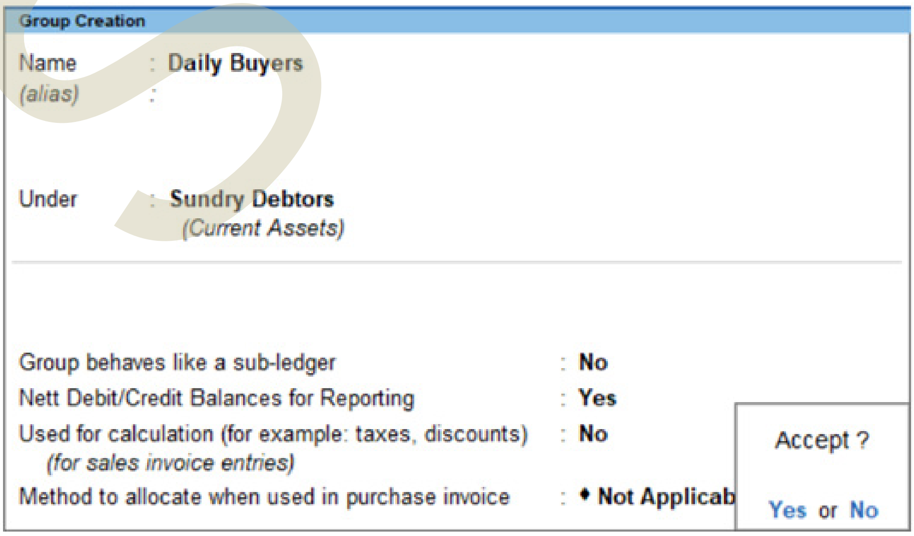

Fig 2.2.1 Group Creation

Enter the name and select the Group under which you want to create this group.

Update the remaining details as needed.

Press Ctrl+A to create the Group.

You can use the Group for any ledger as needed. Similarly, you can create other Groups.

Tip: In TallyPrime, you can accomplish a specific task in different ways, and at different points in time. There are different options to create masters, and these options have similarities. Specific details for each master are captured in the creation screens.

In case you want to enable additional configurations for your Group, as mentioned earlier, press **F12** on the Group Creation screen.

2.2.5 Display or Alter Group

You can view the groups created by you or even the predefined groups one by one.

1. Press Alt+G (Go To) > type or select Chart of Accounts > Group > and press Enter. Alternatively, Gateway of Tally > Chart of Accounts > Group > and press Enter.
2. Select the name of the group required from the List of Groups displayed. The Group Alteration (Secondary) screen appears.

Fig 2.2.2 Group Display

You can view the groups and if required you can alter the details as well.

If you want to alter the details entered in a group, you can do that in the **Group Alteration (Secondary)**.

1. In the **Group Alteration** screen, in the **Under Group** field, select the name of the group required from the **List of Groups** displayed.
2. Make the necessary changes in the **Group Alteration** screen.

3. Accept the screen. As always, press **Ctrl+A** to save the Group Alteration screen.

Similarly, you can alter multiple groups in one go from the **Chart of Accounts** using the **Multi Alter** option.

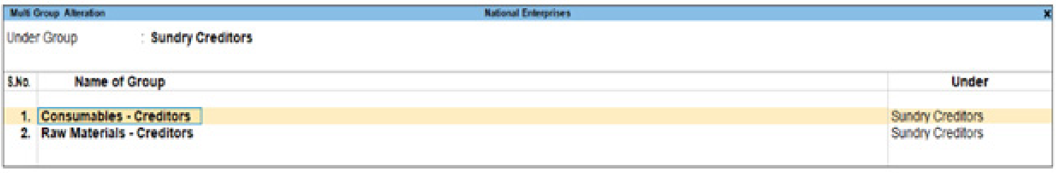

Fig 2.2.3 Group Alteration

2.2.6 Delete a Group

Groups in TallyPrime can be deleted from the alteration screen. It is important to note that you cannot delete groups from the Multiple Group Alteration screens.

To delete a Group one at a time,

◊ From the Group Alteration screen, press Alt+D to delete the Group.

A group cannot be deleted if:

◊ The group has sub-groups.

◊ The group has ledgers classified under it.

◊ The group is a predefined master.

Recap

◊ Groups in TallyPrime help categorise similar ledgers under accounting heads.

◊ These are 28 predefined groups in TallyPrime, including 15 primary and 13 subgroups.

◊ Groups can be created, altered, and deleted based on business needs.

◊ Proper grouping helps in organising ledger accounts and viewing financial statements.

◊ Groups are classified under Assets, Liabilities, Expenses, and Incomes.

Objective Questions

1. How many predefined groups are there in TallyPrime?
2. What is the term for accounting heads in TallyPrime?
3. Under which statement do Groups under Assets and Liabilities appear?
4. What type of group is "Bank Accounts"?
5. Which group is used for recording the owner's capital?
6. Which option allows stock balances to be reflected automatically in the Balance Sheet?
7. Under which group should you create a supplier's account?
8. What is the shortcut key to create a Group in TallyPrime?
9. Which account is a reserved primary account in TallyPrime for adjustment entries?

Answers

1. 28
2. Groups
3. Balance Sheet
4. Subgroup
5. Capital Account
6. Integrated Accounts with Inventory
7. Sundry Creditors
8. Alt+G
9. Profit & Loss A/c

Assignments

1. What are the benefits of using Groups in TallyPrime?
2. Explain the difference between Primary Groups and Subgroups in TallyPrime.

3. How does the "Integrated Accounts with Inventory" option affect the Balance Sheet?
4. Why is it recommended to maintain a single account for a party instead of creating separate debtor and creditor accounts?
5. Create a new Group called "Office Expenses" under the Indirect Expenses group in TallyPrime.
6. Display the Group Summary report for the Sales Accounts group and analyze the information presented.

Suggested Reading

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Unit 3

Create, Display, Alter and Delete Ledger Accounts

Learning Outcomes

Up on the completion of this unit, the learner will be able to:

- ◊ comprehend the concept and key features of a ledger.
- ◊ differentiate between groups and ledgers in Tally software.
- ◊ create, display, alter, and delete ledgers in Tally Prime.

Prerequisites

Anupama had always dreamed of opening her own flower shop. After years of saving, she finally opened "Blooming Wonders" in the heart of her hometown. Excited but overwhelmed, Anupama started managing her business finances. At first, she had been writing sales and expenses in a notebook. Monday: sold ₹200 worth of roses. Tuesday: bought vases for ₹50. Wednesday: purchased ₹150 of tulips from the wholesaler. As days went by, Emma's notebook became cluttered. She struggled to find specific transactions or calculate her total income and expenses. One evening, frustrated after spending hours trying to make sense of her finances, Emma realised she needed a better system. Her friend, an accountant, suggested organising transactions by category. Emma liked the idea and created separate pages for different aspects of her business: "Flower Sales," "Vase Purchases," "Flower Purchases," "Rent," and so on. When Anupama sold roses, she recorded it on the "Flower Sales" page. When she bought vases, it went on the "Vase Purchases" page. This new system made it much easier to track specific areas of her business. These categorised pages were acting as a "ledger account." Each account provided a clear record of all transactions related to a specific aspect of her business. She could now easily see how much she was spending on flowers, how much she was earning from sales, and how her other expenses were adding up. This categorisation not only saved Anupama's time but also gave her valuable insights into her business. She could quickly identify which flowers were selling best, when her expenses were highest, and how her overall profits were trending. Through this experience, Anupama realised the concept of ledger accounts - a systematic way of recording and categorising financial transactions – helped her to better understand and manage her business finances. In this unit, we are going to learn how to create, delete, alter, and display ledger accounts using Tally Prime.

