

PREPARATION OF TRADING AND PROFIT & LOSS A/C AND BALANCE SHEET WITH ADJUSTMENTS

21.1 INTRODUCTION

You have already learnt that Trading, Profit and Loss A/c and Balance Sheet are the two financial statements. Trading and Profit & Loss A/c reveals the results (Profit or Loss) of the business for a specific period of time and Balance Sheet presents the financial position of business on a specific date. It has also been explained that these statements are prepared on the basis of Trial Balance. It is quite possible that after preparing the Trial Balance we come across certain items of income or expenses which do not pertain to the accounting period in reference. On the other hand there may be certain income or expenses which accrue during the concerned accounting period but have not been accounted for. It is important that all such items are incorporated in the financial statements otherwise the results reflected would be misleading. Since these items are to be incorporated after the finalisation of Trial Balance these are called adjustments. The present lesson deals with some of the adjustments and their incorporation.

21.2 OBJECTIVES

After studying this lesson you will be able to:

- recall the objectives of preparing Trading and Profit and Loss A/c and Balance Sheet.
 - recognise the need for adjustments.
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- explain the adjustments : closing stock, depreciation, additional bad debts, provision for Bad and Doubtful Debts, outstanding expenses, prepaid expenses, accrued income and unearned income.
- incorporate the adjustments in Trading and Profit and Loss A/c and Balance Sheet.

21.3 NEED FOR ADJUSTMENTS

You have already learnt that Trading and Profit & Loss A/c and Balance Sheet are the financial statements which are prepared at the end of an accounting period. Trading A/c shows the profit earned out of trading activities. In the debit side of Trading A/c, Opening stock of goods, purchases and direct expenses are shown. The credit side of this account shows the sales revenue and value of unsold or closing stock of goods. If the total of credit side is greater than the total of debit side, the difference is known as Gross Profit. In case total of debit side exceeds total of credit side, the difference is known as Gross Loss. The balance of Trading A/c is transferred to Profit and Loss A/c. Various expense accounts relating to carrying on of business and selling and distribution of goods are posted to the debit side of this account. Likewise all other items of income and gains are shown in the credit side of this A/c. Like Trading A/c, if the total of credit side of P&L A/c is more than the total of its debit side, the difference would be known as Net Profit. In case when total of debit side exceeds the total of credit side, the difference is Net Loss. Whatever be the balance, it is transferred to the Capital A/c in the Balance Sheet.

Balance Sheet is another financial statement which is prepared to show the financial position of a trader on a specific date. It has two sides. The left hand side shows the Capital and other liabilities of the business and right hand side shows the assets of the business. These financial statements have been discussed at length in the previous lesson.

Since both these statements are with reference to specific period of time, it needs to be ensured that such items of income or expenditure, which do not pertain to the particular period of time, have not been included in these statements. If these have been included in the financial statements, they must be excluded by making necessary adjusting entries. The results disclosed by financial statements will be misleading if these adjustments are not considered. For example, the Trial Balance of a businessman shows payment of Rs.1200/- towards rent for two years. It means that half of this amount i.e. Rs.600/- is for the current year and the remaining half for the next year. If this adjustment is not incorporated in the financial statements, it would lead to understatement of profit for the current year by Rs.600/- because expenses for the next year have been charged from the profit of the current year.

Similarly, there can be so many other adjustments which are required to be incorporated in the final accounts in order to disclose the correct profit or loss and to show correct financial position of the business.

You are aware that generally the double entry system of book-keeping is followed in accounting. Double Entry has already been completed in respect of all the accounts that appear in Trial Balance. That is why these accounts are dealt with only once in the preparation of final accounts. These may be placed either in Trading A/c or in Profit & Loss A/c or in the Balance Sheet. However, for all the adjustments appended to the Trial Balance, double entry needs to be completed. Therefore all the adjustments are recorded at two places, one being on the debit and other being on the credit side. This point must be borne in mind while preparing final accounts.

