



# **Module-A Unit-5**

## **JAIIB PAPER-3**

### **Accounting & Financial Management for Bankers(AFM)**



## JAIIB AFM Module A Unit 5- Trial Balance, Rectification of Errors and Adjusting & Closing Entries

### Trial Balance

**Multiple entries in various accounts** will make a Ledger. Taking all the ledger balances and presenting them in a single worksheet as on a particular date is Trial Balance.

*To understand a trial balance, we must first understand the following:*

- **Double entry system** – Recording two entries for a single transaction that is equal and opposite in nature
- **Journal** – All transactions recorded in double entry system of bookkeeping
- **Ledger** – Summary of all journals of a similar nature.

### Features and Purpose of a Trial Balance

- It is a list of debit and credit balance drawn from ledger.
- It includes cash and Bank balance.
- Its main purpose is to establish arithmetical accuracy of transactions recorded in the books of account.
- It is usually prepared at the end of the year but it can also be prepared any time, as and when required, e.g, monthly, quarterly or half yearly.
- It enables the trader to know amounts receivable from customers and amounts payable to suppliers.
- It facilities preparation of final accounts.

### Types of Trial Balance and Preparation of Trial Balance

There are two types of Trial balance:

- Gross Trial Balance
- Net Trial Balance

### Gross Trial Balance

*It is Prepared in the following stages:*

- Take totals of debit and credit columns of each ledger account.
- Take totals of receipts and payments of cashbook showing separately cash, bank and discount columns.
- Write names of all accounts as per the ledger and cash, bank and discount accounts as per cash book onto a statement.
- Enter the debit and credit totals against each item.
- Finally take total of debit and credit columns.

**Example:**

On 31<sup>st</sup> March 2014, the totals of debit and credit sides of various ledger accounts and receipts and payments sides of cash and bank columns of cash book of Mr. Abhinav are as under:

Total of debit side (Rs.)	Name of the account	Total of credit side (Rs.)
10,000	Abhinav Capital	1,35,000
25,000	Drawings	-
15,000	Stock on 31 <sup>st</sup> March, 1996	-
1,90,000	Purchases	4,000
-	Purchases Returns	18,000
6,000	Sales	2,45,000
13,000	Sales Returns	--
12,000	Expenses	-
3,05,000	Customers	2,50,000
2,00,000	Suppliers	2,35,000
1,00,000	Car	-
2,81,000	Dena Bank	2,75,000
43,000	Cash	38,000

**Solution****Gross Trial Balance as on 31<sup>st</sup> March 2014**

Name of the Account	L.F	Debit (Rs.)	Credit (Rs.)
Abhinav Capital		10000	1,35,000
Drawings		25000	--
Stock on 31 <sup>st</sup> March, 2013		15000	--
Purchases		190000	4000
Purchases Returns		--	18000
Sales		6000	2,45,000

Sales Returns		13000	--
Expenses		12000	--
Customers		3,05,000	2,50,000
Suppliers		2,00,000	2,35,000
Car		1,00,000	--
Dena Bank		2,81,000	2,75,000
Cash		43,000	38,000
Total		12,00,000	12,00,000

### Net Trial Balance

Under this trial Balance, net balance of each amount are drawn and shown in trial balance. If debit total of an account is more, it will show debit balance and of credit total of an account is more, it will show a credit balance.

#### Net Trial Balance as on 31<sup>st</sup> march 2014

Name of the Account	L.F	Debit (Rs.)	Credit (Rs.)
Abhinav Capital			1,25,000
Drawings		25000	--
Stock on 31 <sup>st</sup> March, 2013		15000	--
Purchases		186000	
Purchases Returns		--	18000
Sales			2,39,000
Sales Returns		13000	--
Expenses		12000	--
Customers		55000	--
Suppliers			35,000
Car		1,00,000	--
Dena Bank		6000	
Cash		5000	

Total		4,17,000	4,17,000
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## Disagreement of a Trial Balance

**Disagreement of a trial balance may be caused by the wrong totaling or balancing of ledger accounts.** While totaling the figure of subsidiary books there may arise some errors that will cause disagreement of trial balance. Omission to post a ledger balance also causes the disagreement of a trial balance.