Keywords

Ledger, TallyPrime , Double-entry system, Chart of Accounts, Financial transactions

Discussion

2.3.1 What is a Ledger?

A Ledger records transactions from the journal and forms separate accounts for them in chronological order. It is a date-wise record of all the transactions related to a particular account. Ledgers are crucial sources of financial records. A ledger is formed after the journal and is the secondary step of bookkeeping. After the preparation of the journal, there comes the classification of journal entries into separate accounts, which are posted in the ledger like a cash account, salary account, payable accounts, etc., in chronological order.

2.3.1.1 Key Features of Ledger

1. Organisation: A ledger organises financial data into distinct categories or accounts (like Emma's "Flower Sales" or "Vase Purchases" pages).
2. Completeness: It includes all of a business's financial transactions, providing a complete financial picture.
3. Double-entry system: Each transaction is typically recorded in at least two accounts, maintaining the balance between debits and credits.
4. Chronological order: Transactions within each account are recorded in date

order, creating a timeline of financial activities.

5. Balance tracking: Each account in the ledger keeps a running balance, allowing for a quick assessment of the current financial state.
6. Basis for financial statements: The data in the ledger is used to create important financial documents like balance sheets and income statements.
7. Detailed history: It provides a detailed history of all financial activities, useful for audits, tax preparation, and financial analysis.
8. Categories: A ledger typically includes accounts for assets, liabilities, income, expenses, and equity.

The ledger serves as the central repository of a company's financial data, from which business owners and accountants can extract information to understand the company's financial health, make informed decisions, and prepare official financial reports.

In Anupama's flower shop, her ledger gives her a comprehensive view of her business finances, allowing her to track income, expenses, assets, and liabilities all in one organised system.

A Ledger is the actual account head to which you identify a transaction and must be used in all Accounting Vouchers. All Ledgers have to be classified into Groups. Classifying ledgers according to the appropriate groups is very important. The creation and usage of Groups in Tally has been explained earlier. Now let us learn how Tally works with Ledger. A ledger is a heading used to store the accounting transaction. Ledgers are also called the secondary book of accounts or the second book of entry. It is represented in a tabular double-entry system consisting of the debit and credit sides.

Ledger balancing assists in computing how much assets, liabilities, or revenue is left with the firm at the end of the year. Using this computation, an organisation prepares its financial statements. Many accounting software are used to maintain books of accounts.

2.3.1.2 Components of a Ledger

Ledger is a T-format account where the debit is depicted on the left side, and the credit is depicted on the right side. The columns include date, particulars, journal folio (JF), and amount.

Debit: The debit side of an account represents when the debit increases.

Credit: The credit side of an account represents when the credit increases.

Date: The date on which the transaction takes place.

Particulars: The contra entry of the concerned account according to the double entry system is shown under this head.

Journal Folio: The reference number of the journal entry from the journal.

Amount: It is the amount debited or credited to a particular amount during the transaction.

Table 2.3.1: Format of Ledger

Ledger A/c

Date	Particulars	JF	Amount (₹)	Date	Particulars	JF	Amount (₹)

2.3.2 Predefined Ledgers in Tally

In TallyPrime, there are two predefined ledgers - Cash & Profit and Loss accounts. Apart from the predefined ledgers, you can create as many ledgers as required for your business. You can create the ledgers before recording the transactions. In case you come across a new expense head or a new debtor or creditor while recording the transaction, then you can also create the ledger while you are recording them. Apart from creating a ledger, you can also alter or delete them as per the need. You can also view the Ledger vouchers report in the browser and also view, print, or export the opening balance of all ledgers. In TallyPrime, you also have the option to track changes made to the ledgers through Edit Log. A Ledger typically includes:

1. Ledger Name: A unique name for the account, such as "Cash", "Bank", or "Sales".
2. Ledger Type: The type of account, such as Asset, Liability, Equity, Income, or Expense.
3. Transactions: Debit and credit entries that record financial transactions related to the account.
4. Balance: The current balance of the account, which is the net result of all transactions.

2.3.3 Difference between Group and Ledgers

Groups and Ledgers are two distinct concepts that serve different purposes. Collection of Ledgers is known as Groups. A Group is a broad category or classification that comprises multiple related Ledgers, such as Assets, Liabilities, Equity, Income, and Expenses. It's a way to classify and organize Ledgers into logical categories, making it easier to manage and report on financial transactions. On the other hand, a Ledger is a specific account or record that stores and tracks financial transactions related to a particular asset, liability, equity, income, or expense. Ledgers are the individual accounts that are grouped together under a specific Group. For example, Cash, Bank, and Inventory are Ledgers that fall under the Assets Group. By using Groups and Ledgers, users can efficiently manage their financial accounts, generate accurate reports, and ensure compliance with accounting standards.

Differences between Groups and Ledgers

Aspect	Groups	Ledgers
Definition	Broad categories classifying related Ledgers	Specific accounts recording financial transactions
Scope	Broader, encompassing multiple Ledgers	More specific, focusing on individual accounts
Function	Organize and categorize Ledgers	Record and track detailed financial transactions
Examples	Assets, Liabilities, Equity, Income, Expenses	Cash, Bank, Sales, Purchases, Salaries
Hierarchy	Contain multiple Ledgers	Belong to a specific Group
Purpose	Facilitate overall financial organisation and reporting	Provide detailed transaction records for specific accounts

2.3.4 Creating a Ledger

Once the company is created, you can create ledgers to account for the expenses, incomes, assets and liabilities of your business. In TallyPrime, you can create ledgers one at a time or create ledgers in one go.

1. Press **Alt+G** (Go To) > **Create Master** > type or select **Ledger** and press **Enter**. Alternatively, **Gateway of Tally** > **Create** > type or select **Ledger** and press **Enter**.
2. **Name**: Enter the name of the ledger account you want to create. You cannot create two ledger accounts with the same name.
3. **Alias**: Enter the alias of the ledger account, if required. You can access the ledgers using the original name or the alias name. Alias is the alternate name for the ledger accounts. You can create Alias at the time of creation or also can modify the respective ledger later. While selecting the ledger, you can choose the Alias name and the same ledger account gets selected.
4. **Under**: Enter the group from the List of Groups under which the ledger is created. All the ledgers must be grouped correctly to record the transaction under the proper heads. For example: If you are creating a ledger for Office Expenses, then you need to create the ledger under the Indirect Expenses group. Note: To create a new group from this field, press Alt+C. You can alter a ledger account to change its group classification at any time.
5. Fill in the other necessary details such as Mailing Details, Banking Details and Tax Registration Details.
6. **Opening Balance**: Enter the carry forward balance from the previous year as the opening balance. Opening Balance is applicable when the ledger is an asset or a liability, and also if it has a closing balance in the account at the end of the period.
7. As always, press **Ctrl+A** to save.

