

**Purpose or objectives of a Trial Balance :** The Purpose or objectives of a trial balance are explained below :

- 1) Trial Balance enables business firm to detect errors and mistakes, if any committed in the books of accounts.
- 2) Trial Balance enables the businessman to know the final balance of any ledger account.
- 3) Trial Balance is itself a tool to test arithmetical accuracy of business transactions recorded in the books of accounts.
- 4) Trial Balance gives a very concise and convenient summary of the various accounts spread all over the ledger. It also gives the net position at a glance.
- 5) While preparing Trial Balance, we come to know how far double entry principles have been followed.
- 6) It provides a base for the preparation of final accounts.
- 7) It also provides a base to draw conclusions by comparing trial balances of the past with the present.
- 8) It is usually assumed that recording, posting and balancing of all records are correct if the total of debit column and credit column of trial balance tallies.

Hence, when you are asked to prepare a Trial Balance from a given list of balances and it is not clearly indicated whether a particular account has a debit balance or credit balance, you will first have to determine the nature of each balance. In this exercise your knowledge of rules of debit and credit should help you. For example, you are aware that in case of nominal accounts all expenses and losses are debited and all income and gains are credited. Hence, accounts like salaries, wages, etc. will show debit balances and the accounts like interest received, discount received, etc., will show credit balances. Similarly, you know the rules of real and personal accounts. The accounts of assets like cash in hand, machinery, etc., will show debit balances and accounts like capital, creditors, etc., will show credit balances. For convenience, however, a few guidelines may help you to determine quickly the nature of each balance. They are :

- a) All accounts of expenses (including purchases) and losses will be a debit balances.
- b) All accounts of incomes (including sales) and gains will be credit balances.
- c) All accounts of assets will be debit balances.
- d) All accounts of liabilities will be credit balances.
- e) Capital Account will normally be a credit balance.



**Form of Trading Account :** To ascertain the gross profit we have to prepare Trading Account. The Trading Account, like any other account in the ledger, has two sides – debit and credit. The opening stock, purchases (less returns) and all direct expenses are shown on the debit side of the Trading Account while sales (less returns) and the closing stock on the credit side. The gross profit appears as the last item on the debit side which, in fact is the excess of the total of credit side over the total of debit side. If however, the total of the debit side exceeds the total of the credit side, it will be treated as gross loss. This is shown as the last item on the debit side of the Trading Account. The gross profit/gross loss thus worked out is transferred to the Profit and Loss Account. Look at the figure below for the form of Trading Account.

**Figure**  
**Form of Trading Account**  
**Trading Account of .....**  
**(Day, Month and Year)**

<b>Dr.</b>		<b>Cr.</b>	
Particulars	Amount	Particulars	Amount
	Rs.		Rs.
To Opening Stock	.....	By Sales	.....
To Purchases	.....	Less Sales	
Less Purchases	.....	Returns	.....
Returns	.....		-----
	.....	By Closing Stock	.....
To Direct Expenses	.....	By Gross Loss	.....
(specify individually)	.....	(transferred to	
To Gross Profit	.....	Profit and Loss	
(transferred to		Account)	
Profit and Loss	.....		
Account)	.....		
	-----		-----
	.....		.....
	-----		-----

## **Some Important Points**

- 1) Purchases :** This item refers to the goods purchased for resale and includes both cash and credit purchases. The purchases of assets which are meant for permanent use in business such as machinery, furniture, etc., are not included in the purchases. The amount taken to Trading Account will be the net amount of purchases (after deducting purchase returns/returns outwards). If the proprietor has taken away some goods from the business for his personal use, the same should also be deducted from the total purchase.
- 2) Sales :** It includes both cash and credit sales of goods and refers to the net amount of sales (after deducting sales returns-returns inwards). Sales of old furniture, car, machinery, etc. are not included in the sales. Similarly, sales of old newspaper etc. are also excluded from sales. Such items are shown as miscellaneous income in the Profit and Loss Account.
- 3) Wages :** Wages are usually treated as income as a direct expense and so shown in the Trading Account. The difficulty arises when wages are clubbed with salaries (an indirect expense) and the Trial Balance includes a single amount for "Wages and Salaries". In such a situation, the amount may be shown in the Trading Account. It is based on the assumption that the item includes the salaries of the supervisory staff in the factory itself. But, if the item in the Trial Balance reads "Salaries and Wages" it will be taken to the Profit and Loss Account on the assumption that the item includes wages of the office staff only. It should be noted that wages paid in connection with the purchases of fixed assets or the construction of building should not be charged to Trading Account. They are to be included in the cost of the concerned fixed asset. There is another important aspect in relation to wages which must be clarified. If a Manufacturing Account is prepared the wages paid to the factory labour is debited to Manufacturing Account.
- 4) Freight, Carriage and Cartage :** When paid in connection with purchases of goods, they are shown in the Trading Account. Such freight and carriage are also termed as "Freight Inwards" and "Carriage Inwards" respectively. "Freight Outwards" and "Carriage Outwards" relate to sales and therefore taken to the debit of Profit and Loss Account.
- 5) Royalties :** Royalties refer to the payments made for the use of copyright or a patent. The amount of royalty is generally based on the quantity produced. It is, therefore, treated as a direct expense and charged to Trading Account. But if it is calculated on the basis of quantity sold as in the case of books, it is shown in the Profit and Loss Account. Royalties are also paid

