ALLAMA IQBAL OPEN UNIVERSITY

USMAN NOTES
www.usmannotes.com

Name:

Registration No.:

Course Code: 1339

Program: FA/ICom

Semester: Autumn 2026

ALLAMA IQBAL OPEN UNIVERSITY, ISLAMABAD

(Department of Commerce)

Course: Basics of Accounting (1339)

Level: FA/ICom

Semester: Autumn 2026

Assignment No. 2 (Units: 5–9)

Total Marks: 100

Pass Marks: 40

SOLVED ASSIGNMENT GUIDE — For Study & Reference

Note for Students: This guide is prepared for study and reference only. Read it, understand the method and the reasoning, and then write your assignment in your own words. Copying any guide word-for-word is against the spirit of the University's instructions and its plagiarism policy.

Question 1

Q.1 Prepare Bank Reconciliation of Ahmer traders as on 31st May, 2024, with the single balance method. (20)

Introduction

A business that operates a bank account records every banking transaction twice over, in two independent records: the bank column of its own cash book, maintained by the trader, and the pass book (or bank statement), maintained by the bank. In theory the two balances should agree on any date; in practice they very often differ, because some transactions are recorded by one party before the other, and because the bank makes charges and receives collections that the trader learns of only later. The statement prepared to explain and reconcile the two balances is

called a Bank Reconciliation Statement (BRS). This question requires the BRS of Ahmer Traders as on 31st May 2024 by the single balance method, starting from the pass book balance and arriving at the cash book balance.

Causes of Difference Between Cash Book and Pass Book

The differences fall into three families. First, timing differences in deposits: cheques deposited into the bank are entered at once in the cash book but are credited by the bank only after clearing, so uncleared (uncredited) cheques make the cash book balance higher than the pass book balance. Second, timing differences in payments: cheques issued are recorded at once in the cash book, but the bank pays them only when the payee presents them, so unpresented cheques make the pass book balance higher than the cash book balance. Third, transactions originated by the bank itself: bank charges, interest, direct deposits made by customers into the trader's account, dividends collected by the bank, and standing-order payments appear first in the pass book and enter the cash book only when the trader sees the statement. Errors by either party form a fourth, occasional cause. A reconciliation statement works through exactly these items one by one, adding those that make the starting balance grow towards the target balance and deducting those that make it shrink.

The Single Balance Method

Under the single balance method the statement begins with one balance only — here the pass book balance, because the question gives it and asks us to "find out the balance as per the cash book" — and every reconciling item is either added to it or deducted from it, until the required cash book balance emerges. The guiding test for each item is simple: ask whether the cash book figure should be higher or lower than the pass book figure because of that item. If the cash book should be higher, add; if lower, deduct. Applying this test: unpresented cheques (Rs. 15,700)

have reduced the cash book but not yet the pass book, so the cash book is lower — deduct. Uncleared cheques deposited have increased the cash book but not yet the pass book, so the cash book is higher — add. Bank charges of Rs. 1,350 have reduced the pass book only, so the cash book (which has not yet borne them) is higher — add. Amounts received directly by the bank from customers (Rs. 8,000) and dividend collected by the bank (Rs. 25,030) have increased the pass book only, so the cash book is lower — deduct both.

Transparency Note on the Booklet's Wording (please read): The booklet prints this item exactly as follows: "Cheques amounting to Rs. 25,750/- were deposited in the bank, but only cheques of Rs. 11,750/- had not been cleared up to 31st May." The word "only" conflicts with the rest of the sentence, because Rs. 11,750 is the smaller part of Rs. 25,750, not a surprising remainder. The statement below follows the sentence as printed literally — cheques of Rs. 11,750 had NOT been cleared, so Rs. 11,750 is the uncleared amount added in the reconciliation — and the printed total deposited (Rs. 25,750) then simply tells us that the remaining Rs. 14,000 was cleared and is not a reconciling item. If a tutor instead reads the sentence as meaning that cheques of Rs. 11,750 had been cleared (so that the uncleared part is Rs. 25,750 − Rs. 11,750 = Rs. 14,000), the same method gives a cash book overdraft of Rs. 2,880 instead of Rs. 5,130; the working for that reading is shown after the main statement so that the student can follow whichever reading the tutor adopts. The figures have not been altered or "corrected" anywhere in this guide.

