

# Book-Keeping

## for Secondary Schools

Student's Book Form One



Tanzania Institute of Education



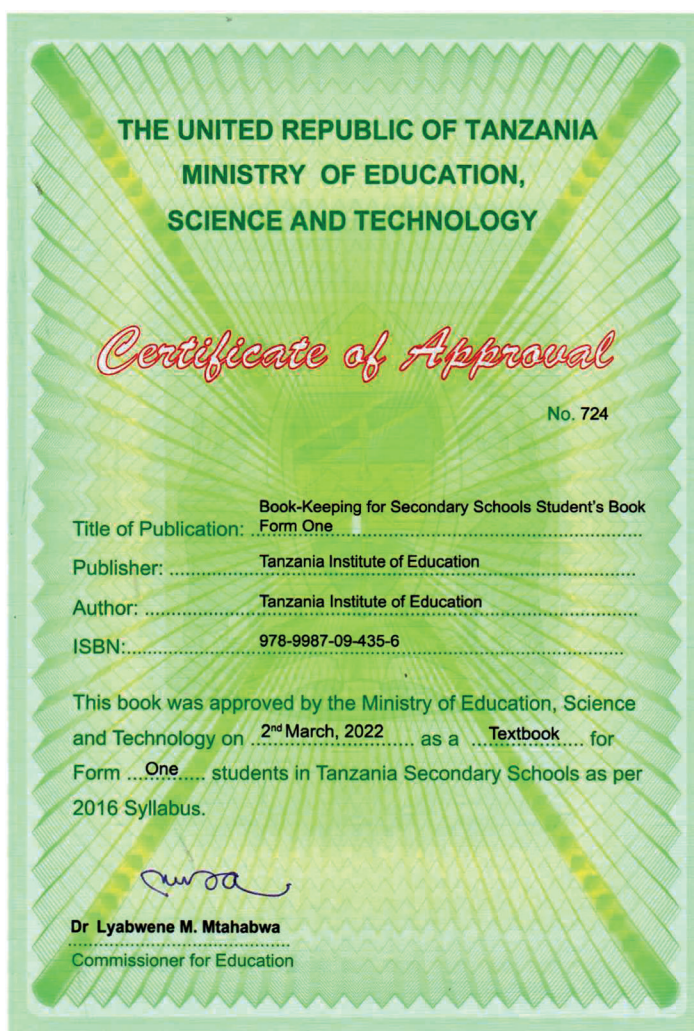


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Tanzania Institute of Education

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Dr Aneth A. Komba  
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# Preface

This textbook, *Book-Keeping for Secondary Schools*, is written specifically for Form One students in the United Republic of Tanzania. It is written in accordance with the 2016 Book-Keeping Syllabus for Ordinary Secondary Education Form I-IV, issued by the Ministry of Education, Science and Technology.

The book consists of six chapters, namely Introduction to Book-Keeping, The principles of double entry, Books of prime entry, Ledgers, Trial balance, and Elementary financial statements. Each chapter contains activities and exercises while some chapters have illustrations. You are encouraged to do all the activities and exercises as well as other assignments provided by your teacher. Doing so will enable you to develop the intended competencies.

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# Chapter One ►

## Introduction to Book-Keeping

### Introduction

*One of the major functions of all business persons is to keep business financial records. For business persons to keep proper records of their financial transactions, they need to establish the habit of recording all financial matters related to their business. In this chapter, you will learn the concept of Book-Keeping, relationship of Book-Keeping and other subjects, basic accounting concepts and principles, and the relevance of accounting concepts and principles in Book-Keeping that govern the recording of financial transactions in the books of accounts. The competencies developed in this chapter will enable you to describe the importance of Book-Keeping and apply accounting principles in recording financial transactions correctly.*

### Concept of Book-Keeping

#### **Financial transaction:**

*This is a business event that has financial value capable of being recorded in books of accounts using double entry system of Book-Keeping.*

#### **Occupation:**

*This is a person's principal work or business used as a means of earning a living.*

One of the common **occupations** that form an important part of a day to day income generation in any country is

business. Business may be conducted by large companies both locally and internationally, but a significant number of people in business are persons conducting small businesses. We interact with small businesses every day in the process of buying our daily necessities. Typical small businesses include food vending (mama/baba lishe), vegetables kiosks, street retail shops, shoe shining, newspaper vending, salon businesses and many others. All these businesses make different **financial transactions** such as buying inputs or materials, doing some processing, and selling their products or delivering services.



