

CHAPTER 18

FINAL ACCOUNTS (WITH ADJUSTMENTS)

❖ Meaning of Financial Statements

Financial statements refer to the statements that depict the financial performance (i.e. profit/loss, surplus/deficit) as well as position (assets and liabilities) of an enterprise.

❖ Need for Adjustments

- To record the hitherto unrecorded transactions
- To make provisions for anticipated losses
- To adjust accrued income, advance income, accrued expenses and advance expenses
- To present fair and unbiased presentation of assets and liabilities
- To locate and rectify errors

❖ TREATMENT OF ITEMS

<i>If given <u>inside</u> the Trial Balance</i>	<i>If given <u>outside</u> the Trial Balance (ADJUSTMENTS)</i>			
TREATMENT	ITEMS	JOURNAL ENTRY	TREATMENT	
Shown in the Assets side of the Balance Sheet	1) Closing Stock (shown with cost price or realisable value whichever is lesser)	Closing Stock A/c Dr. To Trading A/c	Shown in the credit side of Trading A/c	Shown in the Assets side of the Balance Sheet

Shown in the Liabilities side of the Balance Sheet	2) Outstanding Expenses	Concerned Exp. A/c Dr. To O/s Exp. A/c	Added to the concerned expense either in Trading A/c or Profit and Loss A/c debit side	Shown in the Liabilities side of the Balance Sheet
Shown in the Assets side of the Balance Sheet	3) Prepaid Expenses	Prepaid Exp. Dr. To Concerned Expenses A/c	Deducted from the concerned expense either in Trading A/c or Profit and Loss A/c debit side	Shown in the Assets side of the Balance Sheet
Shown in the Assets side of the Balance Sheet	4) Accrued Income	Accrued Income A/c Dr. To Concerned income A/c	Added to the concerned income in Profit and Loss A/c Credit side	Shown in the Assets side of the Balance Sheet
Shown in the Liabilities side of the Balance Sheet	5) Unearned Income	Concerned Income A/c Dr. To Unearned income A/c	Deducted from the Concerned income in Profit and Loss A/c Credit side	Shown in the Liabilities side of the Balance Sheet
Shown in the debit side of Profit and Loss A/c	6) Depreciation	Depreciation A/c Dr. To Concerned Fixed Assets A/c	Shown in the Debit side of Profit and Loss A/c	Deducted from the concerned fixed assets in the Assets side of the

					Balance Sheet
Shown in the debit side of Profit and Loss A/c	7) Interest on capital	Interest on Capital A/c To capital A/c	Dr.	Shown in the debit side of Profit and Loss A/c	Added to the Capital in the Liabilities side of Balance Sheet
Shown in the credit side of Profit and Loss A/c	8) Interest on drawings	Drawings A/c To Interest on Drawing A/c	Dr.	Shown the credit side of Profit and Loss A/c	Deducted from the Capital in the Liabilities side of Balance Sheet
Shown the credit side of Profit and Loss A/c	9) Interest on Loan <u>Case – I</u> If Loan is an Asset (Loan taken)	O/s Interest A/c To Interest on Loan A/c	Dr.	Shown in the credit side of Profit and Loss A/c	Added to the Loan in the Assets side of the Balance Sheet
Shown in the debit side of Profit and Loss A/c	<u>Case – II</u> If loan is a liability (Loan taken)	Interest on loan A/c To O/s Interest A/c	Dr.	Shown in the debit side of Profit and Loss A/c	Added to the loan in the Liabilities side of the Balance Sheet
Shown in the debit side of Profit and Loss A/c	10) Bad-debts	Bad-debts A/c To Sundry Debtors A/c	Dr.	Shown in the debit side of Profit and Loss A/c	Deducted from the Debtors in the Assets side of the Balance Sheet

	11) Further Bad-debts	Further bad-debts A/c To Sundry Debtors A/c	Dr.	Added to the old Bad-debts in the debit side of Profit and Loss A/c	Deducted from the Net debtors (Sundry debtors <i>less</i> Bad-debts (in adjustment) in the Assets side of the Balance Sheet
If Old Provision is <i>lesser</i> than the total of all bad-debts, then Old Provision is deducted from the sum of Bad-debts, further Bad-debts and New provision.	12) Provision for Bad and Doubtful debts *	Profit and Loss A/c To Provision for Bad and Doubtful debts A/c		New Provision is added to the sum total of Bad-debts and further Bad-debts	New Provision is deducted from the Sundry Debtors i.e. {Sundry Debtors <i>less</i> Bad-debts (in adjustments) <i>less</i> Further Bad-debts <i>less</i> New provision for bad and doubtful debts}
But if Old Provision is <i>greater</i> than the sum totals of all the bad-debts, then it is shown in the credit side of the Profit and Loss A/c					
	13) Provision for discount on	Profit and Loss A/c To Provision for	Dr.	Shown in the debit side of the Profit and Loss	Deducted from the Good Debtors i.e.