Bank Reconciliation Statement of Ahmer Traders as on 31st May 2024

Particulars	**Rs.**	**Rs.**
Balance as per Pass Book (Credit balance)		30,500
Add: Cheques deposited but not yet cleared (uncleared cheques)	11,750	

Add: Sundry charges debited by the bank, not yet recorded in Cash Book	1,350	13,100
Sub-total		43,600
Less: Cheques issued but not yet presented for payment	15,700	
Less: Amount received directly by the bank from customers, not yet recorded in Cash Book	8,000	
Less: Dividend received by the bank, not yet recorded in Cash Book	25,030	48,730
Balance as per Cash Book — Bank Overdraft (credit balance in the bank column of the Cash Book)		(5,130)

The result deserves a moment's attention, because students often assume a wrong answer when a reconciliation ends in an overdraft. The pass book shows a comfortable credit balance of Rs. 30,500 only because it still contains two receipts that do not belong to the trader's own recording yet (Rs. 8,000 + Rs. 25,030) and has not yet paid out cheques of Rs. 15,700 which the trader has already treated as paid. Once the position is restated on the cash book basis — Rs. 30,500 + Rs. 11,750 + Rs. 1,350 − Rs. 15,700 − Rs. 8,000 − Rs. 25,030 = −Rs. 5,130 — the bank column of the cash book actually carries a credit balance of Rs. 5,130, that is, an overdraft as per the cash book. This is entirely possible in practice: a trader may issue cheques against expected collections and find that, on his own records, he has temporarily drawn more than his recorded balance, even though the bank's statement still shows funds because the cheques are unpresented. Discovering exactly this kind of danger in time is one of the main purposes of preparing the statement monthly.

Alternative Reading — Working

For completeness, the alternative reading mentioned in the transparency note is worked as follows. If cheques of Rs. 11,750 were the portion cleared, the uncleared portion is Rs. 25,750 − Rs. 11,750 = Rs. 14,000. Then: balance as per pass book Rs. 30,500; add uncleared cheques Rs. 14,000 and bank charges Rs. 1,350, giving Rs. 45,850; less unpresented cheques Rs. 15,700, direct receipts by the bank Rs. 8,000 and dividend Rs. 25,030, totalling Rs. 48,730; the result is again an overdraft as per the cash book, of Rs. 45,850 − Rs. 48,730 = Rs. 2,880. Observe that both readings agree on the method, on every other item, and even on the conclusion that the cash book is overdrawn; they differ only in the size of the uncleared figure, and that difference flows from the booklet's own ambiguous sentence, not from the accounting. After preparing the statement under either reading, the trader must also update his cash book itself with the bank-originated items — debiting bank charges and crediting the direct receipt and the dividend — because a reconciliation explains differences; it does not by itself correct the books.

Conclusion

The Bank Reconciliation Statement of Ahmer Traders as on 31st May 2024, prepared by the single balance method from the pass book credit balance of Rs. 30,500, arrives at a balance as per the cash book of Rs. 5,130 overdrawn (with the alternative reading of the booklet's uncleared-cheque sentence giving an overdraft of Rs. 2,880, as disclosed above). The exercise teaches the three habits that make reconciliations reliable: start from one balance only, test every item by asking which book should be higher, and never force the statement to agree by altering a printed figure.

Question 2

Q.2 Define a bill of exchange and describe the parties involved in it. Also, explain various types of bills of exchange with each example. (20)

Introduction

Credit is the lifeblood of trade, but no seller likes to part with goods against a bare verbal promise to pay later. Business therefore developed written, legally enforceable instruments by which a buyer's promise or a seller's order to pay is recorded, signed, and can even be transferred to a third person. The most important of these negotiable instruments is the bill of exchange. This answer defines the bill of exchange and its essential features, describes every party involved in it, and then explains its various types, giving a concrete example of each type as the question requires.

Definition and Essential Features

A bill of exchange may be defined as an instrument in writing containing an unconditional order, signed by its maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument. This is the sense of the definition used in negotiable instruments law in Pakistan (the Negotiable Instruments Act, 1881), stated here in substance rather than as a verbatim quotation. Every phrase of the definition carries a legal requirement. It must be in writing — an oral order is not a bill. The order must be unconditional: "pay when my ship arrives" is not a bill, because payment depends on an uncertain event. It must be an order, not a request or a promise; this is what separates a bill of exchange from a promissory note, which contains a promise by the maker himself to pay. The sum must be certain, the person to pay (the drawee) must be certain, and the person to be paid (the payee) must be certain or ascertainable. The maker must sign it, and in practice the drawee signs his acceptance across its face, by which he binds himself to pay on the due date. A simple specimen makes the form clear: "Lahore, 1st March 2026. Three months after date, pay to Mr. B

or order the sum of Rupees Fifty Thousand only, for value received. To Mr. A, Karachi. (Signed) Mr. C." Here C orders A to pay B, and once A accepts, A becomes primarily liable.