to the Government for extraction of minerals such as coal, diamond, gold, etc. These are charged to the Profit and Loss Account of the mining companies.

### Profit and Loss Account

After ascertaining the gross profit/gross loss by preparing the Trading Account, the businessman proceeds to prepare the Profit and Loss Account in order to work out the net profit/net loss. You know the net profit is the excess of gross profit and other incomes over the indirect expenses and losses. So, while preparing the Profit and Loss Account we show gross profit and other incomes such as rent received, discount received, commission received, interest and dividends, etc. on the credit side, and all indirect expenses and losses on the debit side. Indirect expenses include all administrative, selling and distribution expenses such as salaries, rent and taxes, postage and stationery, insurance, depreciation, interest paid, office lighting, advertising, packing, carriage outwards, etc. while losses refer to items like loss by fire, loss by theft, etc. The difference between two sides of the Profit and Loss Account represent either the net profit or net loss. If the total of the credit side is higher than the total of the debit side, the difference is called the net profit and if the debit side total exceeds the credit side total, the difference is called net loss. The net profit/net loss belongs to the proprietor and is therefore transferred to his Capital Account. Look at figure below. It shows various expenses, losses, incomes, etc. which usually appear in the Profit and Loss Account.

**Figure**  
**Profit and Loss Account** .....  
**for the year ended** .....

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
To Gross Loss, if any, (transferred from Trading Account) To Salaries To Rent, Rates and Taxes To Postage and Telegrams To Telephone Charges To Printing and Stationery To Legal Expenses		By Gross Profit (transferred from Trading Account) By Interest Received By Discount Received By Rent Received By Commission Received By Dividend Received By Other Incomes and	

<b>To Insurance</b> <b>To Office Lighting</b> <b>To Bad Debts</b> <b>To Depreciation</b> <b>To Advertising</b> <b>To Travelling Expenses</b> <b>To Carriage Outwards</b> <b>To Trade Expenses</b> <b>To Discount Allowed</b> <b>To Interest Paid</b> <b>To Repairs and Renewals</b> <b>To Loss by Fire</b> <b>To Loss by Theft</b> <b>To Other Expenses and Losses, if any</b> <b>To Net Profit</b> <b>(transferred to Capital Account)</b>		<b>Gains</b> <b>By Net Loss</b> <b>(transferred to Capital Account)</b>	
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The Profit and Loss Account shown in the Tally Prime, Tally 9, Tally. ERP 9 software or any accounting software is actually The Trading and Profit and Loss Account. Thus, our Profit and Loss Account or Trading and Profit and Loss Account will display the balances in the above way.

**Balance Sheet :-** After ascertaining the net profit or net loss by preparing the Trading and Profit and Loss Account, the final step in preparing final accounts is the preparation of Balance Sheet. The purpose of Balance Sheet is to ascertain the financial position of a business i.e., to know what the business owes and what it owns on a certain date. Hence it shows all assets and liabilities of the business of the business as at the end of the accounting year.

As we know that final accounts are prepared from the Trial Balance. All items of expense and income appearing in Trial Balance are transferred to the Trading and Profit and Loss Account. The remaining items which represent the balances of personal and real accounts are shown in the Balance Sheet. The accounts showing debit balances represent assets and those showing credit balances represent liabilities.

Look at figure below and note how various assets and liabilities appear in the Balance Sheet.