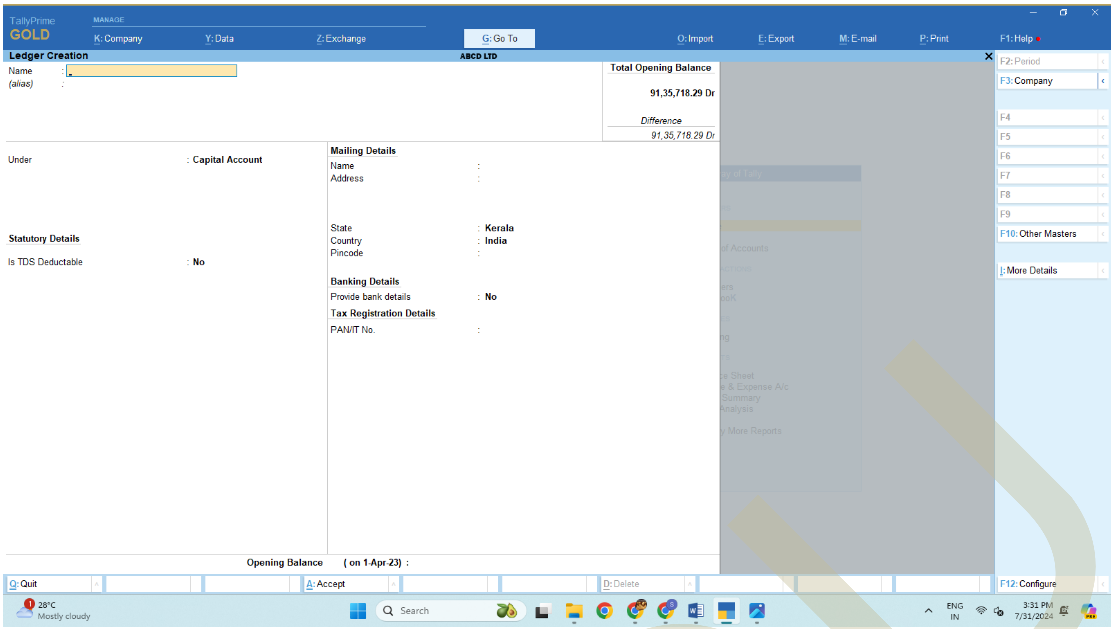

Fig 2.3.1 Ledger creation

A confirmation message will appear asking to create a ledger. Click on "Yes" to confirm.

2.3.5 Display of Ledgers.

The display of ledgers is a comprehensive and organised presentation of ledger accounts, allowing users to easily access and view financial information. Each ledger account is displayed with its name, alias, and opening balance, providing a clear snapshot of the account's status. Additionally, Ledgers are grouped into categories, such as Assets, Liabilities, Income, and Expenses, making it simple to locate and reference related accounts. The Ledger Vouchers screen displays all transactions related to a ledger, including date, voucher type, and amount, giving users a detailed view of account activity. The current balance of each ledger is also prominently displayed, reflecting all transactions and providing a real-time picture of financial positions. Overall, the display of ledgers in Tally enables users to efficiently manage and analyse financial data, making it an essential tool for informed decision-making.

You can view the ledgers by following the steps. You can see the already-created ledgers through the Display of Ledgers Option.

Step I

Gateway of Tally>Accounts info>Ledgers>Display.

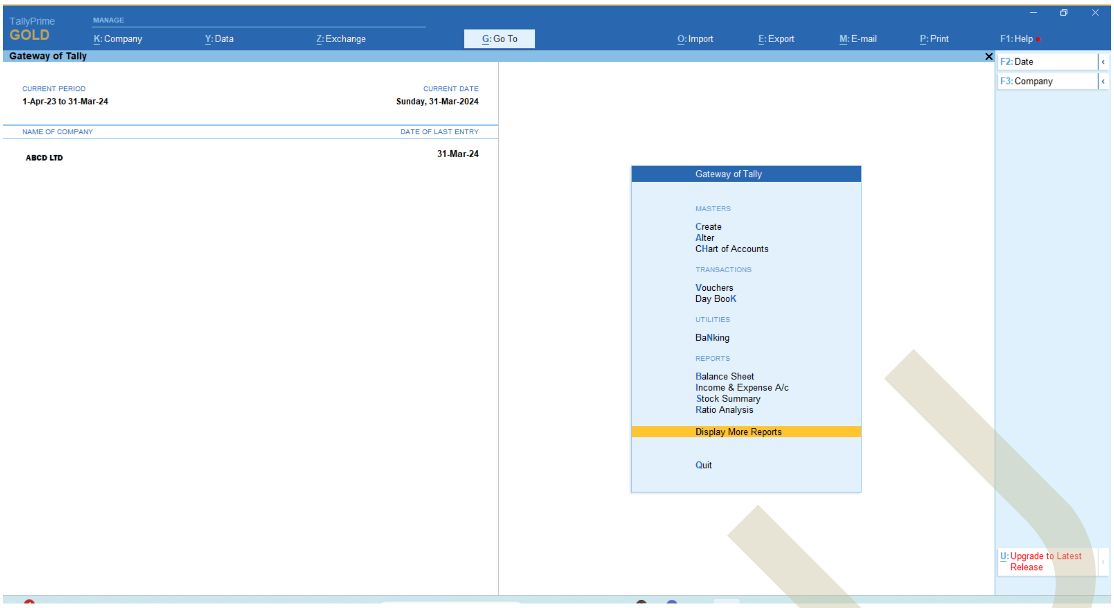

Fig 2.3.2 Display menu

Step II.

Click on "display".

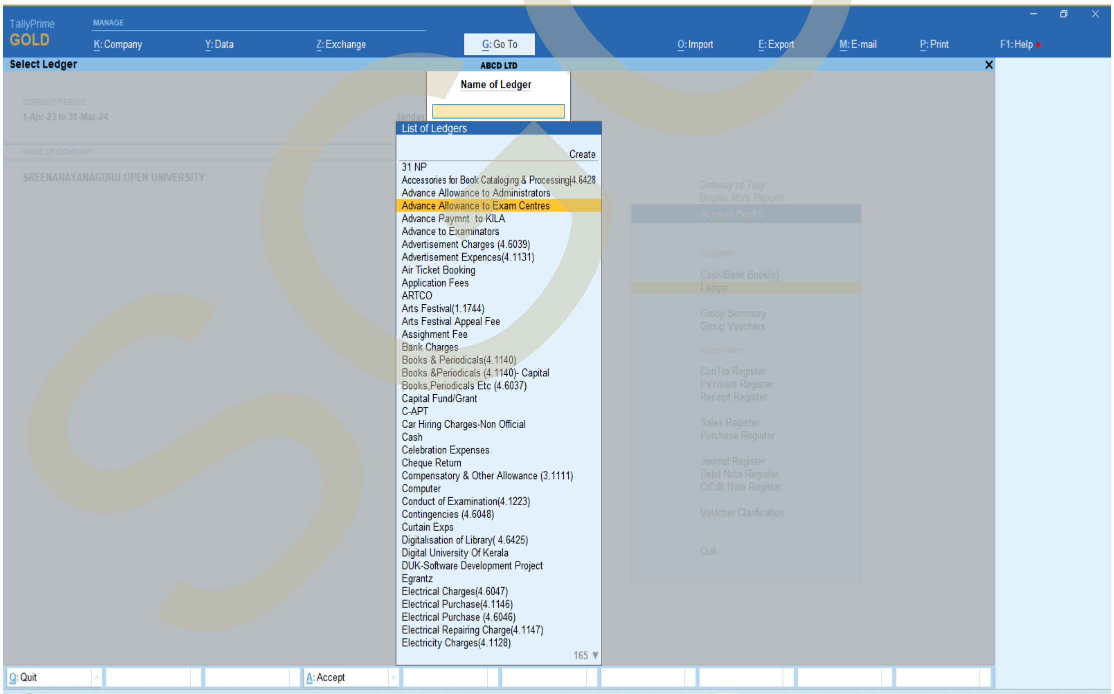

Fig 2.3.3 Displaying the list of Ledgers

2.3.6 Alter the Ledger

After you create the ledgers as per your requirement, you can alter the details of such ledgers. You can even alter the group under which the ledger was created. After you create the ledgers, you may want to update certain details. For instance, you may update GSTIN/UIN or the Mailing Details, based on the information you receive from your customer or vendor. In TallyPrime, you can alter the details in the ledgers and use them as needed. You can alter the ledger one at a time or you can also alter multiple ledgers from the Multi Alter screen in the Chart of Accounts. However, you cannot alter all fields of ledgers through the Multi Alter screen.