Parties to a Bill of Exchange

Three parties are essential, and a few more may join as the bill travels. (1) The Drawer is the person who draws (makes and signs) the bill and gives the order to pay; he is usually the seller or creditor, who wants his money from the buyer. In the specimen, C is the drawer. The drawer is liable to compensate the holder if the bill is dishonoured, provided due notice is given. (2) The Drawee is the person on whom the bill is drawn — the one ordered to pay; he is usually the buyer or debtor (A in the specimen). Before acceptance he is not liable on the bill at all; the moment he writes "accepted" and signs, he becomes the Acceptor, the party primarily liable to pay at maturity, and the bill is then called an acceptance in commercial language. (3) The Payee is the person to whom, or to whose order, the payment is to be made (B in the specimen); the payee may be the drawer himself, as happens when a seller draws a bill payable to his own order. Beyond these three, later parties can appear: an Endorser is a holder who signs the back of the bill to transfer it to another person, who then becomes the Endorsee and holder; the Holder is the person in possession of the bill entitled to payment; a Drawee in Case of Need is a person named in the bill to whom the holder may go for acceptance or payment if the original drawee refuses; and an Acceptor for Honour is a stranger who, after the bill has been noted for non-acceptance, accepts it to save the credit of the drawer. Understanding these roles matters because the rights of each party differ, and on dishonour the holder must give notice to the drawer and endorsers to preserve his claim against them.

Types of Bills of Exchange — By Time of Payment

(1) Demand Bill (Sight Bill): payable immediately on demand or on presentation ("at sight"). Example: a Karachi exporter draws a bill on a London importer expressed "at sight, pay to our order…"; the importer must pay as soon as the bill is presented to him, with no period of credit. (2) Term Bill (Time Bill or Usance Bill): payable after a specified period, such as 30, 60 or 90 days after date or after sight. Example: a Faisalabad textile mill sells cloth worth Rs. 500,000 to a retailer and draws a bill "three months after date"; the retailer accepts it, trades with the cloth in the meantime, and pays at maturity, with the customary days of grace added in computing the due date. Term bills are the commonest in trade because granting time to pay is their very purpose, and they can be discounted with a bank if the drawer needs cash earlier.

Types of Bills of Exchange — By Place and by Purpose

(3) Inland Bill: drawn and payable within the same country, with both drawer and drawee in that country. Example: the Faisalabad–retailer bill above, drawn in Pakistan and payable in Pakistan, is an inland bill. (4) Foreign Bill: drawn in one country and payable in another (or drawn on a person resident abroad). Example: a Sialkot sports-goods maker draws a bill in euros on its German buyer, payable in Hamburg; such bills are usually drawn in sets of two or three identical copies ("first of exchange", "second of exchange") sent by different mails so that if one copy is lost another remains valid, payment on any one copy cancelling the others. (5) Trade Bill: drawn and accepted for a genuine trade transaction, against actual goods sold. Example: the textile mill's bill against cloth actually delivered is a trade bill; banks discount such bills readily because real goods stand behind them. (6) Accommodation Bill: drawn and accepted without any trade transaction or value received, merely to oblige and financially assist the drawer, who discounts it and uses the money, undertaking to provide funds before maturity. Example: Mr. X, needing Rs. 200,000 for two months, draws a bill on his friend Mr. Y, who accepts it as an act of

friendship although X owes him nothing; X discounts the bill at his bank, and before the due date hands Y the money to pay it. Because no goods back it, an accommodation bill carries more risk, and the parties' liability between themselves differs from the position of an outside holder.

Types of Bills of Exchange — Other Varieties

(7) Documentary Bill: a bill to which the documents of title to goods — bill of lading, invoice, insurance policy — are attached, so the drawee gets the documents (and thus the goods) only on acceptance (documents against acceptance, D/A) or on payment (documents against payment, D/P). Example: an exporter ships surgical instruments to Dubai and sends the bill with shipping documents through his bank; the buyer must accept or pay before the bank releases the documents that let him clear the goods. (8) Clean Bill: a bill drawn without any documents attached, used where the parties know and trust each other. Example: a head office drawing routine monthly bills on its own branch, or a long-standing supplier drawing on a trusted customer, uses clean bills. (9) Fictitious Bill: a bill in which the name of the drawer or payee is fictitious (not a real person); it is a defective and dangerous variety mentioned mainly so students can recognise the term — unlike the other types, it is not a recommended commercial practice. Finally, bills are also described by their payee clause: a bill may be payable to bearer (rare and restricted for bills, since law requires most bills to be order bills) or to order, the latter being transferable by endorsement and delivery, which is the normal negotiable form used in trade.