**Figure**  
**Balance Sheet of** .....  
**as on** .....

<b>Liabilities</b>	<b>Amount</b>	<b>Assets</b>	<b>Amount</b>
<b>Current Liabilities</b>	<b>Rs.</b>	<b>Current Assets</b>	<b>Rs.</b>
Bank Overdraft	.....	Cash in Hand	.....
Bills Payable	.....	Bills Receivable	.....
Sundry Creditors	.....	Cash at Bank	.....
		Sundry Debtors	.....
		Closing Stock	.....
<b>Long-term Liabilities</b>		<b>Investments</b>	.....
Loan	.....	<b>Fixed Assets</b>	.....
Mortgages	.....	Vehicles	.....
<b>Capital</b>		Furniture	.....
Balance	.....	Plant & Machinery	.....
Add Net	.....	Land & Buildings	.....
Profit	.....	Goodwill	.....
Less	.....		.....
Drawings	.....		.....
	.....		.....
	.....		.....
	.....		.....

**Notes या Accounts को कुछ कण्टे :-**

- 1) Profit and Loss या Balance Sheet की information details देखने के लिए "Alt + F1" press कर। पहले जैसी अवस्था में वापस आने के लिए फिर से "Alt + F1" press कर।
- 2) Friends & Relatives को Unsecured Loans में इसलिए रखते हैं क्योंकि ये पैसे डूब नी सकते हैं। ये अपन Capital Accounts को जैसे रहते है।
- 3) कमी नी जब Transaction में Purchase या Sale cash में की गई हो तो Party के नाम का Account create नहीं करना है।
- 4) जैसे हमारा nick name होता है वैसे ही है alias.

5) Accountant का काम Data Entry Operator जैसा होता है। वो बस Accounts Entry करता है बाकि Final Accounts C.A देखता है। इसलिए Accounts entry करते समय कुछ गलती से भी जाय तो tension नहीं लेना।

6) Credit Sale/Credit Purchase की Entry करते वक़्त सदा "New Ref" में डालना है। अगर Debtor part payment कर रहा हो तो "On Account" में डालना है।



### Problem 1

- 1) Mr. Vinzy started business with capital of Rs. 5,00,000.
- 2) Cash sale of Rs. 15,930.
- 3) Cash purchase of Rs. 8,862.
- 4) Paid Hamali Expenses of Rs. 500.
- 5) Paid Rent Expenses of Rs. 3,000 by cheque.
- 6) Purchased material from A to Z Mobiles of Rs. 1,51,356.
- 7) Paid rent to Landlord/Shop owner Prakash Sharma in advances Rs. 150.
- 8) Sold goods to Sai Krupa Mobile Shop of Rs. 1,58,298.
- 9) Sent money order to Radhika of Rs. 8,000.
- 10) Received Commission of Rs. 500.
- 11) Paid for Income-Tax Rs. 2,000.
- 12) Drawings of Rs. 700.
- 13) Received Rs. 1,00,000 from Sai Krupa Mobile Shop as part payment through cheque.
- 14) Received cash Rs. 58,298 from Sai Krupa Mobile Shop in full settlement of his account.
- 15) Paid Commission of Rs. 300 to Mr. Vijay for selling goods.
- 16) Goods withdrawn by Proprietor (Drawings) for personal use Rs. 295.

### Ledger Creation :-

- 1) Name :- Proprietor's /Partner's (Vinay)  
Under :- Capital Account.
- 2) Name :- Sales A/c  
Under :- Sales Accounts
- 3) Name :- Purchase A/c  
Under :- Purchase Accounts
- 4) Name :- Hamali Expense  
Under :- Indirect Expense
- 5) a) Name :- Rent Expense  
Under :- Indirect Expense  
b) Name :- Punjab National Bank  
Under :- Bank Accounts

- 6) Name :- A to Z Mobiles  
Under :- Sundry Creditors
- 7) Name :- Rent (Prepaid)  
Under :- Deposits (Assets)
- 8) Name :- Sai Krupa Mobile Shop  
Under :- Sundry Debtors
- 9) Name :- Postage and Courier Expense  
Under :- Indirect Expense
- 10) Name :- Commission Received  
Under :- Indirect Incomes
- 11) Name :- Income-Tax  
Under :- Capital Accounts
- 12) Name :- Drawings  
Under :- Capital Accounts
- 15) Name :- Commission Expense  
Under :- Indirect Expense

### Voucher Entries

Sr. No.	Function Keys	Particular	Debit Rs.	Credit Rs.
1	F6	Cr. Vinay Dr. Cash Narration :- started business	5,00,000.00	5,00,000.00
2	F8	Cr. Sales A/c Cr. Central Tax Cr. State Tax Dr. Cash Narration - Rec No. & Tax Invoice No	15,930.00	13,500.00 1,215.00 1,215.00
3	F9	Dr. Purchase Dr. Central Tax Dr. State Tax Dr. Rounding off Cr. Cash Narration - Rec No & Inv No	7,510.00 675.90 675.90 0.20	8,862.00