INTEXT QUESTIONS 21.1

Fill in the blanks with suitable words :

- (i) There are _____ financial statements. (Two, three)
- (ii) The net profit disclosed by Profit and Loss A/c is taken to the _____ A/c in the Balance Sheet (Asset, Capital).
- (iii) Adjustments appended to the Trial Balance _____ incorporated in the final accounts (must be, need not be).
- (iv) Adjustment entries are recorded in _____ accounts (one, two).

21.4 ADJUSTMENTS AND THEIR INCORPORATION

The number and nature of adjustments differ from organisation to organisation. It depends upon the volume and nature of activities in the organisation. However, certain adjustments are common in all types of organisations e.g. closing stock, outstanding expenses, accrued income, etc. In this section, you will study about the following adjustments :

1. Closing stock
 2. Depreciation
 3. Additional Bad Debts
 4. Provision for Bad and Doubtful Debts
 5. Outstanding expenses
 6. Prepaid Expenses
 7. Accrued Income
 8. Unearned Income
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1. Closing Stock

Closing stock means the stock of goods remaining unsold at the close of the accounting year. This closing stock appears on the credit side of Trading A/c. Since this stock is an asset for the organisation it is also shown on the 'Asset' side of the Balance Sheet. The same stock becomes opening stock for the next accounting year. Suppose the value of closing stock is Rs.2000/-. The adjusting entry for this will be as follows :

Closing stock A/c	Dr.	2,000
To Trading A/c		2,000
(Being closing stock appearing at the end of the year)		

The following voucher will be prepared for this adjustment :

Firm's Name		
Voucher No. _____		Date _____
		Amount (Rs.)
<i>Debit</i>	Closing stock A/c	2,000
		2,000
<i>Credit</i>	Trading A/c (Being closing stock appearing at the end of the year)	2,000
		2,000
<i>Sd/-</i> <i>Manager</i>		<i>Sd/-</i> <i>Accountant</i>

The Final accounts will show this adjustment as follows :

Trading A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
		By Closing stock	2,000

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
		Closing stock	2,000

Note : In case the closing stock is given in the Trial Balance it will be shown only on the 'Assets' side of the Balance sheet.

2. Depreciation

There is a fall in the value of an asset on account of wear and tear, lapse of time and for other reasons. It is, therefore, justified that an expense on this account is charged from the profits. Such a charge or expense is called 'depreciation'. Suppose the value of furniture is Rs.10,000 and depreciation is to be charged @ 10% p.a. This means the amount of depreciation is to be charged is 10% Rs.10,000 which will be equal to Rs.1,000/-. The following journal entry is passed for this adjustment :

Depreciation A/c	Dr.	1,000
To Furniture A/c		1,000
(Being depreciation charged)		

The following voucher is prepared for this adjustment:

Firm's Name		
Voucher No. _____		Date _____
		Amount (Rs.)
Debit	Depreciation A/c	1,000
		1,000
Credit	Furniture A/c (Being depreciation charged on Furniture)	1,000
		1,000
Sd/- Manager		Sd/- Accountant

The Profit and Loss A/c is debited by the amount of depreciation. In the Balance sheet, the asset is shown at a reduced value after deducting the amount of depreciation.

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
To Depreciation	1,000		

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
		Furniture 10,000	
		Less : 1,000 Depreciation	
			9,000

Note : In case the amount of depreciation is given in the Trial Balance and not in the adjustments, it will be recorded only on the debit side of Profit & Loss A/c.

3. Additional Bad debts

Bad debts mean irrecoverable debts. It is a loss to the business and, therefore, is shown on the debit side of Profit & Loss A/c. When business is transacted on credit basis, some of the debtors donot settle the accounts by paying in full. It may also happen that some of the debtors fail to pay on account of insolvency. Additional bad debts mean bad debts in addition to what is shown as bad debts in the Trial Balance. The following adjusting entry is passed in case of additional or further Bad debts.