1. Press **Alt+G** (Go To) > **Alter Master** > type or select **Ledger** and press **Enter**. Alternatively, **Gateway of Tally** > **Alter** > type or select **Ledger** and press **Enter**. The **Ledger Alteration** screen appears.
2. Alter the details, as required, and save the ledger. You can alter any information provided in the ledger master with the exception of the closing balance under the group Stock-in-Hand.

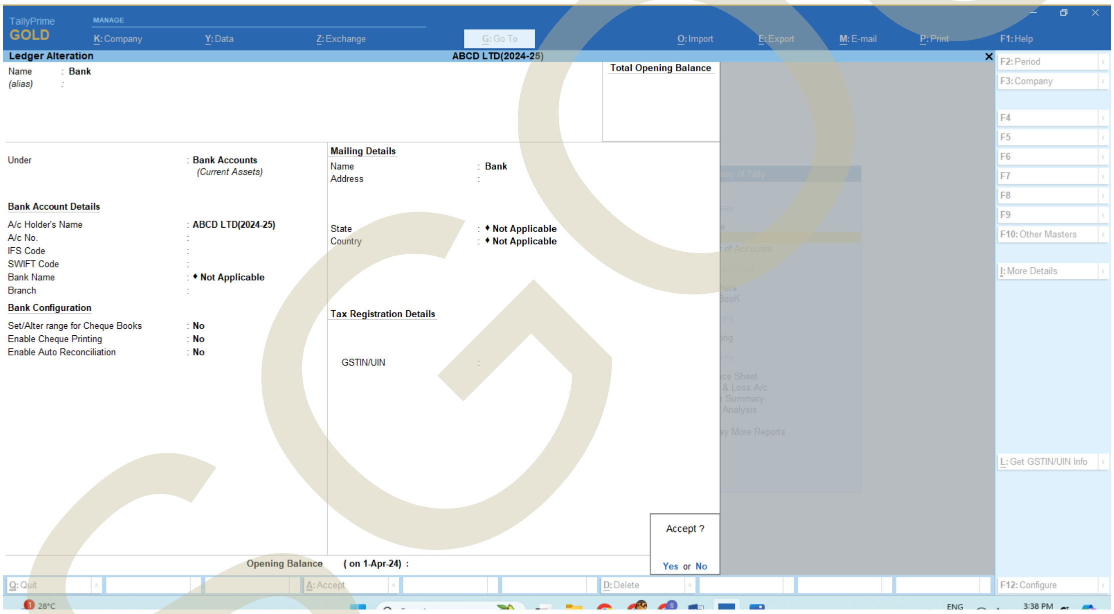

Fig 2.3.4 Alter Accept window

2.3.7 Delete the Ledger

Apart from altering the ledger, you can also delete ledgers which are not required. You can alter or delete ledgers one at a time or in one go. You can alter or delete the ledgers and other masters from the Chart of Accounts as well. Using Chart of Accounts, you can alter multiple masters in one go and delete masters from a single screen.

You can delete ledgers one at a time or delete multiple ledgers from the Chart of Accounts. However, there are certain situations where deleting a ledger has the following dependencies.

- ◊ You cannot delete a ledger that is already used in a voucher. Therefore, you need to first delete all the vouchers related to the ledger and then delete that ledger.
- ◊ You cannot delete a ledger that is referenced in any voucher class, configurations, or other masters. You need to remove the references of the ledger from all such cases, before deleting that ledger.

To delete a ledger one at a time:

- ◊ From the Ledger Alteration screen, press Alt+D to delete the ledger.

Recap

- ◊ A ledger is a secondary book of accounts that records transactions in chronological order.
- ◊ Ledgers are organised into groups like assets, liabilities, income, and expenses.
- ◊ TallyPrime has predefined ledgers (Cash and Profit & Loss accounts) and allows custom ledger creation.
- ◊ Ledgers can be created, displayed, altered, and deleted in TallyPrime.
- ◊ The ledger format includes debit and credit sides, date, particulars, journal folio, and amount.

Objective Questions

1. What is the primary book of accounts called?
2. What does JF stand for in a ledger entry?
3. Which side of a T-account represents debits?
4. What type of system does a ledger typically use?
5. What is the broader category that contains multiple ledgers called?
6. What key do you press to save a ledger in TallyPrime?
7. What is an alternate name for a ledger called?
8. What is the command to go to the ledger creation screen in TallyPrime?
9. Can you create two ledgers with the same name in TallyPrime?
10. What is displayed in the 'Particulars' column of a ledger?

Answers

1. Journal
2. Journal Folio
3. Left
4. Double-entry
5. Group
6. Ctrl+A
7. Alias
8. Alt+G
9. No
10. Contra entry of the concerned account according to the double entry system

Assignments

1. What are the key features of a ledger?
2. How does a ledger differ from a journal?
3. Explain the process of creating a ledger in TallyPrime.
4. What are the components of a ledger and their functions?
5. Create a ledger for "Office Supplies Expense" in TallyPrime, categorizing it under the appropriate group.
6. Alter an existing ledger in TallyPrime to update its mailing address and banking details.
7. Display the list of ledgers in TallyPrime and identify which ones fall under the Assets group.

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Unit 4

Management of Inventory

Learning Outcomes

Upon the completion of this unit, the learner will be able to:

- ◊ grasp the concept of inventory and its importance in business operations.
- ◊ create and manage stock groups and stock items in Tally Prime.
- ◊ comprehend the process of setting up stock units and their significance in inventory tracking.

Prerequisites

Sarah wiped the sweat from her brow as she surveyed the chaos in her small boutique's backroom. Stacks of unsorted clothing teetered precariously, and she couldn't shake the nagging feeling that she was losing track of her inventory. Just yesterday, a customer asked about a particular dress, and Sarah confidently assured her it was in stock only to discover, after 20 minutes of frantic searching, that they had sold out weeks ago. As she stared at the jumble of price tags and sizes, Sarah knew something had to change.

That night, as she locked up the shop, Sarah's eyes fell on an advert for Tally Prime. The promise of effortless inventory management seemed too good to be true, but she was desperate. Little did she know, this moment would mark the beginning of a transformation not just for her boutique, but for her entire approach to running her business. In this unit, we'll follow Sarah's journey as she discovers the power of digital inventory management with Tally Prime. From creating her first stock item to generating comprehensive reports that reveal hidden trends in her sales, we will explore how this powerful tool can turn the daunting task of inventory management into a strategic advantage for businesses of all sizes.

Keywords

Inventory, Stock Group, Stock Item, Units of Measure

Discussion

2.4.1 What is Inventory or Stock?

An inventory is a comprehensive list or record of items owned or controlled by a business or organisation. It serves multiple crucial functions, including asset tracking, stock management, financial reporting, planning, and loss prevention. Inventories typically encompass raw materials, work-in-progress goods, finished products, office supplies, and equipment. The scope and complexity of inventory management can vary widely depending on the size and nature of the business, ranging from simple spreadsheet-based systems to sophisticated software solutions. Maintaining an accurate and up-to-date inventory is essential for efficient operations, financial accuracy, and strategic decision-making in various industries, from retail and manufacturing to healthcare and hospitality.