Type	Distinguishing Feature	Example in Brief
Demand / Sight bill	Payable on presentation	Exporter's bill payable at sight by importer
Term / Usance bill	Payable after a fixed period	90-day bill for cloth sold on credit
Inland bill	Drawn and payable in one country	Faisalabad mill's bill on a local retailer
Foreign bill	Drawn/payable across countries; drawn in sets	Sialkot exporter's bill on a German buyer

Trade bill	Backed by a real sale of goods	Bill against goods actually delivered
Accommodation bill	Accepted to oblige; no value received	Friend accepts bill so drawer can discount it
Documentary bill	Shipping documents attached (D/A or D/P)	Bill with bill of lading sent through bank
Clean bill	No documents attached	Routine bill between trusted parties

Conclusion

A bill of exchange is thus a signed, unconditional written order by a drawer to a drawee to pay a certain sum to a payee, which becomes fully effective when the drawee accepts it. Its parties — drawer, drawee-cum-acceptor and payee, with endorsers, holders and others joining on transfer — each carry defined rights and liabilities, and its types, classified by time (demand and term), by place (inland and foreign), by purpose (trade and accommodation) and by documents (documentary and clean), equip it for almost every credit situation in domestic and international trade. That flexibility, backed by negotiable instruments law, is why the bill of exchange has remained a central instrument of commerce for centuries.

Question 3

Q.3 ABC Corporation Ltd. purchased machinery for Rs. 1,280,000 on 1st January 2024. It spent Rs. 45,000 on its carriage and installation. On 1st January 2026, additional machinery was purchased for Rs. 1,240,000, and old machinery was sold for Rs. 625,000 on the same date. The rate of depreciation to be charged is 20% p.a. Accounts are closed on 31st December every year. Prepare machinery account for the first five years under: (i) Straight-line Method; (ii) Diminishing Balance Method. (20)

Introduction

Depreciation is the systematic allocation of the cost of a fixed asset over its useful life, recognising that machinery loses value through use, wear and tear, passage of time and

obsolescence. Two classic methods of charging it are compared in this question. Under the Straight-Line Method (also called the Fixed Instalment Method), an equal amount is charged every year, calculated as a fixed percentage of the original cost of the asset. Under the Diminishing Balance Method (also called the Written Down Value Method), the same percentage is applied each year to the reducing (written down) balance of the asset, so the annual charge is large in the early years and smaller later. The question gives one old machine, sold after two years, and one new machine bought on the day of the sale, and asks for the combined Machinery Account for the first five years, 2024 to 2028, under each method in turn.

Working Notes — Cost and Depreciation of the Old Machinery

The cost of an asset for depreciation purposes is not merely its purchase price; every expense necessary to bring it to the place and condition for use is capitalised. The old machinery therefore cost Rs. 1,280,000 + Rs. 45,000 (carriage and installation) = Rs. 1,325,000. Under the straight-line method, annual depreciation is 20% of Rs. 1,325,000 = Rs. 265,000, charged for 2024 and 2025, so the book value on 1st January 2026 is Rs. 1,325,000 − Rs. 265,000 − Rs. 265,000 = Rs. 795,000. It was sold for Rs. 625,000, giving a loss on sale of Rs. 795,000 − Rs. 625,000 = Rs. 170,000, which is transferred to the Profit and Loss Account. Under the diminishing balance method, depreciation for 2024 is 20% of Rs. 1,325,000 = Rs. 265,000, leaving Rs. 1,060,000; for 2025 it is 20% of Rs. 1,060,000 = Rs. 212,000, leaving a written down value of Rs. 848,000 on 1st January 2026. Sold for Rs. 625,000, the loss on sale under this method is Rs. 848,000 − Rs. 625,000 = Rs. 223,000 — larger than under straight line, because the diminishing method had written the machine down more slowly in total over the two years (Rs. 477,000 against Rs. 530,000). No depreciation is charged on the old machine in 2026, because it was sold on the very first day of that year. The new machinery, bought on 1st January

2026 for Rs. 1,240,000, bears a full year's depreciation in 2026 and each later year: Rs. 248,000 a year under straight line (20% of cost), and under diminishing balance Rs. 248,000 in 2026, Rs. 198,400 in 2027 (20% of Rs. 992,000) and Rs. 158,720 in 2028 (20% of Rs. 793,600).

(i) Machinery Account — Straight-Line Method

Year / Date	Debit Side (Dr.)	Rs.	Credit Side (Cr.)	Rs.
1 Jan 2024	To Bank A/c (purchase 1,280,000 + carriage & installation 45,000)	1,325,000	By Depreciation A/c (20% of 1,325,000)	265,000
31 Dec 2024			By Balance c/d	1,060,000
	Total	1,325,000	Total	1,325,000
1 Jan 2025	To Balance b/d	1,060,000	By Depreciation A/c	265,000
31 Dec 2025			By Balance c/d	795,000
	Total	1,060,000	Total	1,060,000
1 Jan 2026	To Balance b/d 795,000; To Bank A/c (new machinery purchased)	2,035,000	By Bank A/c (old machinery sold) 625,000; By Profit & Loss A/c (loss on sale) 170,000; By Depreciation A/c (new machinery) 248,000; By Balance c/d 992,000	2,035,000
1 Jan 2027	To Balance b/d	992,000	By Depreciation A/c 248,000; By Balance c/d 744,000	992,000
1 Jan 2028	To Balance b/d	744,000	By Depreciation A/c 248,000; By Balance c/d 496,000	744,000
1 Jan 2029	To Balance b/d (closing book value of machinery)	496,000		