Bad Debts A/c Dr.

To Debtors A/c
(Being additional Bad Debts)

The following voucher is prepared for recording this adjustment :

Firm's Name		
Voucher No. _____		Date _____
		Amount (Rs.)
Debit	Bad Debts A/c	500
		500
Credit	Debtors A/c (Being amount due from debtors irrecoverable)	500
		500
Sd/- Manager		Sd/- Accountant

The amount of debtors is reduced by the amount of additional bad debts as shown below in the Balance Sheet.

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
To Bad Debts A/c			
Add :			
Additional Bad debts			

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
		Debtors	
		Less : Addition- al Bad Debts	

4. Provision for Bad and Doubtful Debts

This provision is created to show the true position of debtors in the Balance Sheet. Therefore, provision is created for bad and doubtful debts. The basis to provide for this provision is the past experience and practice of the business. It may be calculated in various ways. The position of each debtor may be studied individually or money due from all debtors may be summed up and at a certain rate on it. The amount of provision may be determined.

While dealing with this adjustment, we may come across following three situations :

- (i) Bad debts are given in the Trial Balance and provision is to be made at a given rate.
- (ii) When Bad debts are given in the Trial Balance and also in adjustments and provision is required to be created.
- (iii) If bad debts and provision for bad debts are given in Trial Balance, further bad debts are given in adjustments and also provision for doubtful debts is to be created.

The treatment in final accounts will be different in these three situations

In the first situation, Bad debts A/c will be posted to the debit side of Profit & Loss A/c. The provision will be created on the balance of Debtors A/c and following journal entry will be passed:

Profit & Loss A/c Dr

To Provision for Doubtful Debts A/c
(Being provision for Doubtful debts created)

Suppose Trial Balance shows Bad Debts Rs.500/- and at 5% rate provision for doubtful debts is to be created, Debtors Amounted to Rs.10,000. The final accounts will show this as under:

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
To Bad Debts A/c	500		
Add :			
Provision for doubtful debts	500		
	1,000		

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
		Debtors 10,000	
		Less : 500	
		Provision for Doubtful Debts	9,500
			9,500

In the second case, Bad debts A/c given in the Trial Balance will be taken to the debit side of Profit & Loss A/c. The additional bad debts will be added with the Bad Debts in Profit & Loss A/c and amount of debtors will be reduced by amount of additional bad debts. The amount of provision for Doubtful Debts will be calculated on the reduced balance of debtors. The following example will make this point clear. Suppose, the Bad Debts as per Trial Balance are Rs.1,000. Additional Bad debts amounted to Rs.500, Balance of Debtors is Rs.19,500 and provision is to be created @ 5% on debtors.

The Bad debts for Rs.1,000 given in Trial Balance will directly be taken to the debit side of Profit & Loss A/c. Additional Bad debts Rs.500/- will be added to Bad debts A/c and will be subtracted from the balance of debtors. This will make balance of Bad Debts A/c to Rs. 1500 and Debtors will show a balance of Rs. (19500-500). The amount of provision will be calculated @ 5% on Rs. 19000 which will be Rs. 950/-. The final accounts will show this case as follows :

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
To Bad Debts A/c	1,000		
Add : Additional Bad Debts	500		
Provision for doubtful debts	950		
	2,450		

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
		Debtors 19,500	
		Less : 500	
		Bad Debts	
		19,000	
		Less : 950	
		Provision for Doubtful Debts	18,050
			18,050

In the third situation, both Bad Debts and Provision for Doubtful debts are given in the Trial Balance as well as in the adjustments. Suppose in the above example, the trial balance shows bad Debts A/c Rs.1,000 and Provision for Doubtful Debts Rs. 500/-, other information being the same. In this case, the amount of provision will be calculated as shown in the above case but final accounts will show the following treatment :

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
To Bad Debts A/c	1,000		
Add : Additional Bad Debts	500		
New Provision	950		
	2,450		
Less : Old Prov.	500		
	1,950		

