

TRIAL BALANCE, RECTIFICATION OF ERRORS AND ADJUSTING & CLOSING ENTERIES

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.

- **Recording** of transaction is a Journal entry.
- **Summarizing** them and categorizing them are Ledgers.
- Creating a worksheet and classifying the ledgers is a Trial Balance.



A trial balance is a sheet recording all the ledger balances categorized into debit and credit. A typical trial balance will have name of ledger and the balances.

This is prepared as at a **particular date** 📅 which can be financial year end or calendar year.

Trial balance is a **statement** showing debit and credit balances taken from ledger including cash and bank balances as on a particular date.

Account	Debit	Credit
Purchases		
Sundry Debtors		
Stock (as on Apr, YYYY)		
Sales		
Cash at Bank		
Machinery		
Discount Received		
Bank Loan		
Bad Debts		
Sundry Creditors		
Carriage Outwards		
Capital		
Provision for Doubtful Debts		
Rent		
Discount Allowed		
TOTAL =		



FEATURES AND PURPOSE OF A TRIAL BALANCE

1. It is a **list of debit and credit balances** drawn from ledger.
2. It **includes cash and bank balances**.
3. Its main purpose is **to establish arithmetical accuracy** of transactions recorded in the books of account.

4. 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.
5. It enables the trader to know amounts receivable from customers and amounts payable to suppliers.
6. It facilitates preparation of final accounts.



TYPES OF TRIAL BALANCE AND PREPARATION OF TRIAL BALANCE

There are two types of trial balance:

1. **Gross** trial balance
2. **Net** trial balance

Gross Trial Balance

It is prepared in the following stages:

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

All these steps should be taken as on a particular date.

Net Trial Balance

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

DISAGREEMENT OF A TRIAL BALANCE

Trial balance is **prepared to verify arithmetical accuracy** of the transactions recorded in the books.

Under the double entry system of book-keeping, if all the transactions are correctly recorded through various books of prime entry, correctly posted there from to the ledger and if totaling is correct, then only the trial balance should tally.

But if there are a few mistakes committed by the persons

entrusted with the work of Journalising and posting, **the trial balance will not tally.**



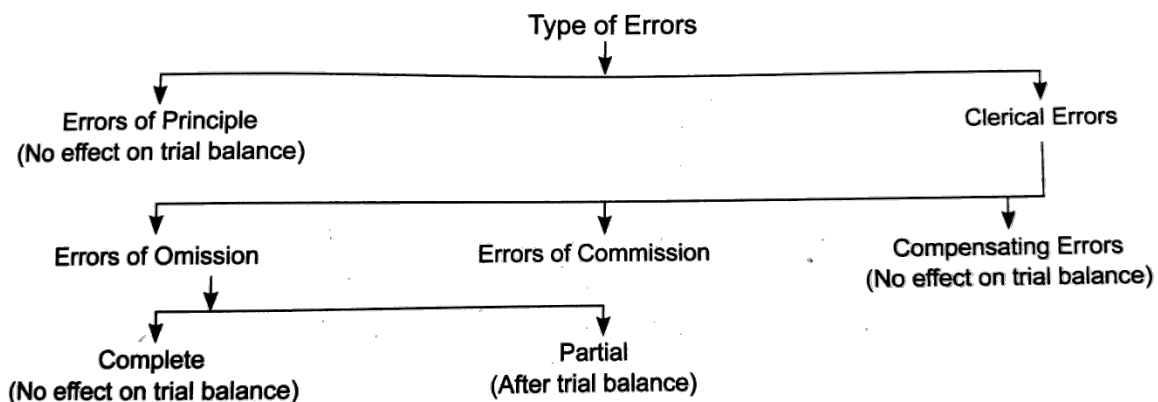
Also there are certain errors which are not disclosed even though the trial balance agrees.



CLASSIFICATION OF ERRORS

Errors can be broadly divided into two types:

1. Clerical errors
2. Principle errors



Clerical Errors

These errors can be divided into:

- (a) errors of **omission**
- (b) errors of **commission**
- (c) **compensating** errors

ERRORS OF OMISSION

- When a transaction is completely or partially omitted to be recorded in books of account, it is called an "Error of omission".