Book-Keeping is a necessary process for any business enterprise. Even business operators or owners without a proper knowledge of Book-Keeping will somehow unknowingly apply Book-Keeping principles in order to achieve various objectives of their businesses.

Take an example of Mrs Misosi who starts a food vending business by the name of Misosi-poa. This business operates near Soma-sana Secondary School in Tarangire. The business will need equipment like cookers, pans and serving utensils. It will also need some furniture such as benches, tables and cupboards. It will buy raw food and cook it for sale. To ensure that the food business runs successfully, Mrs Misosi would have to do the following:

- (i) Employ some cooks and service attendants;
- (ii) Supervise cooking operation;
- (iii) Sell food;
- (iv) Receive cash from sales made; and
- (v) Record credit sales (in case some food is sold on credit).

All these activities will involve a movement of money. At the end of the day, Mrs Misosi would need to evaluate whether the business is achieving its objectives. One of the likely objectives is to make a profit from such operations. This means that Mrs Misosi will need to calculate whether her business has generated a profit or not. To be able to determine the profit (or a loss), some calculations will have to be done by comparing the sales (revenue) made from

selling food against the costs of materials and services used. To do this, there would be a need to keep records of the money paid on each material and services, as well as the money received from selling food to customers. Simply put, the process of keeping records of money spent on each material and service as well as money received from selling goods to customers is what is known as “Book-Keeping”.

### **Meaning of Book-Keeping**

Book-Keeping is an important part of the accounting process as it plays an important role in the early stages in the accounting process. As explained earlier, Book-Keeping can be defined as the art of recording business financial transactions in the books of accounts in an orderly manner. In principle, every transaction has to be recorded in a systematic manner, which includes proper classification according to the nature of the transaction. The end result of Book-Keeping is having net figures or balances that will help to determine a profit or a loss and the financial position of the business. Apart from profit or loss determination, Book-Keeping also helps in the management of credit dealings, proper control of the business and appropriate computation of taxes.

### **Relationship of Book-Keeping with other subjects**

Book-Keeping supports school subjects and other disciplines in the realisation of their intended benefits. Book-Keeping knowledge and skills are applied in almost

all subjects that are set in the Secondary Education Curriculum. The relationship that exists between Book-Keeping and some other subjects is explained as follows:

### ***Accountancy***

Book-Keeping is the basis of the Accountancy subject. It records and posts entries to various ledgers that are used by accountants to analyse, interpret and make informed decisions about a business. Accountants produce accounts reports popularly known as financial statements, which show not only the income and financial positions of businesses or institutions but also other financial information. Financial information is important for business management, investments, tax assessment, and government activities. Therefore, without the knowledge of Book-Keeping, it would be difficult, if not impossible for accountants to prepare and analyse financial statements.

### ***Commerce***

Book-Keeping provides skills for preparing manufacturing accounts and how to accumulate various costs which are related to commercial activities. Thus, to accumulate data for evaluation of business performance in commercial activities (advertising, transportation, and production), you need to have knowledge and skills of Book-Keeping.

### ***Information and Computer Studies***

Information and Computer Studies (ICS) subject provides knowledge and skills to

process data and information. Some of the information collected is obtained from accounting books prepared by bookkeepers. ICS provide tools that enable bookkeepers together with accountants to prepare and analyse, interpret and add meaning to the processed data so that financial reports produced are good and attractive. The correct and neatness of the financial reports help users to make informed decisions.

### ***Agriculture***

Agriculture deals with farming management that requires preparation of farm records and farm accounting. This includes depreciating the value of farming equipment and keeping inventories of farm produce. The analysis of farming accounts is done after preparing their books of accounts. In order to do that, you need to have Book-Keeping knowledge and skills.

