

Financial Accounting
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Lecture – 41
3.6 Practice Problem I

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FINANCIAL ACCOUNTING

3.6 Practice Problem I

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I hope you are ready for some practice problems, let us look at one.

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Prepare Cash Account from following transactions

1. Started business with cash Rs 10,000
*Cash A/c Dr ✓
 To Owners Capital A/c ✓*
2. Deposited in to bank Rs 9000
*Bank A/c Dr
 To Cash A/c ✓*
3. Purchased machinery for Rs 5000 from ABC Ltd and gave a cheque for the amount.
*Machinery A/c Dr
 To Bank A/c ✓*
4. Paid installation charges on machinery Rs 100 in cash
*Machinery A/c Dr 100
 To Cash A/c 100 ✓*
5. Sold furniture to PQR Ltd Rs 1000
*PQR A/c Dr 1000
 To Sale 1000*
6. Received a cheque from PQR for Rs 990 in full settlement
*Bank A/c Dr 990
 Discount allowed A/c Dr 10
 To PQR 1000*
7. Paid wages Rs 350 and Rent Rs 200 in cash.
*Wages A/c Dr 200
 Rent A/c Dr 350
 To Cash ✓*
8. Paid to ABC Ltd 1900 by cheque in full settlement
*ABC Ltd A/c Dr 2000
 To Bank A/c 2000
 Discount A/c 100
 1900 ✓*

Cash ≠ Bank A/c

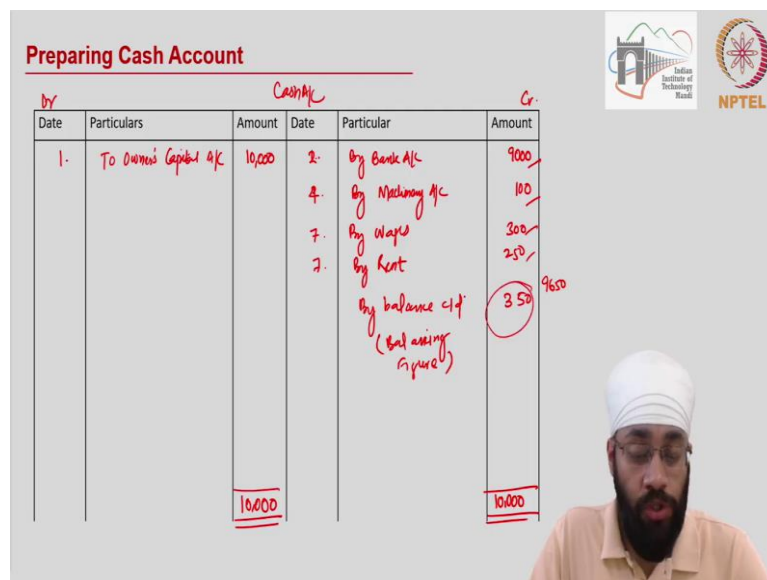
We have 8 transactions, and using these transactions we have to prepare a cash account. So, we only need to worry about preparing one account which is the cash account. Therefore, we are going to look at transactions that involve cash and you have to remember that now we are treating cash differently from bank account. So, you are looking for transactions which affect cash account only.

So, you write the journal entry, and then you go to the ledger posting; however, in this practice problem I will help you post the transactions directly into the ledger. So, we are going to do a quick journal entry here and then we are going to post that journal entry into a cash account, which I also have here on the next slide.

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Preparing Cash Account

<i>Dr</i>			<i>Cash A/c</i>			<i>Cr</i>		
Date	Particulars	Amount	Date	Particular	Amount			
1.	To Owner's Capital A/c	10,000	2.	By Bank A/c	9,000			
			4.	By Machinery A/c	100			
			7.	By Wages	300			
			7.	By Rent	250			
				By balance c/d (bal owing figure)	3,500			9,650
		10,000						10,000



So, I have a cash account: this is the debit side and this is the credit side. Let us look at the first transaction, it says started business with cash. Now this is cash. So, this transaction is going to be posted into the ledger account for cash. The journal entry for cash coming in to business is Cash A/c (Dr.), To Owner's Capital A/c or Share Capital A/c. I am not using a format for journal. I am just doing these working notes here for your convenience. So, cash account is a debit. I am going to the debit side of the cash account and write To Owner's Capital A/c 10,000. This is transaction number 1 and you are done with the first transaction.