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
		Sundry 19,500 Debtors	
		Less: 500	
		Bad Debts	
		19,000	
		Provision for 950 Doubtful Debts	18,050
			18,050

The following voucher will be prepared for this adjustment:

Firm's Name		
Voucher No. _____		Date _____
		Amount (Rs.)
Debit	Profit & Loss A/c	500
		500
Credit	Debtors A/c. (Being provision for doubtful debts created)	500
		500
Sd/- Manager		Sd/- Accountant

INTEXT QUESTIONS : 21.2

I. Give exact term for your answer :

- (i) Stock remaining unsold at the end of year.
- (ii) Fall in the value of asset due to wear and tear or passage of time
- (iii) Irrecoverable Debts.
- (iv) Reserve against money due from debtors.

II. Match Column 'A' with Column 'B'

'A'	'B'
(i) Closing Stock	(a) Deducted from the value of asset
(ii) Additional Bad Debts	(b) Shown in the credit side of Trading A/c.
(iii) Depreciation	(c) Added to the Bad debts A/c in P & L A/c
(iv) Provision for Bad & Doubtful Debts	(d) Deducted from the Balance of Debtors after accounting for additional Bad Debts.

21.5 OTHER ADJUSTMENTS

5. Outstanding Expenses

There are certain expenses which are related to the current accounting period but have not been paid. These are known as **outstanding Expenses**. It is a common practice in most of the organisations to pay certain expenses like rent, wages, salaries etc. of each month in the following month. For example, salaries for the month of December are paid in the month of January next year. If final accounts are prepared for the year ending on 31st Dec, it is necessary that salaries and such other expenses which have accrued upto Dec., 31st, but have not been paid are accounted for. In the case of salaries outstanding, the following journal entry will be passed :

Salaries A/c Dr.

To Salaries Outstanding A/c

(Being salaries outstanding)

Firm's Name		
Voucher No. _____		Date _____
		Amount (Rs.)
Debit	Salaries A/c	
Credit	Outstanding Salaries A/c. (Being the amount of salary due for Dec. not yet paid)	
Sd/- Manager		Sd/- Accountant

In the final accounts, the amount of outstanding salaries is added with the amount of salaries already paid, as shown in the debit side of P & L A/c. On the other hand, it is a liability for the organisation, hence appears in the 'Liabilities' side of Balance Sheet.

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
Salaries			
Add : Outstanding Salaries			

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
Outstanding Salaries			

6. Prepaid or Unexpired Expenses.

Sometimes certain expenses are paid in advance and a part of these relates to the next accounting period e.g. Insurance Premium, Subscription for books and journals, etc. Such expenses must be apportioned between the current and next accounting period. Suppose the financial year of a business ends on 31st March, 1997. On 1st July, 1996 a sum of Rs.600/- was paid as annual insurance premium. While closing the books of accounts it needs to be taken care that insurance premium has been paid in advance for three months, i.e. from April, 97 to June, 97, amounting to Rs.150/-. This is a prepaid expense and following journal entry is passed for this adjustment :

Prepaid Insurance Premium A/c	Dr.	150
To Insurance Premium A/c		150

(Being insurance premium paid in advance).

Firm's Name		Date _____
Voucher No. _____	Amount (Rs.)	
Debit	Prepaid Insurance A/c	150
		150
Credit	Insurance A/c. (Being insurance for three months paid in advance)	150
		150
Sd/- Manager	Sd/- Accountant	

The Insurance Premium of Rs.600/- debited to P & L A/c is in excess by Rs.150/-. Therefore, it will be subtracted. Prepaid Insurance Premium will be shown on the 'Assets' side of Balance Sheet because its benefits are yet to be derived. The final accounts will show this adjustment as given below :

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
To Insurance Premium 600			
Less : Prepaid Insurance 150			
Premium	450		
	450		

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
		Prepaid Insurance Premium	150

7. Accrued Income

Just like outstanding expenses, income may also be outstanding at the close of an accounting year. For example, interest on securities, dividend on shares, commission, etc. becomes due but received at a later date. Such incomes are known as accrued income or income earned but not received. All such incomes should be duly considered while preparing the final accounts. The following example will make this point clear.