### ***Economics***

Book-Keeping knowledge allows students of Economics to be able to calculate both real and opportunity costs. Also, Book-Keeping lays down skills for maintaining economics records, calculating national income, performing cost analysis and production costs.

### ***Home Economics***

Home Economics is a subject which deals with projects and other activities at household level. For the projects to be sustainable, they need to apply Book-Keeping knowledge in keeping different

financial records, for example, costs and revenue associated with those projects. Eventually, by applying Book-Keeping knowledge, it will be possible to determine whether the projects are beneficial or not.



### Activity 1.1

Visit any nearby food or mobile money vendor shops and investigate various activities involving keeping financial records. Thereafter, read textbooks or online resources and then, discuss with your colleagues about what is meant by the term Book-Keeping?

## The importance of Book-Keeping

Book-Keeping is important to business owners and other parties outside of an enterprise for the following reasons:

### Determination of profits

Book-Keeping helps a business to determine whether it is making a profit or a loss. This is possible because Book-Keeping helps an enterprise to keep complete, accurate and up-to-date financial records. If we take an example of Misosi-poa above, Book-Keeping will assist the business to calculate profits or losses made for the year from the food vending business.

### Knowledge of credit transactions

Many businesses are conducted both on cash and credit basis. Misosi-poa, for example, would sell most of its food for cash, but it would occasionally sell to

some customers on credit, who promise to pay for the food later. Similarly, it is possible that Misosi-poa buys some of its raw foods on credit from the market. In practice, many businesses have a significant volume of their transactions conducted on credit. Book-Keeping helps enterprises to maintain appropriate records of their credit transactions and know the amount due from each of its **debtors** and the amount owing to each of its **creditors** since such records can systematically be kept following Book-Keeping principles.

#### Debtor:

*This is a customer who buys from a seller on credit and promises to pay at a later date. Another name is Account receivable or simply “receivables”.*

#### Creditor:

*This is a supplier who sells to us on credit and we promise to pay at a later date. Another name is Account payable or simply “payables”.*

### Control of business

To have an effective control of a business, the owner of the business needs to keep proper records of her financial matters. These records, in the long run, help the owner or proprietor to decide on matters such as expansion or reduction of the business. If Misosi-poa sells breakfast, lunch and dinner; appropriate record keeping may assist in deciding on the effort to dedicate to each of the menus. Additionally, in case the food is sold from more than one location or centre;



Book-Keeping may suggest whether the volume in one or another centre may need to be expanded or reduced according to the sales records. Book-Keeping can also help the proprietor to detect errors, fraud, and any misappropriation of funds. This can be useful in making a decision on the corrective measures to be taken where necessary.

### ***Determination of business's financial position***

Book-Keeping helps the owner to determine the financial position of his or her enterprise. It enables him or her to understand the value of assets, liabilities, and the amount of capital contributed by the owner. This can be useful in establishing whether the business has grown or not. Knowing the financial position of a business can also assist in case it needs to apply for a bank loan for expanding its operations.

### ***Tax assessment***

Tax authorities such as the Tanzania Revenue Authority (TRA) and Zanzibar Revenue Board (ZRB) need to see and examine the books of accounts of every enterprise operating in the United Republic of Tanzania. This is important in calculating the amount of tax that should be paid by the enterprises. Thus, a proper keeping of financial records helps both the owner and tax authorities to assess the amount of tax payable. Tax laws in Tanzania also penalise businesses that do not maintain financial documents and records properly. Book-Keeping therefore, may help the business save money that would otherwise be paid as

a penalty for not maintaining financial records. Figure 1.1 (a) and (b), show logos of Tanzania Revenue Authority and Zanzibar Revenue Board respectively.



(a)



(b)

**Figures 1.1: Logo (a) TRA's (b) ZRB's**

### **The accounting process or accounting cycle**

The determination of a profit or a loss, together with other objectives as we will get to learn later in this subject are done through the preparation of financial statements. The process that businesses use to prepare financial statements is known as the accounting process or accounting cycle. The accounting process involves eight stages and Book-Keeping plays an active role in the first seven.