4	F5	Dr. Hamali Expenses Cr. Cash Narration :- Rec. No.	500 00	500 00
5	F5	Dr. Rent Expenses Cr. Punjab National Bank Narration :- Chq. No. paid for rent	2,500 00	2,500 00
6	F9	Dr. Purchase Dr. Central Tax Dr. State Tax Dr. Rounding off Cr. A to Z Mobiles Narration :- Rec. No. & Inv. No.	1,28,222 68 11,566 53 11,566 53 0 26	1,51,356 00
7	F5	Dr. Rent (Prepaid) Cr. Cash Narration :- Rec. No. , rent paid in advance to Landlord/Shop owner	150 00	150 00
8	F8	Cr. Sales A/c Cr. Central Tax Cr. State Tax Dr. Sai Krupa Mobile Shop Narration :- Rec. No. & Tax Invoice No	1,58,298 00	1,34,100 00 12,099 00 12,099 00
9	F5	Dr. Postage and Courier Expenses Cr. Cash Narration - Rec. No. , of Posts and Telegraphs Office of the city where money-order was done	8,000 00	8,000 00
10	F6	Cr. Commission (Recd) Dr. Cash Narration - Voucher No	500 00	500 00
11	F5	Dr. Income-Tax Cr. Cash Narration - challan no	2,000 00	2,000 00
12	F5	Dr. Drawings	700 00	

		Cr. Cash Narration :- cash withdrawn for personal use		700.00
13	F8	Cr. Sai Krupa Mobile Shop Dr. Punjab National Bank Narration :- Chq No.	1,00,000.00	1,00,000.00
14	F8	Cr. Sai Krupa Mobile Shop Dr. Cash Narration :- Chq No.	58,298.00	58,298.00
15	FS	Dr. Commission Expenses Cr. Cash Narration :- Paid commission to salesman Vijay	300.00	300.00
16	FS	Dr. Drawings Cr. Purchase Cr. Central Tax Cr. State Tax Narration :- goods withdrawn for personal use	295.00	250.00 22.50 22.50

**Notes :-1) Income Tax :-** It is the tax payable by a person on his income. In the case of a sole trading concern, the tax paid by the proprietor on the profits of the business is treated as a personal expense. Hence, it should be added to drawings or directly deducted from capital.

**Difference between GST and Income Tax :** The main difference between GST and Income Tax is, GST is levied on consumption of goods and services whereas Income Tax is levied on income earned in a financial year. In way of collecting the tax, GST is the indirect tax paid to the government whereas Income Tax is the direct tax paid to the government.

**2) Transactions with the Proprietor :-** The business and its proprietor are separate entities. This means that separate accounts must be maintained in the ledger for recording transactions between proprietor and the business. Usually, two accounts viz, Capital Account and Drawings Account are maintained for this purpose. Whatever the proprietor brings into the business is treated as his capital and credited to his Capital Account. Similarly, when

he withdraws cash from the business for his personal use, he is to be debited with the amount withdrawn by him. Such a debit is given to his Drawings Account. Drawings Account is also debited when the proprietor takes goods from business for domestic use. Note that the proprietor can be charged only by the cost of goods taken and not its selling price. In practice, the cost of such goods are credited to the Purchases Account because it is assumed that it was purchased for him and should therefore be excluded from the purchases for the business.

- 3) **Transactions relating to Expenses and Incomes :** Expenses and incomes are generally paid/received in cash. So in case of expenses, we debit the concerned expense account and credit cash account. In case of incomes, we debit cash account and credit the concerned income account.

In above Transaction 7, rent was paid to Landlord/Shop owner, but debit has been given to the nominal account (Rent Account) and not to the personal account of Landlord/Shop owner. Similarly, when commission was received (10<sup>th</sup> Transaction) Commission Received Account has been credited and not the personal account of the giver, whosoever he may be. This is so because these are cash transactions and no debtor/creditor relationship is created as there is no obligation yet to be fulfilled.

There is another point to be noted in this context. In Transaction 7<sup>th</sup>, we have seen that when rent is paid, Rent Account has been debited (it is an expense) and when Commission is received, Commission Received Account has been credited (it is an income). In business, certain nominal accounts like Salaries Account, Wages Account and Postage Account would involve only payments, as these will always be expenses. But certain other items like interest, commission, rent, etc., can sometimes be an expense, sometimes an income. In such case, it is better to maintain separate accounts for their payments and receipts.