Suppose, some office premises are let out for Rs.1000 p.m. and rent for last month of accounting year has not been received till the date of preparing final accounts. Since rent becomes due on the last day of accounting year, Rs. 1000 will be treated as rent receivable, an accrued income. Rent Received A/c shown in the credit side of P & L A/c will be increased by Rs.1000. In the Balance Sheet, 'Rent receivable' will be shown on the 'Assets' side. The journal entry to be passed for this adjustment is as follows :

Rent receivable A/c	Dr.		1,000
		To Rent Received A/c	1,000
(Being the amount of rent receivable)			

The voucher for this adjustment will be prepared as shown below :

Firm's Name		Date _____
Voucher No. _____		
		Amount (Rs.)
Debit	Accrued Rent A/c	1,000
		1,000
Credit	Rent Receivable A/c. (Being rent for last month not received)	1,000
		1,000
Sd/- Manager	Sd/- Accountant	

The final accounts will show this adjustment as given below :

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
		By Rent received	
		Less : Rent receivable	1,000

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
		Rent Receivable	1,000

8. Unearned income

Sometimes, certain income is received before it becomes actually due. Such income is called 'unearned income' or income received in advance. Since this income is not related to the current year, it must be deducted from the relevant head of Income in Profit & Loss A/c. Such unearned income is shown on the 'Liabilities' side of Balance Sheet. Take for example the following case :

An advertising agency received Rs. 5000/- as advertisement fee for six months on 1st January 1997. The accounting period of this company is from 1st April 96 to 31st March 97. In this case you would notice that advertisement fee for three months i.e. from April 97 to June 97 has been received in advance. the services for which will be rendered in future. Hence this is an "unearned income" for the company. Following journal entry is passed for this adjustment :

Advertisement fee A/c Dr.	2,500
To Unearned Advertisement fee A/c	2,500
(Being advertisement fee received in advance)	

The following voucher will be prepared for this adjustment

Firm's Name		Date _____
<i>Voucher No.</i> _____		<i>Amount (Rs.)</i>
<i>Debit</i>	Advertisement fee A/c	2,500
		2,500
<i>Credit</i>	Unearned Advertisement A/c. (Being advertisement fee received in advance)	2,500
		2,500
<i>Sd/- Manager</i>		<i>Sd/- Accountant</i>

The final accounts will show adjustment as given below :

Profit & Loss A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
		By Advertisement Fee	5,000
		Less : Fee Received in advance	2,500
			2500

Balance Sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
Advertisement fee received in advance	2,500		
	2,500		

Example

From the following trial Balance of M/s. Gupta Furnitures as on 31st December, 1996 you are required to prepare a Trading and Profit & Loss A/c for the year ended 31st Dec. 1996 and a Balance Sheet as at that date, after making the necessary adjustments. Trial Balance of M/s. Gupta Furnitures as at 31.12.1996.

Particulars	Dr.(Rs.)	Cr.(Rs.)
Capital A/c of Mr. Gupta		80,000
Cash in Hand	540	
Cash in Bank	2,630	
Purchase A/c	43,120	
Sales A/c		78,100
Wages A/c	10,480	
Fuel and Power A/c	4,730	
Carriage on Sales A/c	3,200	
Carriage on Purchase A/c	2,040	
Stock (on 1-1-96)	5,760	
Land & Building A/c	40,000	
Machinery A/c	20,000	
Salaries A/c	15,000	
Insurance A/c	600	
Sundry Debtors A/c	20,000	
Sundry Creditors A/c		10,000
	1,68,100	1,68,100

Taking into consideration the following adjustments, make necessary journal entries and prepare final accounts.