The stages in the accounting process are summarised as follows:

Eight basic stages in the accounting cycle:

- (i) Identifying transactions and recording in source documents;
- (ii) Recording the transactions in the books of prime entry;
- (iii) Posting transactions to the ledger accounts;
- (iv) Extracting the trial balance;
- (v) Making adjusting entries and correction of errors;
- (vi) Extracting the adjusted trial balance;
- (vii) Preparing financial statements; and
- (viii) Analysing and interpreting the financial statements.

### **Identifying transactions and recording in source documents**

This is the first stage in the accounting process where financial transactions are identified and evidenced through source documents such as receipts, payment vouchers, invoices, cheques, debit note and credit note. For a transaction to be identified and evidenced, it must be of a financial value and it must affect at least two items of the accounting equation.

### **Recording the transactions in the books of prime entry**

After identifying the transaction, the second stage is to record that transaction in the books of prime entry which are also known as books of original entry. The transaction is initially recorded in these books before is recorded or posted anywhere else. For now, students should

know that there are six types of books of prime entry, namely a sales journal, a purchases journal, a sales returns journal, and a purchase returns journal, a general journal and a cash book.

### **Posting transactions to the ledger accounts**

The third stage in the accounting cycle is posting transactions to ledger accounts. This process involves the posting of entries that were initially recorded in the books of prime entry to ledger accounts. The posting of entries to respective ledger accounts is done by following the double entry system of Book-Keeping.

### **Extracting the trial balance**

The fourth stage in the accounting cycle is the extraction of the trial balance. The trial balance is a list (statement) prepared at a specific date showing net figures or balances of all ledger accounts. The account balances extracted from the ledger are listed in the debit and credit columns of the trial balance. The debit and credit columns must balance. The trial balance is usually prepared to check the correctness of double entries made to ledger accounts and it acts as a compiled list of balances for use in the preparation of financial statements.

**Account:** This is a summarised record of a business transaction. It can be presented on a page of a ledger book.

**Debit and Credit:** These are two terms which are used to describe the two sides of an account, that is, the left hand side (Debit) and the right hand side (Credit).

**Double entry:** *The system or principle of Book-Keeping whereby each business transaction is supposed to be recorded twice.*

**Accounting equation:** *Is a statement showing that resources in the business are equal to liabilities owed and capital contributed by the owner.*

### ***Making adjusting entries and correction of errors***

A Trial balance is expected to reveal some errors made when transactions are entered in the books of prime entry or when double entry is done in the ledger. These errors together with some adjustments need to be corrected or adjusted before the preparation of financial statements.

### ***Extracting the adjusted Trial balance***

When the trial balance does not balance, it shows that there are some errors or wrong postings of financial records. After all the errors have been corrected and entries adjusted, the adjusted trial balance will need to be prepared.

### ***Preparing the financial statements***

Financial statements (which include an income statement and a statement of financial position) are prepared using figures extracted from the adjusted trial balance. The aim of preparing the income statement is to know whether an enterprise is making a profit or a loss while the statement of financial position is prepared to know the total values of assets, liabilities and equity of the enterprise as at a certain date.

### ***Analysing and interpreting the financial statements***

The financial statements need to be analysed and interpreted so as to be able to assess the performance of the enterprise in comparison with others, as well as the progress made from one period to another. One of the tools used for analysing financial statements is ratio analysis. Analysed financial statements are useful to several users of financial information such as owners, lenders and creditors to assist them in making informed decision.

### ***The relationship between Book-Keeping and Accounting***

Mistakenly, quite a number of people use the terms Book-Keeping and Accounting interchangeably. This is because they think that Book-Keeping and Accounting are the same while in reality, they are not. The main relationship between Book-Keeping and Accounting is that, Book-Keeping is the basis of Accounting process. It records and posts entries to various ledgers that are used in accounting process. The most important difference is that Accounting has a broader horizon, including deciding about the accounting system and policies, and analysing the financial statements. Book-Keeping, on the other hand, concentrates on analysing the transactions, recording and processing them to generate the financial statements following the chosen system and accounting policies. The following are the differences between Book-Keeping and Accounting.