### Classification of Errors

*Errors can be broadly divided into two type:*

- Clerical Errors
- Principle Errors

#### Clerical Errors

- Errors of Omission,
- Errors of Commission, and
- Compensating errors.

#### Errors of Omission

The Errors of Omission will occur when a transaction is not recorded in the books of accounts or omitted by mistake. The Errors of Omission two types.

- Partial
- Complete

**The partial errors** may happen in relation to any subsidiary books. This is the result of when a transaction is entered in the subsidiary book but not posted to the ledger. For example, cash paid to the suppliers has been entered in the payment side of the cash book but it will not be entered in the debit side of the suppliers account.

**The complete omission** may happen the transaction is completely omitted from the books of accounts. For example, an accountant fails to enter a specific invoice from the sales day book.

#### Errors of Commission

When a transaction is entered in the books of accounts in wrongly, this may be entered as partially or incorrectly. This kind of errors are known as Errors of Commission. The Errors of Commission may happens because of ignorance or negligence of the accountant. This may be of different types, the main reasons are Errors relating to subsidiary books and Errors relating to ledger. **Following are some of the examples:**

- Posting of correct amount but on the wrong side
- Posting of a wrong amount but on the correct side
- Posting of a wrong amount amount on wrong side of an account

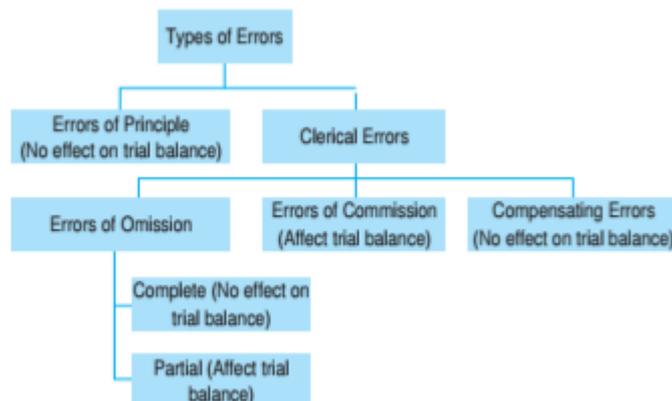
### Compensating Errors

Compensating Errors are those errors which compensates themselves in the net results of the business. This means, if there are over debit in one account which will be compensated by the over credit in some account in the same extent of the business. Like that, if there is a wrong debit in one account which will be neutralized by some wrong credit in the same extent of the business.

### Errors of Principles

This kind of errors are occurs when the entries are made against the principle of accounting. These Errors are made because of the following reasons:-

- Errors happens due to the inability to make a distinction between the revenue and capital items.
- Errors happens due to the inability to make a difference between the business expenses and personal expenses.
- Errors happens because of the inability to make a distinction between the productive expense and nonproductive expenses.



### Rectification of Errors

#### One- sided Errors

- These errors affect only one account. Thus, these are one-sided errors. We can rectify these errors by giving an explanatory note in the account or by passing a journal entry with the help of Suspense A/c. When we detect an error before posting to the ledger, we can correct it by simply crossing the wrong amount, writing the correct amount above it and initializing it. Similarly, we can also correct an error in the ledger account.
- Errors of casting, errors of carrying forward the balances, errors of balancing the accounts, errors of posting the wrong amount in the correct account, error of

posting in the correct account on the wrong side, omitting to show an account in the trial balance, posting in wrong side with wrong amount are the examples of errors affecting the Trial Balance.