☞ Goods are purchased on credit from Mr. A. This transaction is not recorded in the purchase journal. This is called error of "Complete omission".

- If the above entry is recorded in purchase journal but remains to be posted to the supplier, Mr. A's account, then it will be called 'Partial omission'.

The error of complete omission does not affect the trial balance but the partial omission will result in disagreement of trial balance.

ERRORS OF COMMISSION

When an error is committed in recording a transaction with wrong amount or posting to wrong side of the account, it is called an 'Error of Commission'.

1. Posting of correct amount but on the **wrong side**
2. Posting of a **wrong amount** but on the correct side
3. Posting of a **wrong amount on wrong side** of an account
4. **Totaling error in subsidiary book**, i.e. purchase journal, sales journal, returns journal or totaling error in any ledger account.
5. A **mistake committed in balancing** of ledger account.

☞ Goods Sold to Mr A for Rs 5,000 recorded on credit side.

Correct Entry (What should have been recorded):

Mr. A A/c Dr. ₹5,000

To Sales A/c ₹5,000

(Being goods sold on credit to Mr. A)

Wrong Entry (What was actually recorded):

Sales A/c Dr. ₹5,000

To Mr. A A/c ₹5,000

(Wrongly recorded on credit side)

Rectification Entry:

Mr. A A/c Dr. ₹10,000

To Sales A/c ₹10,000

(Being rectification of earlier wrong posting)

☞ A credit sale of goods to Mr. A for Rs 3,000 recorded correctly in the sales journal but while posting to A's account, it is posted as Rs 300.

Error: A credit sale of goods to Mr. A for ₹3,000 was correctly recorded in the sales journal, but while posting to Mr. A's account, it was posted as ₹300.

Type of Error:

Error of Posting / Error of Amount

Correct Entry (What should have been posted):

Mr. A A/c Dr. ₹3,000

To Sales A/c ₹3,000

(Being goods sold on credit to Mr. A)

Wrong Posting Made:

Mr. A A/c Dr. ₹300

To Sales A/c ₹3,000

(Mr. A's account posted with incorrect amount)

Rectification Entry:

Mr. A A/c Dr. ₹2,700

(Being under-posting of ₹2,700 now corrected)

👉 An amount received from a customer Ramesh 2,000 recorded correctly in the cash book but posted to the debit side of Ramesh's account in the ledger.

Error: An amount of ₹2,000 received from customer Ramesh was correctly recorded in the cash book, but wrongly posted to the debit side of Ramesh's account instead of the credit side.

Type of Error:

Error of Posting / Posting to Wrong Side

Correct Entry (What should have been posted):

Cash A/c Dr. ₹2,000

To Ramesh A/c ₹2,000

(Being cash received from Ramesh)

Wrong Entry Posted:

Cash A/c Dr. ₹2,000

Ramesh A/c Dr. ₹2,000

(Ramesh's account wrongly debited)

Rectification Entry:

Ramesh A/c Cr. ₹4,000

(Being reversal of wrong debit of ₹2,000 and recording correct credit of ₹2,000)



Or in journal format:

Ramesh A/c Dr. ₹2,000

To Ramesh A/c ₹4,000

(Being rectification of wrong debit instead of credit)

These errors will result in disagreement of trial balance.

COMPENSATING ERRORS

When one mistake nullifies the wrong effect of another, it is called a compensating error. These are two or more in number and balance each other. These are generally arithmetical errors.

E.g.

- Salary Paid Rs 25000 recorded as Rs 52000
- Goods Purchased 30000 recorded as Rs 3000.

ERRORS OF PRINCIPLE

These are errors arising from not observing the accounting principles correctly.

- ☛ Wages paid for installation of machinery debited to wages account,
- ☛ purchase of fixed asset on credit recorded in purchase journal.

These errors will not affect agreement of trial balance.