### The differences between Book-Keeping and Accounting

Book-Keeping	Accounting
(a) It is concerned with the recording of business financial transactions in the books of accounts.	(a) It is more extensive since it deals with classification, summarisation, and interpretation of financial statements.
(b) It is based on accounting policies and systems already laid down.	(b) It lays down policies and systems for use in Book-Keeping.
(c) It is done according to accounting standards and concepts.	(c) It is done according to accounting standards but techniques used for analysing and interpreting financial statements vary from firm to firm.
(d) Book-Keeping serves the purpose of having the transactions recorded in books and reflected in the financial statements.	(d) It ensures that the system is in place for having the Book-Keeping process undertaken, and spans further into making appropriate assumptions and estimates.
(e) It requires skills in double entry system of Book-Keeping.	(e) In addition to Book-Keeping skills, accounting requires analytical skills, industry experience and deep understanding of accounting standards.



#### Exercise 1.1

1. What are the differences between Book-Keeping and Accounting?
2. How is Book-Keeping as a subject related to other subjects?
3. Why is it important to learn Book-Keeping as a subject?
4. Explain seven stages of the accounting process?

### Common terms used in Book-Keeping

There are several common terms used in the subject of Book-Keeping. The following is a list of common terms used:

#### Business

It is any legal activity undertaken with the aim of making profit. Examples of business include farming, a restaurant, a salon and a kiosk.

#### Capital

It is the amount of money or money's worth provided by the owner to start an enterprise or to expand it. The money contributed by the owner can be used to finance business operations, or grow and expand the business.

#### A sole proprietor

A sole proprietor also known as a business person, is the owner of an enterprise



who provides capital to start or expand the enterprise. The sole proprietorship is the form of business enterprises that is owned by one person. In most cases, sole proprietorship is a family business and is the easiest type of business to establish and operate because it is not highly regulated by the government.

### **Goods**

These are items bought and sold by the proprietor; and they have the characteristics of being seen and touched. Goods are sold by business people to satisfy the needs of customers. Examples of goods include pens, exercise books, hats, food, mobile phones and clothes.

### **Services**

These are activities served or provided by an enterprise in the course of the business but the activities are neither seen nor touched. Examples of services offered by enterprise are hairdressing, drama, advertising and training.

### **Profit**

It is the result achieved by the business when revenues are greater than expenses. In other words, profit is the excess of revenue over expenses. Generally, the goal of every enterprise is to make profit

### **Loss**

A business is said to have made a loss when expenses are greater than revenues. A loss is not desired by any enterprise because it reduces the amount of capital of such enterprises.

### **Transaction**

A transaction is a business event that has monetary impact on business financial statements, and is recorded as an entry in its accounting record. It also refers to the movement of money or money's worth between two or more parties. For example, Juma paid Paula TZS 20,000 to buy a pair of shoes. This is a transaction because TZS 20,000 have been transferred from Juma to Paula and at the same time the pair of shoes has been transferred from Paula to Juma.



#### **Activity 1.2**

Visit any nearby business undertaking(s) and investigate various activities involving exchange of goods or services between a seller and a buyer. Thereafter, read textbooks or online resources, and then discuss with your colleagues about the meaning of the term business transaction.

### **Debtor**

This term refers to a customer who buys goods or services from an enterprise on credit. Thus, a debtor is a person who owes money, that is, has an obligation to the business. The amounts receivable from the debtors of the enterprise is an asset to such enterprise and is treated as a current asset in the statement of financial position. The other name for a debtor is accounts receivable.

### **Creditor**

This refers to a person who sells goods or renders services on credit to an enterprise.

Therefore, a creditor is a person to whom the enterprise owes money. The amounts payable to creditors of the enterprise is a liability to that enterprise and is treated as a current liability in the statement of a financial position. The other name for a creditor is accounts payable.