Manage Stock Items

Does your business involve stock items or inventory in the day-to-day transactions? If so, you certainly need to manage and keep track of all your stocks – how much of them have been sold every day, what is the balance stock, are the stocks moving as per the demand, do you have too much-unused stock and so on. In TallyPrime, you can create as many stock items as you have in the business, specify Units of Measurement (UoM) for each stock item and define tax rates without having to enter these details again during transactions.

Whether you keep your stocks in different groups, batches or godowns based on your business practices, you can find the details of your stock items any way you need. A real-time view of your stock quantity helps to refill your stock in advance to avoid the risk of losing customers, You can also view stock item reports for each group or batch as needed.

Create & use inventory/stock items

Like other masters in TallyPrime, such as ledgers, godowns, stock groups, and so on, you can create stock items by providing a few details. Just enter the name of the stock item and you are done! You can set up details such as Unit of Measurement (UoM) and tax rates any time later. You can also define quantity, rate, and value as the opening balance of your stock.

Once you create a stock item and use it in your transactions, reports in TallyPrime start tracking the stock item – sales or purchase transactions that include that stock item, number of stock items sold from period to period, overall stock position of your business, and so on.

Group your stock items

Having a stock group is not mandatory to create a stock item in TallyPrime. If you have been maintaining your stock items without creating any Stock Group, TallyPrime considers all stock items under an internal group called Primary.

However, if you keep your stock items in different groups depending on any of their common features such as brand, product type, or size, use the Stock Group feature in TallyPrime. For example, stock items made of the same fabric – say synthetic – can be under one stock group and stock items with cotton fabric can be in a different group. This will not only help to organise the stock items but also provide a consolidated view of the stock items with you.

In certain cases, stock items from different groups also have a common property and therefore can be categorised across multiple stock groups, using Stock Categories.

For example, stock items made of synthetic fabric are sold at two different prices – TypeA_Ctt at Rs. 500 and TypeB_Ctt at Rs. 900. Similarly, synthetic stock items are sold as Type1_Syn for Rs. 900 and Type2_Syn for Rs. 500. In such cases, keeping the stock group as is, you can create stock category in TallyPrime to see the pricing wise grouping of stock items at the same time.

The items are classified into Cotton and Synthetic stock groups; at the same time, they are also classified as Items at Rs. 500 and Items at Rs. 900 – the stock categories in this case. Therefore, stock items TypeA_Ctt' and 'Type1_Syn' (which are part of different stock groups) are viewed as part of the stock category – that is 'Items @ Rs. 500'. This also helps you get an insight of how many stock items of a particular price is available or sold at a given time.

Know the stock position of your business

Reports in TallyPrime can provide you details of your stock items in different ways. You can view stock position of your business based on the stock item groups and categories. Like any other reports in TallyPrime, stock item details can further be viewed for different periods, such as daily, weekly, monthly, quarterly or yearly, You can configure your reports to view stock items to each party your business deals with. Knowing the overall stock position of your business helps you to decide if you need to fill in the stock items, if items are moving fast or under a particular period or group and so on.

Inventory/Stock Items

A stock item in TallyPrime requires you to fill in information about the stock or inventory that your business deals with. Once you have created a stock item, you can record your business transactions and keep track of the stock item details. Enter the name of the stock item you want to create and save it. Also, provide the opening balance details such as quantity, rate, value, and applicable tax rates so that you can record transactions in less time without the need to enter all of these details each time in the transactions.

In TallyPrime Edit Log Release 2.1 and TallyPrime Release 2.1 onwards, you also have a facility to track the history of various activities such as creation, alteration, and deletion that affect Stock items. However, you cannot simply delete a stock item that is already used in any transaction or in some other cases like a BOM (Bill of Materials) entry. You will need to first delete all the vouchers and references of the stock item from all such cases before deleting that stock item.

Stock Group

Stock Groups in Inventory are similar to Groups in Accounting Masters. They are helpful in the classification of Stock Items. You can group stock items under different stock groups to reflect their classification based on common features such as brand name, product type, quality, and so on. Grouping enables you to locate Stock Items easily and report their details in statements.

Create Stock Group in Tally Prime

In Tally Prime, the procedure for creating single and multiple stock groups is identical. The software does not distinguish between creating a single stock group or multiple groups; you simply repeat the same process for each group you want to create. This unified approach streamlines the setup process, allowing users to efficiently organize their inventory structure regardless of how many groups they need to establish. Whether you are setting up a single category or building a complex hierarchical structure with numerous groups and subgroups, you will follow the same steps each time, making the process consistent and easy to remember. To create a stock group in Tally Prime, follow these steps:

1. Open Tally Prime and select the company you want to work with.
2. Go to the Gateway of Tally > Masters > Inventory Info > Stock Groups.
3. Click on "Create" or press F2 to create a new stock group.
4. Enter a name for the stock group.
5. Press Enter or click "Yes" to save the stock group.
6. You can continue to create more stock groups or press Esc to exit.