(ii) Machinery Account — Diminishing Balance Method

Year / Date	Debit Side (Dr.)	Rs.	Credit Side (Cr.)	Rs.
1 Jan 2024	To Bank A/c (purchase 1,280,000 + carriage & installation 45,000)	1,325,000	By Depreciation A/c (20% of 1,325,000)	265,000
31 Dec 2024			By Balance c/d	1,060,000
	Total	1,325,000	Total	1,325,000
1 Jan 2025	To Balance b/d	1,060,000	By Depreciation A/c (20% of 1,060,000)	212,000
31 Dec 2025			By Balance c/d	848,000
	Total	1,060,000	Total	1,060,000
1 Jan 2026	To Balance b/d 848,000; To Bank A/c (new machinery purchased)	2,088,000	By Bank A/c (old machinery sold) 625,000; By Profit & Loss A/c (loss on sale) 223,000; By Depreciation A/c (new machinery) 248,000; By Balance c/d 992,000	2,088,000
1 Jan 2027	To Balance b/d	992,000	By Depreciation A/c (20% of 992,000) 198,400; By Balance c/d 793,600	992,000
1 Jan 2028	To Balance b/d	793,600	By Depreciation A/c (20% of 793,600) 158,720; By Balance c/d 634,880	793,600
1 Jan 2029	To Balance b/d (closing book value of machinery)	634,880		

Comparison and Observations

Placing the two accounts side by side teaches the essential contrast between the methods. In 2024 the charge is identical (Rs. 265,000) because both methods start from the same cost. From 2025 the paths separate: straight line keeps charging Rs. 265,000 on the old machine, while diminishing balance charges only Rs. 212,000, since 20% is now taken on a smaller base. Consequently the old machine's book value at sale is lower under straight line (Rs. 795,000) than under diminishing balance (Rs. 848,000), and the loss on sale is correspondingly smaller under straight line (Rs. 170,000) than under diminishing balance (Rs. 223,000); the total charge to profit over the machine's life with the company — depreciation plus loss on sale — is, however, the same Rs. 700,000 under both methods (cost Rs. 1,325,000 minus sale proceeds Rs. 625,000), because the methods differ only in timing, never in the total ultimately written off. For the new machine the two methods agree again in 2026 (Rs. 248,000) and then diverge: by the end of the fifth year, 2028, the machinery stands at Rs. 496,000 under straight line against Rs. 634,880 under diminishing balance. Straight line is simpler and suits assets that render uniform service, such as buildings and leases; diminishing balance suits machinery and vehicles, whose repairs grow with age, because its high early depreciation plus low early repairs roughly equals its low later depreciation plus high later repairs, evening out the total annual burden on profit. All figures in both accounts have been cross-checked: every year's debit and credit totals agree, and each closing balance is the opening balance of the next year.

Conclusion

The Machinery Account of ABC Corporation Ltd. for 2024–2028 has been prepared under both methods from the capitalised cost of Rs. 1,325,000 for the old machine. Under the straight-line method the loss on sale is Rs. 170,000 and the closing book value at 31st December 2028 is Rs. 496,000; under the diminishing balance method the loss on sale is Rs. 223,000 and the closing

book value is Rs. 634,880. The comparison shows that the choice of method changes the timing of the charge against profit, not its lifetime total — the central lesson of depreciation accounting.

Question 4

Q.4 Following is the trial balance of Toor & Co. Prepare the Trading and Profit and Loss A/C & Balance Sheet for the year ended 31st Dec 2019. (20) Adjustments: (i) Closing stock was valued at Rs. 250,000. (ii) Outstanding insurance Rs. 9,000. (iii) Depreciation on building @ 10% p.a.

Introduction

This question carries the student through the final stage of the accounting cycle: converting a trial balance into the three final statements. The trial balance of Toor & Co. (as printed in the booklet, and reproduced in the working below) totals Rs. 21,70,640 on each side, so the books are arithmetically balanced and the final accounts can be prepared directly, after giving effect to the three printed adjustments. The Trading Account will find the gross profit by matching net sales against the direct cost of goods sold; the Profit and Loss Account will find the net profit by charging all indirect expenses (including the adjustments for outstanding insurance and depreciation) against the gross profit and indirect income; and the Balance Sheet will present the resulting financial position. Each figure used is traceable to the printed trial balance, and a student should reproduce that trial balance in the answer before the final accounts, exactly as the working notes below do.