1. Goods sold to X for Rs. 10,000 recorded as Rs. 6,000

Error:

Goods sold to X for ₹10,000 was recorded as ₹6,000, i.e., ₹4,000 was under-recorded.

Type of Error:

Error of Amount / Error of Underposting

Correct Entry (What should have been passed):

X A/c Dr. ₹10,000

To Sales A/c ₹10,000

(Being goods sold on credit to X)

Wrong Entry Passed:

X A/c Dr. ₹6,000

To Sales A/c ₹6,000

Rectification Entry:

X A/c Dr. ₹4,000

To Sales A/c ₹4,000

(Being correction of under-recorded credit sale to X)

2. Goods sold to X for Rs. 10,000 recorded as Rs. 15,000

Error:

Goods sold to X for ₹10,000 was recorded as ₹15,000, i.e., ₹5,000 was over-recorded.

Type of Error:

Error of Amount / Overposting

Correct Entry (What should have been passed):

X A/c Dr. ₹10,000

To Sales A/c ₹10,000

(Being goods sold on credit to X)

Wrong Entry Passed:

X A/c Dr. ₹15,000

To Sales A/c ₹15,000

Rectification Entry:

Sales A/c Dr. ₹5,000

To X A/c ₹5,000

(Being correction of over-recording of credit sale to X)

3. Goods sold to X for Rs. 10,000 recorded in purchase A/c

Error:

Goods sold to X for ₹10,000 was **wrongly recorded in Purchase A/c** instead of Sales A/c.

Type of Error:

Error of Principle

Correct Entry (What should have been passed):

X A/c Dr. ₹10,000

To Sales A/c ₹10,000

(Being credit sale made to X)

Wrong Entry Passed:

Purchase A/c Dr. ₹10,000

To X A/c ₹10,000

Rectification Entry:

Sales A/c Dr. ₹10,000

X A/c Dr. ₹20,000

To Purchase A/c ₹10,000

(Being rectification of credit sale wrongly recorded as purchase)

 **Explanation:**

- Reverse wrong credit to X by debiting ₹10,000
- Record correct debit to X by debiting additional ₹10,000
- Cancel wrong debit to Purchase by crediting ₹10,000

4. Goods Purchased from Mr X for Rs. 20,000 Purchase A/c Dr with Rs. 15,000

Error:

Goods purchased from **Mr. X** for ₹20,000 was recorded as ₹15,000 in **Purchase A/c**, i.e., ₹5,000 was under-recorded.

Type of Error:

Error of Amount / Underposting

Correct Entry (What should have been passed):

Purchase A/c Dr. ₹20,000

To Mr. X A/c ₹20,000

(Being goods purchased on credit from Mr. X)

Wrong Entry Passed:

Purchase A/c Dr. ₹15,000

To Mr. X A/c ₹15,000

Rectification Entry:

Purchase A/c Dr. ₹5,000

To Mr. X A/c ₹5,000

(Being correction of under-recording of credit purchase from Mr. X)

Types of Errors that do not affect the Trial Balance

1. Error of complete omission
2. Error of Commission
3. Error of Principle
4. Compensating Error

RECTIFICATION OF ERRORS

ONE-SIDED ERRORS

One-sided errors, when located before preparing a trial balance, can be rectified by simply correcting the posting.



No entry is required to be passed as it affects only one account.

1. Salary paid Rs. 8,000 posted as Rs. 80,000
2. Sales register undercast by Rs. 100
3. Amount received from Suresh Rs 200 posted to his debit.



TWO-SIDED ERRORS

Two or more accounts are affected and mostly affected with equal amount.