debtors	Discount on Debtors A/c		A/c	{Sundry Debtors <i>less</i> Bad debtors <i>less</i> Further Bad debt <i>less</i> New Provision for Bad and doubtful debts <i>less</i> Discount on debtors} in the Assets side of the Balance Sheet
14) Provision for discount on creditors	Creditors A/c To Provision for discount on Creditors	Dr.	Shown in the Credit side of Profit and Loss A/c	Deducted from the Creditors in the Liabilities side of the Balance Sheet
15) Abnormal loss **	Loss by Accident A/c	Dr.		
Case-I If goods are <u>not</u> Insured	To Purchases A/c Profit and Loss A/c To Loss by Accident A/c	Dr.	Deducted from Net purchases (Purchases <i>less</i> Purchases return) in the Debit Side of Trading A/c	Shown in the Debit side of Profit and Loss A/c
Case-II If goods are Insured	Loss by Accident A/c To Purchases A/c	Dr.	Deducted from Net purchases (Purchases <i>less</i> Purchases return) in the Debit Side of	Shown in the debit side of Profit and Loss A/c with actual loss and

				<i>less</i> Purchases Returns) in the debit side of Trading A/c	and Loss A/c
18) Goods distributed as free samples	Advertisement A/c To Purchases A/c	Dr.		Deducted from the Net Purchases in the debit side of Trading A/c	Shown in the debit side of Profit and Loss A/c
19) Withdrawal of goods for personal use (Drawings in form of goods)	Drawings A/c To Purchases A/c	Dr.		Deducted from the Net Purchases in the debit side of Trading A/c	Shown in the debit side of Profit and Loss A/c
20) Deferred revenue Expenditure	Profit and Loss A/c To Deferred Revenue Expenditure A/c (With current year's amount only)	Dr.		Shown in the debit side of Profit and Loss A/c (With current year's amount only)	Shown in the Assets side of the Balance Sheet (With current year's amount only)

NOTE:

* If Provision for Bad and Doubtful debt is given inside the Trial Balance then it is known as old provision. But if it is given in the adjustments then it is known as New Provision.

** Gross Loss of goods implies Total Loss of goods, where Actual Loss implies Net Loss (i.e. Total loss – Insurance claim received). For e.g. if goods worth Rs 10,000

were destroyed by fire then Rs 10,000 is total or gross loss. If Insurance company accepts 80% of the loss claimed, then Rs 2,000 (i.e. 10,000 – 8,000) is net (actual) loss and will be shown in the debit side of Profit and Loss A/c.

21) Manager's Commission on Net Profit

Generally, there are two practices followed for providing manager's commission:

- Manager's Commission on net profit *before* charging his commission
- Manager's commission on net profit *after* charging his commission

Steps to compute Manager's Commission on Net Profit before charging his commission

- **Step 1:** Calculate the total of debit side and the total of credit side
- **Step 2:** Calculate Net profit by deducting total of debit side from the total of credit side.
- **Step 3:** Calculate Manager's Commission by the formula:
$$\text{Net Profit before charging commission} = \text{Net Profit} \times \frac{\text{Rate}}{100}$$
- **Step 4:** Show manager's commission in the debit side of Profit and Loss A/c and in Liabilities side of Balance Sheet as Manager's Commission Payable.
- **Step 5:** Deduct manager's commission from the Net Profit computed in the Step (2) and show the balance as Net Profit in the debit side of Profit and Loss A/c

Steps to compute Manager's Commission on Net Profit after charging his commission

- **Step 1:** Calculate the total of debit side and the total of credit side
- **Step 2:** Calculate Net profit by deducting total of debit side from the total of credit side.
- **Step 3:** Calculate Manager's Commission by the formula:

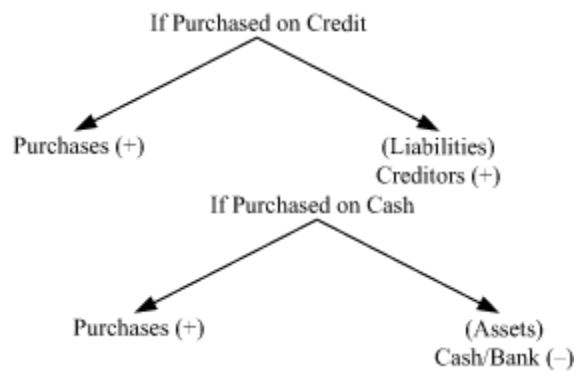
$$\text{Net Profit before charging commission} \times \frac{\text{Rate}}{100 + \text{Rate}}$$

- **Step 4:** Show manager's commission in the debit side of Profit and Loss A/c and in Liabilities side of Balance Sheet as Manager's Commission Payable.
- **Step 5:** Deduct manager's commission from the net profit computed in the Step (2) and show the balance as Net Profit in the debit side of Profit and Loss A/c

NOTE:

- If manager's commission is given inside the Trial Balance, then it will be shown only in the debit side of the Profit and Loss A/c.
- If manager's commission is given inside the Trial Balance as 'Manager's Commission Payable', then it will be shown only in the Liabilities side of the Balance Sheet.

22) Goods purchased but not recorded



23) Goods sold but not recorded