Working Notes

Net sales = Sales Rs. 7,50,000 − Sales Return Rs. 26,250 = Rs. 7,23,750. Net purchases = Purchases Rs. 5,00,000 − Purchases Return Rs. 9,900 = Rs. 4,90,100. The debit item “Stock Rs. 1,33,500” in the trial balance is the opening stock of the year. Wages (Rs. 54,590) are a direct

expense and go to the Trading Account; rent (Rs. 2,24,000) is an indirect expense and goes to the Profit and Loss Account; commission (Rs. 27,000), appearing on the credit side, is income received and is credited in the Profit and Loss Account. Adjustment (i): closing stock Rs. 2,50,000 is credited in the Trading Account and shown as an asset in the Balance Sheet. Adjustment (ii): outstanding insurance Rs. 9,000 — no insurance premium appears anywhere in the printed trial balance, so the outstanding amount is treated as the insurance expense accrued for the year: it is debited in the Profit and Loss Account and shown as a current liability in the Balance Sheet; this treatment is also the one under which the Balance Sheet agrees exactly, as the verification below confirms. Adjustment (iii): depreciation on building at 10% of Rs. 4,55,000 = Rs. 45,500, debited to the Profit and Loss Account and deducted from Building in the Balance Sheet, leaving the building at Rs. 4,09,500. Drawings (Rs. 60,500) are neither an expense nor a liability of the firm to outsiders; they are deducted from capital. Machinery (Rs. 3,80,500) carries no depreciation adjustment in the booklet and is shown at its trial balance figure.

Trading Account of Toor & Co. for the Year Ended 31st December 2019

Debit Particulars	Rs.	Credit Particulars	Rs.
To Opening Stock	1,33,500	By Sales 7,50,000 − Sales Return 26,250	7,23,750
To Purchases 5,00,000 − Purchases Return 9,900	4,90,100	By Closing Stock	2,50,000
To Wages	54,590		
To Gross Profit c/d (transferred to Profit & Loss A/c)	2,95,560		
Total	9,73,750	Total	9,73,750

Profit and Loss Account of Toor & Co. for the Year Ended 31st December 2019

Debit Particulars	Rs.	Credit Particulars	Rs.
To Rent	2,24,000	By Gross Profit b/d (from Trading A/c)	2,95,560
To Insurance (outstanding, per adjustment ii)	9,000	By Commission	27,000
To Depreciation on Building (10% of 4,55,000)	45,500		
To Net Profit (transferred to Capital A/c)	44,060		
Total	3,22,560	Total	3,22,560

Balance Sheet of Toor & Co. as on 31st December 2019

Liabilities	Rs.	Assets	Rs.
Capital 8,23,740 + Net Profit 44,060 − Drawings 60,500	8,07,300	Building 4,55,000 − Depreciation 45,500	4,09,500
Loan	4,20,000	Machinery	3,80,500
Creditors	1,40,000	Debtors	3,30,000
Outstanding Insurance	9,000	Closing Stock	2,50,000
		Cash	6,300
Total	13,76,300	Total	13,76,300

Verification and Interpretation

The three statements verify each other completely. The Trading Account balances at Rs. 9,73,750 on both sides and yields a gross profit of Rs. 2,95,560, which is about 40.8% of net sales (Rs. 2,95,560 ÷ Rs. 7,23,750) — a healthy trading margin. The Profit and Loss Account balances at Rs. 3,22,560 and yields a net profit of Rs. 44,060: the margin falls sharply at the net

level chiefly because rent of Rs. 2,24,000 absorbs most of the gross profit, an observation that is exactly the kind of insight final accounts exist to provide, since it tells the proprietor that premises cost, not trading margin, is the pressure point of this business. The Balance Sheet totals agree at Rs. 13,76,300 on both sides — capital as adjusted Rs. 3,07,300, plus loan Rs. 4,20,000, creditors Rs. 1,40,000 and outstanding insurance Rs. 9,000 on the one side; building (net) Rs. 4,09,500, machinery Rs. 3,80,500, debtors Rs. 3,30,000, closing stock Rs. 2,50,000 and cash Rs. 6,300 on the other — and this exact agreement is the final proof that every trial balance item and every adjustment has been given its proper double effect. Two cautions for the student's own writing: closing stock, being an adjustment, appears twice (Trading Account credit and Balance Sheet asset), never in the trial balance itself; and outstanding insurance, likewise, appears twice (Profit and Loss debit and Balance Sheet liability), while depreciation appears as a Profit and Loss debit and as a deduction from the asset, not as a separate liability.