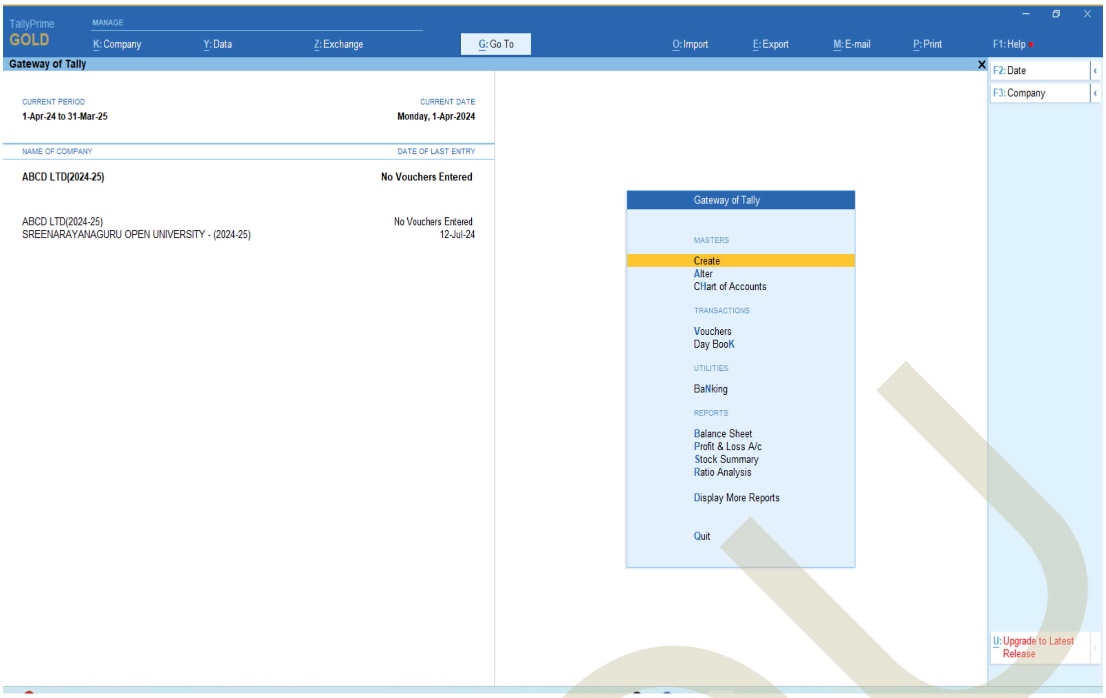

Fig 2.4.1 Click on Create stock group

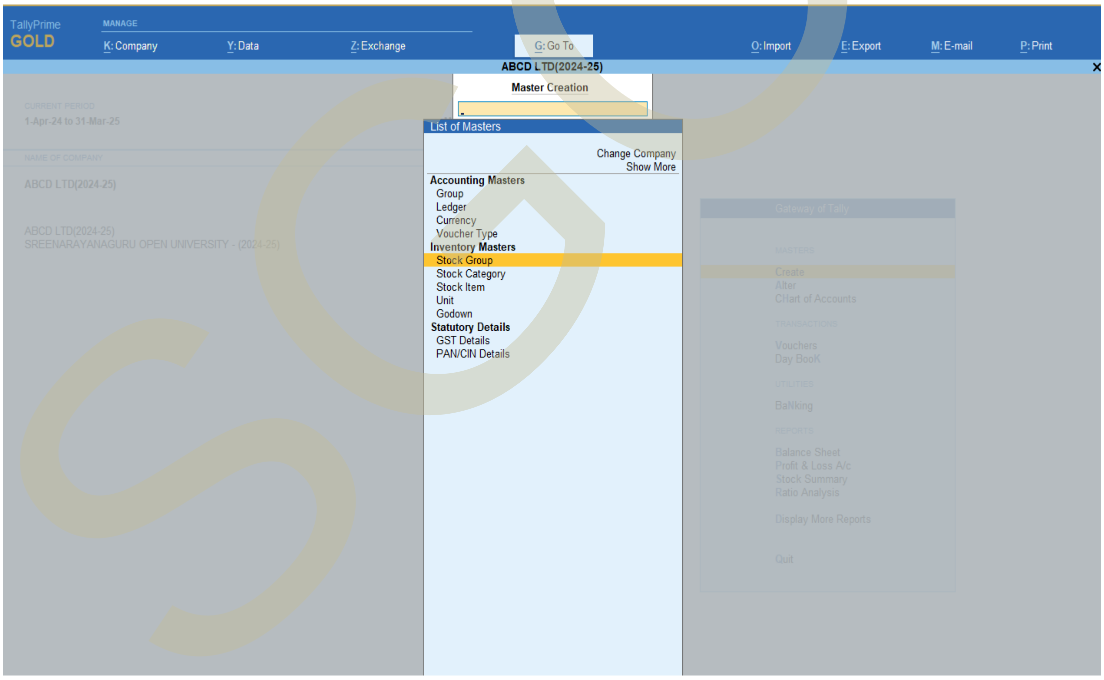

Fig 2.4.2 Click on Stock Group

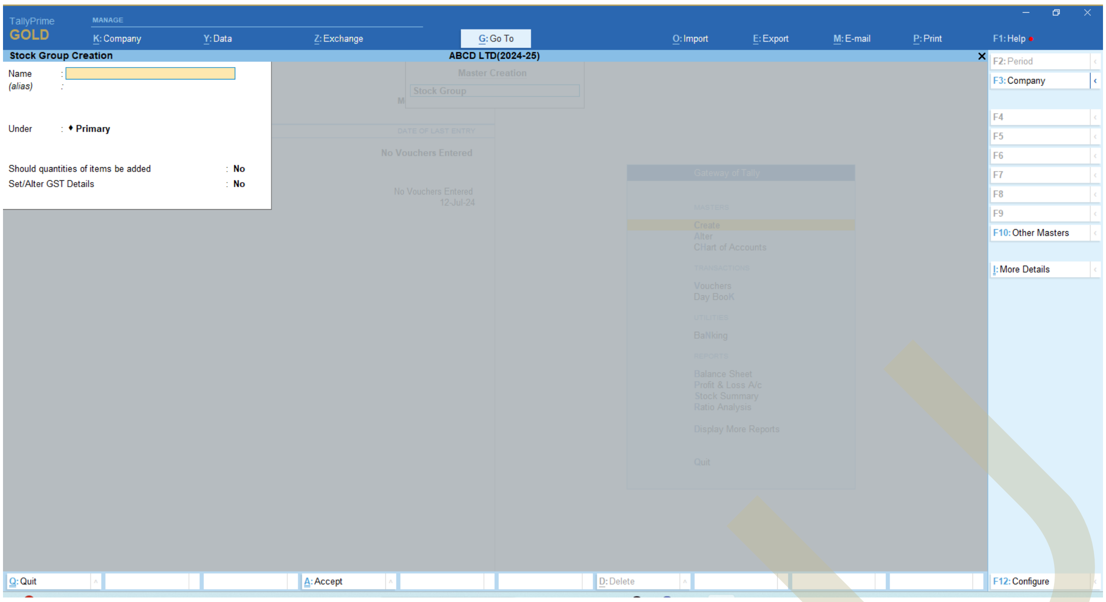

Fig 2.4.3 Confirmation Message to create stock group

A well-organized stock group can significantly improve your inventory management efficiency. Consider your business structure and reporting needs when creating these groups.

Stock Unit Creation in Tally Prime

Stock Unit creation in Tally Prime is an important step in setting up your inventory management system. Here's how to create stock units:

1. Go to Gateway of Tally > Masters > Units of Measure.
2. Press F2 or click "Create" to add a new unit.
3. Enter the symbol for the unit (e.g., "kg" for kilogram).
4. Provide the formal name of the unit (e.g., "Kilogram").
5. If it is a compound unit, you can define its relationship to other units. For example, if creating "dozen":
6. Set "Number of decimal places" to 0.
7. Choose the first unit (e.g., "Nos" for Numbers).
8. Set the conversion as 1 dozen = 12 Nos.
9. Press Enter or click "Yes" to save the unit.
10. You can continue adding more units or press Esc to exit.

Creating accurate stock units is crucial for proper inventory tracking and reporting. Make sure to set up all the units you will need for your various stock items. Please see the figure given below.

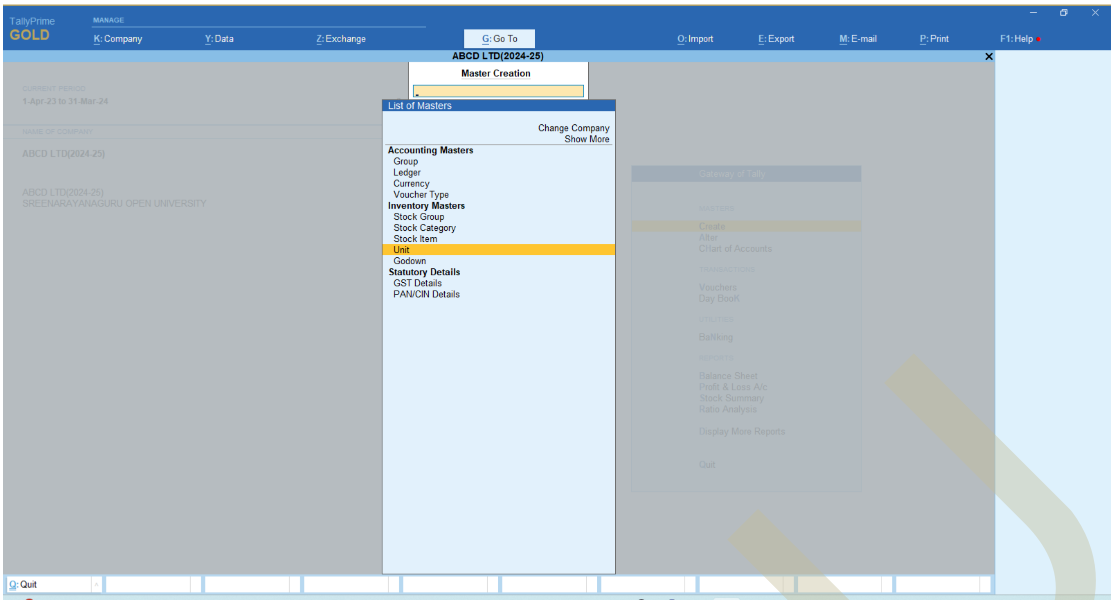

Fig 2.4.4 Click on 'Unit'

Then, you see the following window.