### Activity 1.3

Sakara is a businessman who does not have a Book-Keeping knowledge and has been running a restaurant for years. His friend, Kipara told Sakara about you, specifying that you are a student studying Book-Keeping at Busara Secondary School. He informs Sakara that you can explain some of the basic concepts of Book-Keeping to him. You are approached by Sakara to clarify for him on what Book-Keeping is all about and the importance of using Book-Keeping in his business.

#### Required:

Prepare a brief note that will guide your talk to Sakara in relation to his concerns.

## Basic accounting concepts and principles

The recording of financial transaction in the books of accounts is governed by some accounting concepts and principles. Accounting concepts and principles refer to the basic assumptions, rules, and principles which govern the recording of financial transactions in the books of accounts. This section presents seven basic accounting concepts and principles that you need to

understand at the moment. More concepts, including accrual concept, realisation concept, prudence/conservatism concept and materiality concept will be introduced in subsequent books as further learning in Book-Keeping study.

### *Business entity*

This principle requires the business to be treated as a separate legal entity from the owner(s) and other entities. This means that records of a business will only capture transactions that are conducted for the purpose of the business. This means that personal transactions of owners should not be recorded in the business books.

### *Money measurement*

This principle requires an enterprise to record only those business transactions that can be expressed in terms of money. Book-Keeping therefore, only records transactions in monetary terms.

### *Dual aspect concept*

This concept requires every financial transaction to be recorded in at least two different accounts. This concept is the basis of the double entry system of Book-Keeping, which will be further discussed in Chapter Two.

### *Going concern concept*

Going concern concept states that an enterprise prepares its books of accounts assuming that the business will continue to operate in the foreseeable future. That is to say, the business is assumed to operate forever or at least beyond the next accounting period (usually 12 months), unless conditions indicate otherwise.

### ***Accounting period principle***

While a business is expected to continue in operation for a foreseeable future, it is not possible to wait forever before evaluating the success or progress of the business. The accounting period concept requires that the life of a business is divided into uniform time intervals. At the end of each period, the financial statements are prepared to establish the business progress.

### ***Historical cost concept***

This concept requires assets to be recorded in the books of accounts and presented on the statement of financial position at their acquisition cost rather than the value at which the business can sell such assets at the present time. This is because such assets are acquired for use in the business and if the business is a going concern, the assets will be used rather than sold.

### ***Matching concept***

This principle requires an enterprise to match revenues and their related expenses in the same accounting period in the process of determining a profit or a loss.

### **The relevance of accounting concepts and principles in Book-Keeping**

The relevance of accounting concepts and principles in Book-Keeping is to improve the communication of financial information in a language that is acceptable and understandable among enterprises. The principles promote uniformity in the preparation of financial statements, making it possible for people

to compare the financial performance and position of different enterprises. The concepts are there to make financial statements and reports relevant, reliable, and understandable to users of the financial information.



#### **Exercise 1.2**

1. Define the terms debtors and creditors.
2. What is the importance of the matching concept in Book-Keeping?
3. Define the term sole proprietor.

### **The relationship between accounting concepts**

None of the accounting concepts presented above is expected to be applied in isolation. In many cases, the application of some accounting concepts will reinforce others. A few examples are given to explain such relationships.

### ***The going concern principle and the historical cost concept***

The assumption of a going concern has an effect on the values of assets and liabilities that are reported in the financial statements. When thinking about the figure to be reported for different assets in the financial statements, a business has to avoid looking at the value that each such asset can be sold at in the market at present time. This is because doing so will reflect an assumption that the assets are held for the purpose of being sold rather than for the purpose of being used in a business. Reporting assets at

market value would be appropriate when the business is expected to be closed in the near future (That is, within the next 12 months) or the business is no longer a going concern.

The historical cost concept makes this possible by prescribing that assets should be reported at their historical cost unless there are reasons to conclude that the business is no longer a going concern.