The Balance Sheet also rewards a careful reading of the firm's position. Fixed and long-term resources — building Rs. 4,09,500, machinery Rs. 3,80,500 and the long-term loan within the financing — dominate the statement, while current assets of debtors Rs. 3,30,000, closing stock Rs. 2,50,000 and cash Rs. 6,300 (total Rs. 5,86,300) comfortably exceed the current liabilities of creditors Rs. 1,40,000 and outstanding insurance Rs. 9,000 (total Rs. 1,49,000), so the firm is solvent in the short term. The one figure a lender would watch is cash of only Rs. 6,300: the business is profitable on paper, but most of its profit is locked up in stock and debtors, which is a liquidity observation, not a defect in the accounts, and a good illustration of why profit and cash are never the same thing.

Conclusion

For the year ended 31st December 2019, Toor & Co. earned a gross profit of Rs. 2,95,560 and a net profit of Rs. 44,060, and its Balance Sheet at that date balanced at Rs. 13,76,300 with closing capital of Rs. 8,07,300. The exercise demonstrates the complete logic of final accounts: every figure in the printed trial balance is used once if it belongs to the Trading or Profit and Loss Account and once if it belongs to the Balance Sheet, while each of the three printed adjustments is used twice, once for the period's performance and once for the position at its end.

Question 5

Q.5 Mr. Zubair runs a sole proprietorship business dealing in the manufacturing and sale of computer accessories. During August 2025 the transactions printed in the booklet were recorded. You are required to enter the transactions in the three-column cash Book. (20)

Introduction

The cash book is both a subsidiary book and, for cash and bank, a part of the ledger itself: it records all receipts and payments in chronological order, and its balances are taken directly into the trial balance. A three-column cash book carries, on each side, a discount column, a cash column and a bank column. The discount columns are memorandum (total) columns only — they are not balanced; their totals are posted to the Discount Allowed and Discount Received Accounts. The cash and bank columns are balanced like ordinary accounts. Entries that move value between cash and bank (depositing cash into the bank, or withdrawing it for office use) are contra entries, marked "C", and are not posted anywhere else because both aspects are inside the cash book itself. The booklet's introductory paragraph about Mr. Zubair's competitive market and product quality is background colour only; it creates no entry. The transactions for August 2025 printed in the booklet are entered below, each according to these rules, and the treatment of every item is explained after the cash book.

Three-Column Cash Book of Mr. Zubair — August 2025 (Debit Side: Receipts)

Date	Particulars	Discount (Rs.)	Cash (Rs.)	Bank (Rs.)
2025 Aug. 2	To Balance b/d (cash in hand; cash at bank)	—	13,00,000	5,22,500
Aug. 8	To Sales A/c (cash sales)	—	67,500	—
Aug. 12	To Mr. Farooq A/c (cheque received and deposited into bank; discount allowed 1,55,000 − 1,54,000)	1,000	—	1,54,000
Aug. 23	To Interest A/c (interest received from bank)	—	—	27,000
Aug. 25	To Cash A/c (C) — contra: cash deposited into bank	—	—	30,000
Aug. 28	To Mr. Asif A/c (cheque received, not yet deposited — treated as cash in hand)	—	60,000	—
Aug. 29	To Cash A/c (C) — contra: Mr. Asif's cheque deposited into bank	—	—	60,000
Aug. 30	To Bank A/c (C) — contra: cash withdrawn from bank for office use	—	10,000	—
	TOTALS (discount column is a memorandum total, not balanced)	1,000	14,37,500	7,93,500

Three-Column Cash Book of Mr. Zubair — August 2025 (Credit Side: Payments)

Date	Particulars	Discount (Rs.)	Cash (Rs.)	Bank (Rs.)
2025 Aug. 5	By Machinery A/c (machinery purchased — paid in cash, see note)	—	1,35,000	—
Aug. 15	By Mr. Furqan A/c (paid in cash and by cheque — see transparency note)	—	75,000	78,500
Aug. 17	By Purchases A/c (cash purchases)	—	25,500	—

Aug. 20	By Electricity Bill A/c (paid by bank)	—	—	15,000
Aug. 25	By Bank A/c (C) — contra: cash deposited into bank	—	30,000	—
Aug. 29	By Bank A/c (C) — contra: Mr. Asif's cheque deposited into bank	—	60,000	—
Aug. 29	By Mr. Kaleem A/c (paid by cheque)	—	—	70,000
Aug. 30	By Cash A/c (C) — contra: cash withdrawn from bank for office use	—	—	10,000
Aug. 31	By Drawings A/c (cash drawn from bank for personal use)	—	—	7,500
Aug. 31	By Balance c/d (closing balances)	—	11,12,000	6,12,500
	TOTALS	—	14,37,500	7,93,500
2025 Sep. 1	To Balance b/d (opening balances of September)	—	11,12,000	6,12,500