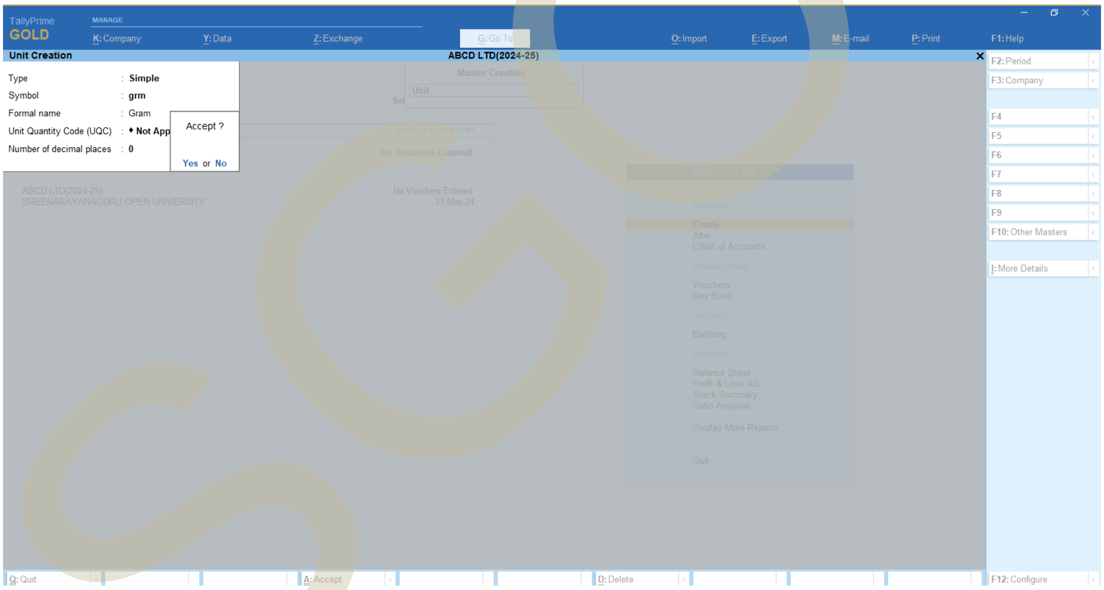

Fig 2.4.5 Accept window

2.4.2 Stock Items

Stock items in Tally refer to the individual products or goods that a business buys, sells, or manufactures, and are tracked and managed within the inventory management system. Each stock item represents a unique product or variant, such as a specific size, colour, or model, and is assigned to a specific stock group or sub-group. Stock items have their own set of attributes, including description, unit of measurement, rate, and opening balance, which are used to track and manage inventory levels, valuations, and movements. By creating and managing stock items, businesses can accurately track their inventory, optimize stock levels, and make informed decisions about production, procurement, and sales. Stock items can be created and customized to suit the specific needs of a business, and can be used to generate reports, analyse inventory performance, and automate inventory-related tasks.

To create stock items in Tally Prime, follow these steps:

1. Go to Gateway of Tally > Masters > Inventory Info > Stock Items.
2. Press F2 or click "Create" to add a new stock item.
3. Enter the name of the stock item.
4. Select the parent stock group under which this item should be categorized.
5. Choose the unit of measurement for the item.
6. Set the opening balance if applicable (quantity and rate).
7. Configure additional details as needed:
    - ◊ GST/Tax details
    - ◊ Alternative units
    - ◊ Batch tracking (if required)
    - ◊ Manufacturing details (for manufactured items)
    - ◊ Reorder levels
8. Press Enter or click "Yes" to save the stock item.
9. You can continue adding more items or press Esc to exit.

This process allows you to create detailed stock items that accurately represent your inventory. Remember to be consistent in how you name and categorize items to make future inventory management easier.

Recap

- ◊ Inventory is a comprehensive list of items owned by a business, crucial for asset tracking and management.
- ◊ Tally Prime allows creation of stock groups for organizing inventory items.
- ◊ Stock items can be created with detailed attributes like unit of measurement, tax details, and opening balance.
- ◊ Stock units are essential for accurate inventory tracking and reporting.
- ◊ Tally Prime provides various reports for analysing stock positions and movement.

Objective Questions

1. What is the internal group name for ungrouped stock items in Tally Prime?
2. What feature in Tally Prime allows categorisation across multiple stock groups?
3. What is the keyboard shortcut to create a new item in Tally Prime?
4. What type of balance is set when creating a new stock item?
5. What does UoM stand for in inventory management?
6. What report helps in deciding when to refill stock items?
7. In which menu can you find the option to create stock groups?
8. What is the term for goods that are partially completed in the production process?

Answers

1. Primary
2. Stock Categories
3. F2
4. Opening balance
5. Unit of Measure
6. Stock position
7. Inventory Info
8. Work-in-progress

Assignments

1. How does grouping stock items benefit inventory management in Tally Prime?
2. Explain the process of creating a unit in Tally Prime.
3. What are the key attributes to consider when creating a stock item in Tally Prime?

4. How does Tally Prime handle the deletion of stock items that have been used in transactions?
5. Create a stock group for "Electronics" with subgroups for "Smartphones" and "Laptops" in Tally Prime.
6. Set up a stock item for a specific model of smartphone, including its unit of measure, opening balance, and tax details.
7. Generate a report showing the stock position of all items in the "Electronics" group for the last quarter.

Suggested Reading

1. Anthropic. (2024). *Claude AI conversation about inventory management in Tally Prime*.
2. Tally Solutions. (n.d.). *TallyPrime user guide: Inventory management*.
3. Smith, J. (2023). *Effective inventory control strategies using Tally software*. Journal of Accounting Technology, 15(2), 45-60.
4. Brown, A. (2022). *Modern inventory systems: From spreadsheets to ERP*. Business Management Review, 8(4), 112-128.

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1. Johnson, L. (2021). *Stock categorization methods in retail: A comparative study*. Retail Management Quarterly, 33(1), 78-95.
2. Davis, M. (2023). *The impact of real-time inventory tracking on business efficiency*. Operations Research Journal, 18(3), 201-215.
3. Wilson, R. (2022). *Inventory valuation methods: FIFO, LIFO, and weighted average in practice*. Accounting Standards Review, 12(2), 156-170.
4. Lee, S. (2023). *Integration of inventory management and financial reporting in ERP systems*. Journal of Information Systems, 29(4), 312-328.
5. Tally Education Private Ltd. (2021). *TallyPrime: Level 1. The Official Book from Tally*, Bengaluru: Sahaj Enterprise
6. Tally Education Private Ltd. (2021). *TallyPrime: Level 2. The Official Book from Tally*, Bengaluru: Sahaj Enterprise

MODEL QUESTION PAPER

SET - 01

SREENARAYANAGURU OPEN UNIVERSITY

QP CODE: ………

Reg. No:……….................
Name ………………...