- (i) Stock on hand on 31.12.96 is Rs.5,000.
- (ii) Machinery is to be depreciated @ 10% p.a.
- (iii) Salaries for the month of December outstanding amounted to Rs.3,500.
- (iv) Insurance prepaid for 3 months.

Solution

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Adjusting Entries				Rs.	Rs.
1996					
Dec.	31	Closing Stock A/c To Trading A/c (Being closing stock taken into account)	Dr.	5,000	5,000
Dec.	31	Depreciation A/c To Machinery (Being depreciation charged on Machinery @ 10%)	Dr.	2,000	2,000
Dec.	31	Salaries A/c To Salaries Outstanding (Being outstanding salaries provided for)	Dr.	3,500	3,500
Dec.	31	Prepaid Insurance A/c To Insurance A/c (Being prepaid insurance taken into account)	Dr.	150	150

Trading Account of M/s. Gupta Furnitures for the year ended on 31st Dec. 1996

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
To Stock (1.1.96)	5,760	By Sales	78,100
To Purchases	43,120	By Stock (31.12.96)	5,000
To Wages	10,480		
To Fuel and Power	4,730		
To Carriage on Purchase	2,040		
To Gross Profit transferred to Profit and Loss A/c	16,970		
	<u>83,100</u>		<u>83,100</u>

Profit and Loss A/c
for the year ended on 31st Dec., 1996

To Carriage on Sales	3,200	By Gross Profit	16,970
To Salaries 15,000		By Net Loss transferred to capital A/c of	7,180
Add : Outstanding 3,500		Mr. Gupta	
To Insurance 600	18,500		
Less : Prepaid 150			
	450		
To Depreciation on Machinery	2,000		
	24,150		24,150

Balance Sheet of M/s. Gupta Furnishers
as on 31st Dec., 1996

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry Creditors	10,000	Cash in Hand	540
Outstanding Salaries	3,500	Cash at bank	2,630
Capital A/c of		Sundry Debtors	20,000
Mr. Gupta 80,000		Closing Stock	5,000
Less : Net Loss 7,180		Prepaid Insurance	150
	72,820	Land and Building	40,000
		Machinery A/c 20,000	
		Less :	
		Depreciation 2,000	18,000
	86,320		86,320

Example

From the following trial Balance of Navin Goyal and Co., prepare Trading and Profit and Loss A/c for the year ending on 31st Dec. 97 and Balance Sheet as on that date after passing necessary journal entries for adjustments.

Dr. Balance		Cr. Balance	
Land and Building	6,000	Capital	17,000
Plant and Machinery	4,000	S. Creditors	3,000
Bills Receivable	800	Sales	10,000
Stock on 1.1.1997	4,000	Reserve for Bad and doubtful debts	450
Purchases	5,100	Loan	1,000
Wages	2,000	Commission Recd.	200
Coal, Gas & Coke	580		
Salaries	500		
Rent	280		
Cash at Bank	2,500		
Sundry Debtors	4,500		
Repairs	180		
Bad Debts	550		
Sales Returns	200		
Furniture and Fixture	400		
Interest on Loan	60		
	31,650		31,650

Adjustments

1. Closing stock valued at Rs.5,000.
2. Depreciate Plant & Machinery @ 5%, Furniture & Fixture @10%.
3. Provide for Bad and Doubtful Debts at 5%.
4. Outstanding Wages Rs.100, Rent Rs. 50/-.
5. Commission accrued Rs.100/-.