Transparency Note on a Booklet Defect (15th August): The booklet prints: "Payment to Mr. Furqan, cash Rs. 75,000/- and a cheque for Rs. 78,500 in full settlement of his account 150,000/-." The two payments total Rs. 75,000 + Rs. 78,500 = Rs. 1,53,500, which EXCEEDS the account said to be settled (Rs. 1,50,000) by Rs. 3,500. A payment in full settlement can earn discount received only when it is LESS than the amount owed, so no discount received can arise here, and none has been entered. The cash book above records the two payments exactly as printed (cash Rs. 75,000; bank Rs. 78,500), because a cash book must record what was actually paid; the resulting Rs. 3,500 excess would in real practice be an overpayment recoverable from Mr. Furqan or adjustable against future purchases, and the student may add one line noting this if the tutor wishes. No printed figure has been changed. A second, minor point: the booklet does not state how the

machinery of 5th August was paid for; it is entered as a cash payment, the normal convention when no bank or credit is mentioned, and this assumption is stated openly here.

Explanation of the Special Entries

Four groups of entries deserve explanation. First, settlements with discount: on 12th August Mr. Farooq owed Rs. 1,55,000 and his cheque of Rs. 1,54,000 was accepted in full settlement, so Rs. 1,000 is discount allowed, entered in the debit-side discount column with the cheque in the bank column because it was deposited the same day. Contrast Mr. Furqan: as the transparency note shows, his printed figures produce no discount at all. Secondly, contra entries: cash deposited into the bank on 25th August (Rs. 50,000), Mr. Asif's cheque deposited on 29th August (Rs. 60,000), and cash withdrawn for office use on 30th August (Rs. 10,000) each appear on both sides of the cash book, once in the cash column and once in the bank column, marked (C); they change the form in which the business holds its money, never the total of its money, and they require no posting to any other account. Thirdly, the cheque of 28th August: because Mr. Asif's cheque was received but not deposited, it is at that moment the equivalent of cash in hand and is entered in the cash column; when it is deposited the next day it moves, by contra entry, from the cash column to the bank column. Fourthly, drawings: the Rs. 7,500 drawn from the bank on 31st August for personal use is not a business expense at all; it is credited to the bank column and debited in the ledger to Drawings Account, and it will reduce Mr. Zubair's capital in the Balance Sheet, unlike the office withdrawal of 30th August, which is a pure contra entry within the business. Interest received from the bank (23rd August, Rs. 27,000) and the electricity bill paid by the bank (20th August, Rs. 15,000) are entered directly in the bank column, since no cash passed through the office.

Closing Balances and Verification

The cash book balances exactly. On the debit side the cash column receives Rs. 13,00,000 (opening) + Rs. 67,500 (sales) + Rs. 60,000 (Asif's cheque) + Rs. 10,000 (contra withdrawal for office) = Rs. 14,37,500; against this the credit side pays out Rs. 1,35,000 + Rs. 75,000 + Rs. 25,500 + Rs. 30,000 (contra) + Rs. 60,000 (contra) = Rs. 3,25,500, leaving a closing cash balance of Rs. 11,12,000. The bank column receives Rs. 5,22,500 (opening) + Rs. 1,54,000 (Farooq) + Rs. 27,000 (interest) + Rs. 30,000 (contra) + Rs. 60,000 (contra) = Rs. 7,93,500; payments are Rs. 78,500 (Furqan) + Rs. 15,000 (electricity) + Rs. 70,000 (Kaleem) + Rs. 10,000 (contra) + Rs. 7,500 (drawings) = Rs. 1,81,000, leaving a closing bank balance of Rs. 6,12,500. Both balances are therefore favourable (debit) balances, brought down as the opening balances of 1st September 2025, and the only discount of the month is the Rs. 1,000 allowed to Mr. Farooq, whose total will be posted to the credit of Discount Allowed Account in the ledger. The arithmetic has been checked column by column, and each side of each money column carries the same total, Rs. 14,37,500 for cash and Rs. 7,93,500 for bank.

Conclusion

All the August 2025 transactions printed in the booklet have been entered in Mr. Zubair's three-column cash book, closing with cash in hand of Rs. 11,12,000, cash at bank of Rs. 6,12,500 and discount allowed of Rs. 1,000. The exercise brings together every standard cash book skill: opening balances, cash and bank receipts and payments, discount on settlement, contra entries, a cheque in hand later deposited, bank-originated items such as interest and a bill paid by the bank, and the separation of business drawings from business expenses — together with one booklet misprint, disclosed openly in the transparency note rather than silently corrected.