1. Goods Sold to X Rs. 10,000- omitted to be recorded.

 Particulars	 Details
Type of Error	Error of Omission (Complete omission)
Nature of Transaction	Credit sale to Mr. X for ₹10,000
Error Description	Transaction was completely omitted from the books
Correct Entry (Which was missed)	X A/c Dr. ₹10,000
	To Sales A/c ₹10,000
Rectification Entry to be Passed	X A/c Dr. ₹10,000
	To Sales A/c ₹10,000
Reason	Since the transaction was not recorded at all, the original entry itself is passed now

2. Goods Sold to X Rs. 10,000- recorded Rs. 6,000.



 Particulars	 Details
Type of Error	Error of Amount (Underposting)
Nature of Transaction	Credit sale to Mr. X for ₹10,000
Error Description	Recorded only ₹6,000 instead of ₹10,000
Correct Entry	X A/c Dr. ₹10,000
To Sales A/c ₹10,000	
Wrong Entry Passed	X A/c Dr. ₹6,000
To Sales A/c ₹6,000	
Rectification Entry to be Passed	X A/c Dr. ₹4,000
To Sales A/c ₹4,000	
Reason	To correct the under-recording of ₹4,000 in both X's and Sales accounts

3. Goods Sold to X Rs. 10,000- recorded Rs. 25,000.

 Particulars	 Details
Type of Error	Error of Amount (Overposting)
Nature of Transaction	Credit sale to Mr. X for ₹10,000
Error Description	Recorded as ₹25,000 instead of ₹10,000 (Over by ₹15,000)
Correct Entry	X A/c Dr. ₹10,000
To Sales A/c ₹10,000	
Wrong Entry Passed	X A/c Dr. ₹25,000
To Sales A/c ₹25,000	

Rectification Entry to be Passed	Sales A/c Dr. ₹15,000
To X A/c ₹15,000	
Reason	To reverse the excess amount wrongly posted in both X's and Sales accounts

4. Goods Sold to X Rs. 10,000- recorded in purchase book.

 Particulars	 Details
Type of Error	Error of Principle
Nature of Transaction	Credit sale to Mr. X for ₹10,000
Error Description	Instead of recording in Sales Book, it was recorded in Purchase Book
Correct Entry	X A/c Dr. ₹10,000
To Sales A/c ₹10,000	
Wrong Entry Passed	Purchase A/c Dr. ₹10,000
To X A/c ₹10,000	
Rectification Entry to be Passed	Sales A/c Dr. ₹10,000
X A/c Dr. ₹20,000	
To Purchase A/c ₹10,000	
Reason	Reverse wrong credit to X and wrong debit to Purchase A/c, then pass correct entry

SUSPENSE ACCOUNT AND RECTIFICATION

- After preparation of a trial balance, if there is a difference, it may be temporarily transferred to a new account called "**Suspense**".
- **Suspense account is a temporary account.**

- During the course of checking or audit, some one-sided errors may be found out.
- To rectify these one-sided errors, second account can be suspense account, as the difference is transferred to suspense account.

RECTIFICATION OF ERRORS WHEN BOOKS ARE CLOSED

When difference in trial balance remains even after applying various checks, it is carried forward to the balance sheet on the appropriate side, as preparation of final accounts cannot be delayed indefinitely.

Personal accounts balances, i.e, those of customers and suppliers are carried forward to the next year.

But nominal accounts (expenses and incomes accounts) are always closed by transferring these to trading and profit and loss account.

Any difference located in nominal accounts, in the next year, cannot be adjusted to the nominal accounts, as this will affect current year's profit and loss.

Therefore, a new account '**Profit and Loss Adjustment account**' will be opened to rectify the errors in nominal account. The balance in this account is then directly transferred to capital account.

Error: Wages ₹10,000 of last year not recorded.

Profit & Loss Adjustment A/c Dr. ₹10,000

To Outstanding Wages A/c ₹10,000

(Being previous year's unrecorded wages now adjusted)

ADJUSTING AND CLOSING ENTRIES



Adjusting Entries

- At the end of the accounting year, all ledger accounts are balanced and then a 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.**



ADJUSTING ENTRIES: 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.

Like accrued revenue (receivables), accrued expenses (payables), prepaid expenses (asset), prepaid revenue (liability).



Closing Entries

- At the end of each year, all accounts of expenses and incomes must be closed.

- The balances of these accounts are transferred to trading account and profit and loss account. The entries passed to transfer these balances are called Closing Entries.