### Two-sided Errors

- These errors affect two or more accounts simultaneously. Thus, these are two-sided errors. We can rectify these by passing a journal entry giving the correct debit and credit to the accounts. In order to rectify an error, we need to cancel the effect of wrong debit or credit by reversing it and restore the effect of correct debit or credit.
- When there is short debit or excess credit in an account we need to debit the concerned account. Whereas, when there is short credit or excess debit in an account we need to credit the concerned account.
- Complete omission to record an entry in the journal or the subsidiary books, incorrect recording of transactions in the books, complete omission of posting and errors of principle are the examples of these errors.

### Suspense Account

When the trial balance does not tally due to the one-sided errors in the books, an accountant puts the difference between the debit and credit side of the trial balance on the shorter side as the Suspense A/c. As and when we locate and rectify the errors, the balance in the Suspense A/c reduces and consequently becomes zero. Thus, we cannot categorize the Suspense A/c. It is a temporary account and can have debit or credit balance depending upon the situation.

***While using the Suspense A/c to rectify the one-sided errors, the accountant needs to follow the following steps:***

- Identification of the account with the error.
- Ascertainment of the excess debit or credit or short debit or credit in the above account.
- In case of short debit or excess credit in an account, we need to debit the concerned account. Whereas, in case of short credit or excess debit in an account we need to credit the concerned account.
- Pass the necessary journal entry by debiting or crediting the Suspense A/c

### Example

Q: Trial Balance of M/s Srivastav Enterprises did not agree. It puts the difference to the Suspense A/c. Rectify the following errors and prepare the Suspense A/c to ascertain the original difference in the trial balance.

Amount paid for the installation of the machinery ₹10000 was posted to the Repairs and maintenance A/c.

Total of Purchases book ₹50000 was not posted to the ledger.

Goods returned to John ₹3000 were recorded in Sales Book.

Salary paid to Ram ₹6000 was debited to his personal account.

Depreciation written-off on furniture ₹500 was not posted to the furniture account.

**Ans: In the books of M/s Srivastav Enterprises**

Date	Particulars		Amount (Dr.)	Amount (Cr.)
1.	Machinery A/c	Dr.	10000	
	To Repairs and Maintenance A/c			10000
	(Being rectification of the wrong journal entry in the Repairs and maintenance A/c)			
2.	Purchases A/c	Dr.	50000	
	To Suspense A/c			50000
	(Being rectification of the omission to post the total of purchases book in the ledger)			
3.	Sales A/c	Dr.	3000	
	To Purchases Return A/c			3000
	(Being rectification of wrong recording of the purchases return in the sales book)			
4.	Salary A/c	Dr.	6000	
	To Ram's A/c			6000

	(Being rectification of wrong debit to the personal account of an employee)			
5.	Suspense A/c	Dr.	500	
	To Furniture A/c			500
	(Being rectification of omission of posting in the furniture account)			

### Suspense A/c

Date	Particulars	Amount	Date	Particulars	Amount
	Difference as per Trial balance	49500	2.	By Purchases A/c	50000
5.	To Furniture A/c	500			
		<b><u>50000</u></b>			<b><u>50000</u></b>

### Entries Adjusting and Closing

#### Adjusting Entries

- Final Account are the accounts which are prepared at the end of the trading year. These accounts show the final results of the business carried out. Final accounts are prepared to find out profit earned or loss sustained by a concern.
- At the end of the accounting year, all ledger accounts are balanced and then trial balance is prepared. From the trial balance, final accounts, i.e. trading, profit and loss account and balance sheet are drawn. While preparing trading and profit and loss account, all expenses and incomes for the full period are to be taken into consideration. If expenses have been incurred but not paid or income is due but not received, necessary entries are required to be passed to show the correct picture of the business. These entries are called "Adjusting Entries".

## Closing Entries

At the end of cash year, all accounts of expenses and incomes must be closed. The balance of these accounts are transferred to trading account and profit and loss account. The entries passed to transfer these balances are called “Closing entries”.

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