### *The going concern concept and the accounting period concept*

The going concern principle literally assumes no end in the lifespan of a business. It means that one has to wait up to the end of business to determine a profit or a loss. Because of the need to know the performance of business, the life of a business is divided into uniform accounting periods at the end of which financial statements are prepared and presented. In this way, the going concern principle is observed, but without affecting the ability of the business to measure its performance.

### *Accounting period concept and the matching principle*

As already defined, the accounting period is reflected in the act of dividing the life of a business into a uniform length of accounting periods. It is known that at the end of each period, the performance of an entity is measured by matching revenue and expenses. If there was no uniformity in the period covered by expenses and the one covered by revenues, then there would not be any meaningful profit or loss determination.



### Activity 1.4

As a Book-Keeping student you have an appointment to meet with your subject teacher and discuss with him the relationship between the accounting principles or concepts you have read in the section titled “Basic Accounting concepts and principles”. Prepare the points that you will use to discuss the relationship between the accounting concepts. In your discussion, you should give out examples that indicate how these principles are applied in our daily life.



### Revision Exercise 1

Answer the following questions:

1. Describe at least five common terms used in Book-Keeping.
2. Using three points, differentiate between Book-Keeping and Accounting.
3. Determine the importance of Book-Keeping.
4. Briefly explain each of the following accounting concepts:
  - (a) Going concern
  - (b) Dual aspect concept
  - (c) Historical cost concept
5. Write short notes on each of the following terms:
  - (a) Transaction
  - (b) Capital and
  - (c) Profit
6. Mention any five services offered by sole proprietors in your community
7. Mention and briefly explain any three accounting concepts.
8. Discuss the relevance of the accounting concepts and principles in Book-Keeping.
9. Explain the relationship between accounts and accounting concepts.

# Chapter Two ►

## Principles of double entry

### Introduction

*The use of the double entry system requires that every business transaction must be recorded twice in the books of accounts. In this chapter, you will learn the accounting equation, statement of affairs and the concept of double entry. The competencies developed in this chapter will enable you to use double entry principles accurately on posting the business transactions in the books of accounts.*

**Stock (inventory)** are goods which are held by the business for resale. For a manufacturing firm, they may be finished goods, partly finished goods or raw materials awaiting conversion or processing into finished goods which will then be sold.

### The accounting equation

The accounting equation shows resources owned by a business against those due to others (liabilities). To understand this equation, let us think of Habibu, who just started a barber shop business on 1 January 2020. To start this business, he rented a room, bought equipment (shaving machines), furniture (chairs and shelves), fittings (wall fittings and glasses), and consumables (soap, creams and towels).

He had also some cash to pay for day to day running costs such as electricity, water and repairs. The items needed to start and operate this business (equipment, furniture, fittings, consumables and cash) are called assets.

Assets are resources that an enterprise controls and uses to conduct its business. Also, they include goods kept for sale which are called **stock or inventory**. The question here would be, how did Habibu's business come to have these assets? One of the possible answers is that Habibu saved money from his previous work and decided to invest this money into his business. In this case, we refer to the amount that Habibu saved to start the business as capital. Another possibility is that Habibu borrowed money from friends, relatives, banks



and other financial institutions to start a business. In this case, we refer to the amount borrowed by Habibu as debts, commonly known as liabilities. Thus, a capital (also known as owner's equity) may be defined as the amount of resources contributed by the owner, while liability is defined as the financing from other sources to start or expand a business. In other words, liabilities are resources in the business supplied by non-owners of the business. They are obligations that a business has to settle by means of transferring economic resources to other person(s) or business (es).

Capital or owners' equity refers to the amount of money or money's worth contributed by the owner to start or expand a business.

At a point when the business has just started, the total value of assets equals the value of capital:  $\text{ASSETS} = \text{CAPITAL}$ .