Solution

1997		Adjusting Entries		Rs.	Rs.
Dec.	31	Closing Stock A/c	Dr.	5,000	
		To Trading A/c			5,000
		(Being closing stock taken into account)			
Dec.	31	Depreciation A/c	Dr.	240	
		To Plant & Machinery			200
		To Furniture & Fixture			40
		(Being depreciation charged @ 5% on Plant & Machinery & @ 10% on furniture)			
Dec.	31	Profit & Loss A/c	Dr.	225	
		To Reserve for doubtful debts			225
		(Being reserve for doubtful debts created)			
Dec.	31	Wages A/c	Dr.	100	
		Rent A/c	Dr.	50	
		To Outstanding Expenses			150
		(Being outstanding expenses provided for)			
Dec.	31	Commission Accrued	Dr.	100	
		To Commission Received			100
		(Being Commission accrued taken into consideration)			

Trading and Profit & Loss A/c of M/s Navin Goyal & Co. for the year ended on 31.12.97.

Dr.		Cr.	
Particular	Amount	Particulars	Amount
To Opening Stock	4,000	By Sales 10000	
To Purchases	5,100	Less : Sales 200	
To Wages 2,000		Returns	9,800
Add : Outstanding 100		By Closing Stock	5,000
	2,100		
To Coal, Gas & Coke	580		
To Gross Profit	3,020		
	14,800		14,800
To Salaries	500	By Gross Profit	3,020
To Rent 280		By Commission	
Add : Outstanding 50		Received 200	
	330	Add : Accrued	
To Repairs	180	Commission 100	300
To bad Debts 550			
Add : New Reserve 225			
	775		
Less : Old Reserve 450			
	325		
To Interest on Loan	60		
To Depreciation :			
Plant & Machinery 200			
Furniture & Fixture 40			
	240		
To Net Profit Transferred			
To Capital A/c	1,685		
	3,320		3,320

Balance Sheet of M/s Navin Goyal & Co. as on 31.12.97

Liabilities	Amount	Assets	Amount
Sundry Creditors	3,000	Cash at Bank	2,500
Loan A/c	1,000	Bills Receivable	800
Outstanding Expenses :			
Wages 100		Sundry Debtor 4,500	
Rent 50		Less:	
	150	Reserve for 225	
Capital 17,000		Doubtful	
Add : Net Profit 1,685		Debts	4,275
	18,685	Closing Stock	5,000
		Furniture	
		& Fixture 400	
		Less : Dep. 40	
			360
		Plant & Machinery 4000	
		Less : Dep. 200	
			3,800
		Land & Building	6,000
		Commission	100
		Accrued	
	22,835		22,835

INTEXT QUESTIONS : 21.3

Given below are the statements regarding adjustments. Some of these statements are true and some of these statements are false. Write 'T' before true statements and 'F' before False statements.

- (i) Outstanding expenses are those which are due but unpaid.
 - (ii) After adjusting for Prepaid expenses, the profit disclosed by P&I A/c is increased.
 - (iii) Unearned income is added to the related income shown by Trial Balance.
 - (iv) Prepaid expenses are shown on the Asset side of Balance Sheet.
 - (v) Income Accrued is shown on the Asset side of Balance Sheet.
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21.4 WHAT YOU HAVE LEARNT

1. Trading A/c and Profit and Loss A/c and Balance Sheet are two financial statements which are prepared at the end of the accounting year.
 2. Trading A/c and Profit and Loss A/c shows net results, in terms of profit or loss, for the accounting year while Balance sheet reflects financial position of a business on a specific date.
 3. In order to disclose correct results and true financial position, it is important that all outstanding and accrued income and expenses are accounted for.
 4. Adjustment given at the end of Trial Balance are recorded at two places, one on debit and the other on credit.
 5. Closing stock is unsold stock of goods at the end of accounting year.
 6. Depreciation refers to fall in the value of asset on account of wear and tear or lapse of time.
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7. Additional bad debts are irrecoverable debts in addition to what has been shown in the Trial Balance as Bad debts.
8. Provision for Bad and Doubtful debts is created for future payments due from debtors but seems to be irrecoverable. It is created on the basis of past experience.
9. Outstanding expenses are such expenses which have become due but have not been paid in the concerned accounting year.
10. Prepaid expenses are those expenses which have not become due but have been paid during the accounting year in question.
11. Accrued income is income earned but not received.
12. Unearned income is that income which is not due but has been received.