Third Semester BA Economics Examination
Skill Enhancement Course - 1 - B21EC01SE - Accounting with Tally
(CBCS - UG)
2023 - Admission Onwards

Time: 3 Hours | Max Marks: 70

Section A

(Answer any 10, each carries 1 mark)

(10×1= 10)

1. Define financial accounting.
2. What is an external transaction in accounting?
3. What is the primary focus of the single-entry system in accounting?
4. Which type of business is most likely to use the single-entry accounting system?
5. What are subsidiary books also known as?
6. What is the primary purpose of a cash book in accounting?
7. State one purpose of preparing a Trading Account.
8. What does a balanced Trial Balance indicate?
9. What is the primary function of Tally software?
10. Name any two benefits of computerised accounting.
11. Under which category would you classify 'Sales Accounts' in TallyPrime?
12. What key feature allows you to copy Groups from one company to another in TallyPrime?
13. What does the abbreviation "JF" stand for in a ledger entry?
14. What is the primary book of accounts called before the ledger is formed?
15. What is the keyboard shortcut to create a new item in Tally Prime?

Section B

(Answer any 5, each carries 2 marks)

(5×2=10)

16. Explain the difference between tangible and intangible assets.
17. What is the purpose of the income statement in financial accounting?
18. What are the key elements recorded in a cash book under the single-entry system?
19. Differentiate between a Cash Book and a Journal Proper.
20. What is the significance of the dual nature of a Cash Book in accounting?
21. Explain the difference between a Sales Return Book and a Purchase Return Book.
22. Explain the significance of a Trial Balance in financial accounting.
23. Differentiate between error of principle and error of commission with an example.
24. What steps are involved in setting up the financial year in Tally?
25. What are the predefined ledgers in TallyPrime?

Section C

(Answer any 4, each carries 5 marks)

(4 x 5 = 20)

26. Describe the structure and purpose of a Double-Column Cash Book with an example.
27. Explain the process of recording transactions in the Sales Book, including an example.
28. Compare and contrast the cost efficiency and complexity of the single-entry and double-entry systems.
29. A company recorded a purchase of equipment for ₹10,000, which was paid in cash. Demonstrate the impact of this transaction on the accounting equation (Assets = Liabilities + Owner's Equity).
30. Describe the steps involved in the preparation of a Trial Balance using the balance method.
31. Describe the process of creating a new Group in TallyPrime and mention any important configurations that can be made during this process.
32. Explain the process of creating a new ledger in TallyPrime.

Section D

(Answer any 2, each carries 15 marks)

(2 x 15 = 30)

33. Discuss in detail the process of setting up a stock group for "Electronics" with subgroups for "Smartphones" and "Laptops" in Tally Prime. Include the considerations and steps involved in ensuring efficient inventory management through this setup.
34. Discuss the role and importance of predefined account groups in TallyPrime. How do these groups help in the organisation and management of financial data within a business? Provide examples to support your explanation.
35. Explain Accounting concepts in detail.
36. Prepare a Trading Account for ABC Traders for the year ended December 31, 2023, using the following information:

    Opening stock of goods: ₹45,000

    Purchases during the year: ₹320,000

    Sales for the year: ₹480,000

    Carriage inwards: ₹8,500

    Customs duty on imports: ₹12,000

    Wages paid to factory workers: ₹55,000

    Factory rent and utilities: ₹18,000

    Closing stock of goods: ₹52,000

    Purchase returns: ₹5,000

    Sales returns: ₹7,000

You are required to prepare:

a. Prepare the Trading Account for ABC Traders.

b. Calculate the Gross Profit or Gross Loss for the year.

MODEL QUESTION PAPER

SET - 02

SREENARAYANAGURU OPEN UNIVERSITY

QP CODE: ………

Reg. No:………...............
Name ………………...

Third Semester BA Economics Examination
Skill Enhancement Course- 1- B21EC01SE - Accounting With Tally
(CBCS - UG)
2023 - Admission Onwards

Time: 3 Hours | Max Marks: 70

Section A

(Answer any 10, each carries 1 mark)

(10 x 1 = 10)

1. Name two types of assets.
2. What is a ledger in the context of accounting?
3. In double-entry accounting, what ensures that the accounting equation remains balanced?
4. What are the two aspects of every transaction in the double-entry system?
5. Which subsidiary book records all the credit sales of products made by a company?
6. In which subsidiary book would you record a transaction where goods are returned to a supplier?
7. Define a Trial Balance.
8. What is an error of omission in accounting?
9. Who co-founded Tally Solutions?
10. What is the shortcut key to quit Tally directly?
11. How many predefined groups are there in TallyPrime?
12. What is the primary purpose of Groups in TallyPrime?
13. What key do you press to save a ledger in TallyPrime?
14. What does UoM stand for in inventory management?
15. Which side of a T-account represents debits?

Section B

(Answer any 5, each carries 2 marks)

(5 x 2 = 10)

16. Identify and briefly describe two limitations of accounting.
17. Explain the primary difference between single-entry and double-entry systems.
18. List two advantages of the single-entry system.
19. Briefly describe the concept of closing stock and its role in a Trading Account.
20. Explain the term "Double Entry Accounting" as used in Tally.
21. List two key features of Tally Prime.
22. What are the predefined ledgers in TallyPrime?
23. What is the role of the "Particulars" column in a ledger account?
24. Explain the role of stock categories in Tally Prime.
25. Describe the process of creating a unit of measure in Tally Prime.

Section C

(Answer any 4, each carries 5 marks)

(4 x 5 = 20)

26. How does a company use the Purchase Book, and what are its benefits? Illustrate with an example.
27. Discuss the limitations of the single-entry system for complex businesses.
28. Describe the error detection mechanism inherent in the double-entry accounting system.
29. Explain the process of accounting, including the steps involved from recording to communication.
30. Discuss the advantages of accounting as a decision-making tool for businesses.
31. Discuss the components of a Trading Account and their importance in determining gross profit or loss.
32. Outline the steps to create a stock item in Tally Prime, including the details that need to be configured.

Section D

(Answer any 2, each carries 15 marks)

(2 **x 15 = 30)**

33. Explain in detail how a small business might transition from a single-entry system to a double-entry system. Discuss the advantages this transition could bring to the business.

34. Explain in detail the benefits of computerised accounting as provided by Tally, with examples of how each benefit enhances business operations. Include at least five benefits in your discussion.
35. Discuss in detail the differences between groups and ledgers in TallyPrime, including their purposes and how they are used to manage financial transactions effectively. Provide examples to support your explanation.
36. The following trial balance was extracted from the books of XYZ Corporation as of December 31, 2023:

XYZ Corporation Trial Balance as of December 31, 2023

Account	Debit ($)	Credit ($)
Cash	45,000	
Accounts Receivable	68,000	
Inventory	82,000	
Equipment	150,000	
Accumulated Depreciation - Equipment		30,000
Accounts Payable		35,000
Notes Payable		80,000
Common Stock		100,000
Retained Earnings		55,000
Sales Revenue		480,000
Cost of Goods Sold	290,000	
Salaries Expense	85,000	
Rent Expense	36,000	
Utilities Expense	12,000	
Interest Expense	7,000	
Depreciation Expense	5,000	
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Totals	780,000	780,000

You are required to prepare:

a. Prepare an Income Statement for XYZ Corporation for the year ended 31st December, 2023.

b. Prepare a Balance Sheet for XYZ Corporation as of 31st December, 2023.

സർവ്വകലാശാലാഗീതം

വിദ്യയാൽ സ്വതന്ത്രരാകണം
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സൂര്യവീഥിയിൽ തെളിക്കണം
സ്നേഹദീപ്തിയായ് വിളങ്ങണം
നീതിവൈജയന്തി പാറണം

ശാസ്ത്രവ്യാപ്തിയെന്നുമേകണം
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ബോധരശ്മിയിൽ തിളങ്ങുവാൻ
ജ്ഞാനകേന്ദ്രമേ ജ്വലിക്കണേ

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Accounting with Tally

COURSE CODE: B21EC01SE

ISBN 978-81-973709-0-8

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