Transaction 2 says, deposited into the bank. So, when cash is deposited into the bank, the journal entry is Bank A/c (Dr.) and cash goes out of the business to the cash account. So, cash

account is being credited. I will go to the credit side of the cash account and I will write By bank. So, by bank account the amount is 9,000 transaction 2.

Next up, purchase machinery rupees 5,000 from ABC and give a cheque for the amount. When you purchase machinery here your journal entry is Machinery A/c (Dr.)- not the purchase account, because this is an asset. You gave a cheque which means it is going to be paid through the bank. So, To Bank A/c and if you notice that, this transaction does not involve cash and cash and bank are being treated differently in this practice problem. So, we are not going to post transaction 3 into cash account.

Next up is paid installation charges on machinery and this is in cash. So, when you pay installation charges on machinery, we discussed this earlier, that up to the installation of an asset all the charges are added to the cost of the asset. So, the journal entry for this is going to be Machinery A/c (Dr.), To Cash and if you were to combine these to journal entries 3 and 4 then you would say Machinery A/c (Dr.), To Bank A/c, To Cash A/c and cash account will only have 100. So, the 5,000 rupees are paid through bank account, and 100 installation charges are paid in cash. So, in the cash account only 100 rupees are going to be entered. WE will go to the credit side of the cash account, and we write By Machinery A/c. This is transaction 4, the amount is 100.

Then you have sold furniture to PQR. When you sell furniture, you are receiving cash. If you are receiving cash- pardon, this is not a cash transaction, there is actually a credit transaction which is happening here. So, when you sell to PQR the journal entry is PQR account debit to sales, now there is no cash involved. So, we are not going to record this journal entry, not post this journal entry into the cash account. Then, we have received a cheque from PQR in full settlement, when you receive the cheque, it is going to come into your bank account. So, the journal entry is Bank A/c (Dr.), To PQR.

Now, when you had sold to PQR ,the amount was 1,000. So, you have to cancel the whole 1,000, but you are receiving only 990 therefore, there seems to be a discount allowed account, Discount Allowed A/c (Dr.) 10 rupees. However, none of this includes a cash account, therefore, we have to ignore this transition as far as the cash account is concerned.

Then, we have paid wages and rent. We can assume this to be in cash. So, you are going to say Wages A/c (Dr.), Rent A/c (Dr.), To Cash and this is 200 wages, 350 is rent. So, 550 is the total cash that is being paid, now this will go to credit side By wages and By rent. So, you have 300

and 250, this is transaction 7 and you posted this journal entry in the cash account. Let us go to transaction 8, you paid to ABC 1,900 by cheque in full settlement. When you paid to ABC, the journal entries ABC Limited A/c (Dr.) and you are going to pay through cheque. So, there is going to be a bank account involved, ABC's account was given a debit somewhere. So, ABC is also a vendor and you also purchased; you also purchased machinery from ABC. So, let us say 1,900 being paid in full settlement and you would have purchased from them for let us say 2,000. So, you are paying 1,900 and there is 100 rupees worth of discount which you are receiving, discount account and ABC Limited account debit 2,000. But the point is there is no cash involved here either. So, you cannot post this transaction into cash account.

So, these are all the transactions in the cash account and all we have to do is balance this account. So, you are going to total this debit side and we know that cash account always has a debit total. So, 10,000 and 10,000 here and you have this is 400 this is 650, 9,650 therefore, there is a balance of 350 in the cash account. So, by balance carried down this is a balancing figure; that means, we have calculated the sum of the two sides up and figured out the difference. So, this is the amount of cash that is left with you.

So, we have learnt in this practice problem is first that not all the transactions are going to be posted into cash account. You have to identify which transactions involve cash, and sometimes there is confusion if it is not stated clearly in the practice problems. Then you have to make an assumption if it is in cash or it is through the bank. But in practice you would always know whether cash has been paid or it has been paid through cheque, through bank. Secondly, all the journal entries written on this page are just working notes. Going forward, we would not write the journal entry but directly post the journal entry into the cash account by doing a mental journal entry and then posting it in the account directly.

We will do more practice and I will see you in the next practice problem.