Note 1) Cash is calculated as follows :-

Dr T1—5,00,000 - + T2—15,930 - + T10—500 - + T14—58,298 - + 1.16 =  
5,74,729.16 (Total) [where T stands for Transaction ]

Cr T3—8,862 - + T4 500 - + T9—8,000 + T11,12—2000 - + 700 - + T15—300 - +  
2189 - = Rs 22,551 - (Total)

Therefore Total Dr – Total Cr = 5,74,729.16 – 22,551 = Rs. 5,52,178.16.

2) Sales is calculated as follows :-

T2—15,930/- + T8—1,58,298/- = Rs.1,74,228/- (Total).

3) Purchase is calculated as follows :- T3—8,862/- + T6—1,51,356/- =  
Rs.1,60,218/- (Total).

Trial Balance will show the above balances of accounts in this way :

Sr.No	Particulars	L.F	Vinay & Co. 1-Aug-2020 to 31-Aug-2020	
			Closing Balance	
			Debit	Credit
1	Capital Account		2,995.00	5,00,000.00
	Drawings		995.00	
	Income-Tax		2,000.00	
	Vinay			5,00,000.00
	Current Liabilities			1,51,356.00
	Duties and Taxes			
	Sundry Creditors			1,51,356.00
	A to Z Mobiles			1,51,356.00
4	Current Assets		6,49,178.16	
	Opening Stock			
	Sundry Debtors			
	Cash-in-Hand		5,52,478.16	
	Bank Accounts		97,000.00	
5	Sales Accounts			1,47,600.00
	Sales A/c			1,47,600.00
6	Purchase Accounts		1,35,482.68	
	Purchase A/c		1,35,482.68	
7	Indirect Incomes			500.00
	Commission (Received)			500.00
8	Indirect Expenses		11,500.16	
	Hamali Expense		500.00	
	Postage and Courier Expense		8,000.00	
	Rent Expense		3,000.00	
	Rounding Off		0.16	
	Grand Total		7,99,456.00	7,99,456.00

Note :- After pressing "Enter" Key we can look the details of the groups whose figures are red coloured. Please do not count the red coloured figures, they are for understanding only.

**Profit and Loss Account of Vinay & Co.**

**for 31<sup>st</sup> Aug 2020 (displays upto the last transaction of the year)**

Dr.		Cr.	
Particulars	Amount	Particulars	Amount
	Rs.		Rs.
<b>Opening Stock</b>		<b>Sales Accounts</b>	
Stock @ 18%		Sales A/c	1,47,600.00
Stock @ 28%			55,996.84
<b>Purchase Accounts</b>	1,35,482.68	<b>Closing Stock</b>	
Purchases A/c	1,35,482.68	Stock @ 18%	55,732.00
		Stock @ 28%	264.84
<b>Gross Profit c/o</b>	68,114.16		2,03,596.84
	2,03,596.84		68,114.16
<b>Indirect Expenses</b>	11,500.16	<b>Gross Profit b/f</b>	500.00
Hamali Expenses	500.00	<b>Indirect Incomes</b>	
Postage and Courier	8,000.00	Commission (Recd.)	500.00
Rent Expense	3,000.00		
Rounding Off	0.16		
<b>Nett Profit</b>	57,114.00		
<b>Total</b>	68,614.16	<b>Total</b>	68,614.16

**Balance Sheet of Vinay & Co.**  
**as on 31<sup>st</sup> Aug 2020**

<b>Liabilities</b>	<b>Amount</b>	<b>Assets</b>	<b>Amount</b>
<b>Capital</b>	<b>4,97,005.00</b>	<b>Current Assets</b>	<b>7,05,475.00</b>
Drawings                    (-)995.00		Closing Stock            55,996.84	
Income Tax                (-)2,000.00		Deposits (Asset)	
Vinay <u>5,00,000.00</u>		Sundry Debtors	
<b>Loans Liability</b>		Cash in Hand            5,52,478.16	
		Bank Accounts <u>97,000.00</u>	
<b>Current Liabilities</b>	<b>1,51,356.00</b>		
Duties and Taxes			
Sundry Creditors <u>1,51,356.00</u>			
<b>Profit and Loss Account</b>	<b>57,114.00</b>		
Opening Balance			
Current Period <u>57,114.00</u>			
<b>Total</b>	<b>7,05,475.00</b>	<b>Total</b>	<b>7,05,475.00</b>