21.5 TERMINAL QUESTIONS

1. Answer following questions briefly :
 - i. Why adjustments are important?
 - ii. Why outstanding expenses are treated as liabilities ?
 - iii. What is the difference between accrued and unearned income?
2. Write journal entries for following adjustments :
 1. Outstanding expenses
 2. Depreciation
 3. Income received but unearned
 4. Prepaid insurance.
3. Why Reserve for doubtful debts is created?
4. From the following Trial Balance, prepare Trading & Profit & Loss A/c for Ram Shyam & Co. for the year ending on 30th June, 1997 and Balance Sheet as on that date. Also pass necessary journal entries.

Trial Balance as on 30-6-1997

Dr. Balance		Cr. Balance	
Land & Building	10,000	Bills Payable	1,000
Stock 1-7-96	3,800	Ram's Capital	6,000
Plant & Machinery	4,500	Shyam's Capital	9,000
Bills Receivable	2,000	Sales	34,200
Purchases	12,000	Discount	100
Wages	4,000	Creditors	3,000
Salaries	2,000	Interest	200
Debtors	1,500	Return Outwards	500
Furniture	500		
Cash at Bank	8,750		
Rent (Office)	2,200		
Bad Debts	100		
Insurance	1,500		
Freight & Carrage	200		
Gas & Fuel	450		
Factory lighting	100		
Return Inwards	400		
	54,000		54,000

Adjustments

1. Stock on 30th June 1997 was Rs.5000/-
2. Write off depreciation 10% on Furniture, 5% on Land and Building and 20% on plant and machinery.
3. Provide for following outstanding expenses : wages Rs.650/-, Salaries Rs.250/-, Office Rent Rs.200 Insurance paid in advance Rs.300/-

(Ans: G.P. 18,100, N.P. 11,000, Total of B/s 31,100)

5. The Reserve for Bad and Doubtful Debts Account Shows a balance of Rs.800 on 1st Jan, 1996. The Bad Debts during the year 1996 amounted to Rs.300. The sundry debtors on 31st Dec. 1996 are Rs.8,000. Create a reserve of 5% on Bad and doubtful debts.

Make necessary journal entries and show the P&L A/c & Balance Sheet.

6. On the basis of Trial Balance of Subhash Bros., prepare Trading & Profit & Loss A/c for the year ending on 31st Dec. 1997 and Balance Sheet as on that date after considering adjustments given after the Trial Balance.

Dr. Balances		Cr. Balances	
Land & Building	6,000	Capital	15,000
Plant & Machinery	4,000	Sundry Creditors	3,000
Stock (1-1-97)	4,000		
Purchases	5,100	Sales	11,500
Wages	2,000		
Carriage Inward	100	Reserve for	
Carriage outward	40	Doubtful Debts	450
Salaries	500	Discount	140
Discount	150	Commission	200
Rent	280		
Cash at Bank	2,500		
Cash in Hand	40		
Sundry Debtors	4,500		
Repairs	180		
Printing & Stationary	55		
Bad Debts	320		
General Expenses	525		
	30,290		30,290

Adjustments

1. Closing stock valued at Rs.5,000
2. Depreciate Plant & Machinery @ 15%, Land & Building @ 10%.
3. Provide for bad & Doubtful Debts @ 5%.
4. Outstanding wages Rs. 500/-

(Ans: Gross Loss : Rs.200/-, Net Loss : Rs. 2885, B/s
Total Rs.18,500/-)

21.8 ANSWERS TO INTEXT QUESTIONS

21.1 (i) two, (ii) Capital, (iii) must be, (iv) two

21.2 I (i) Closing stock, (ii) Depreciation, (iii) Bad Debts,
(iv) Reserve for bad & doubtful debts.

II. (i) (b), (ii) (c), (iii) (a), (iv) (d)

21.3 (i) T, (ii) F, (iii) F, (iv) T, (v) T