When a business has resources supplied by the owner of the business and others who do not own the business, the accounting equation changes as follows:

$$\text{ASSETS} = \text{CAPITAL} + \text{LIABILITIES}.$$

The equation can also be changed or written in words as follows:

$$\begin{array}{cc} \text{Resources Owned} & = & \text{Resources Supplied} \\ \text{(Assets)} & & \text{(Capital + Liabilities)} \end{array}$$

What we have just presented is the accounting equation in its very basic form. We can assign values to each of the items and see how the equation will look like. Let us assume that the values are as presented below:

#### Habibu's assets at 1 January 2020

Item (s)	TZS
Shaving machines	480,000
Furniture	620,000
Fittings	216,000
Consumables (soap, creams and towels)	115,000
Cash	510,000

To be able to arrive at the accounting equation, you are firstly required to add up all assets. The total obtained will be TZS 1,941,000. Secondly, show the resources that were supplied to acquire the assets. The resources in this case of Habibu are capital

and liabilities. From these figures, applying our equation,  $\text{ASSETS} = \text{CAPITAL}$ , we find that Capital = TZS 1,941,000, being the sum of the assets i.e. TZS 480,000 + TZS 620,000 + TZS 216,000 + TZS 115,000 + TZS 510,000. This means Habibu supplied TZS 1,941,000 to the business and used that amount to start his business.

## Statement of affairs

### *A statement of affairs:*

*Is a statement which lists all assets and liabilities (together with their financial value) to enable one to calculate the value of capital.*

We can also show this effect on the **statement of affairs**, which lists the elements of the accounting equation in a systematic manner to show how such equation balances. The statement lists all the assets (with their values) together, and in the same manner lists all items of capital and liabilities.

This approach is specifically helpful in a situation where one knows the assets and liabilities of the business and wants to calculate the figure of capital. In this case, the figures of assets will be listed together and the total assets known. Thereafter, the figures for liabilities will be listed and the total liabilities established. The capital figure will be calculated as the difference between total assets and total liabilities and is usually presented below the liabilities' section. Habibu's statement of affairs from the above data can now be presented as follows.

### Habibu's statement of affairs as at 1 January 2020

Details	TZS
<b>Assets:</b>	
Shaving machines	480,000
Furniture	620,000
Fittings	216,000
Consumables (soap, creams, and towels)	115,000
Cash	<u>510,000</u>
<b>Total Assets</b>	<b><u>1,941,000</u></b>
<b>Capital and liabilities:</b>	
Liabilities	-
<b>Total liabilities</b>	-
Capital	<u>1,941,000</u>
<b>Total Capital and Liabilities</b>	<b><u>1,941,000</u></b>

The example shown does not provide other alternatives for getting resources in relation to Habibu's efforts in starting his barber shop business. One alternative is that Habibu had enough money for only shaving machines, consumables, and a necessary amount of cash to meet daily running costs. If Habibu had only TZS 1,105,000 and still needed furniture and fittings to start the business, he would arrange with the supplier (let's call him Mwakapande) for furniture and fittings to be supplied on credit. This would mean that the amount for furniture and fittings would be paid later. The transaction means that Habibu will now have an obligation to pay TZS 836,000 (TZS 620,000 and TZS 216,000 for furniture and fittings respectively, assuming the same costs as per the data given above). In this situation, the accounting equation will read as follows:

ASSETS = CAPITAL + LIABILITIES and in figures for Habibu's business, we will have TZS 1,941,000 = TZS 1,105,000 + TZS 836,000.

When such information is presented on the statement of affairs, the statement will look like this:

**Habibu's statement of affairs as at 1 January 2020**

Details	TZS
<b>Assets:</b>	
Shaving machines	480,000
Furniture	620,000
Fittings	216,000
Consumables (soap, creams, and towers)	115,000
Cash	<u>510,000</u>
<b>Total Assets</b>	<b><u>1,941,000</u></b>
<b>Capital and liabilities:</b>	
<b>Liabilities</b>	
Payable to Mwakapande	836,000
<b>Total Liabilities</b>	
Capital	<u>1,105,000</u>
<b>Total Capital and Liabilities</b>	<b><u>1,941,000</u></b>

Now every transaction conducted by the Habibu's business will have dual effect such that the equation maintains the relationship between assets, liabilities and capital.

Based on the previous scenario where Habibu contributed capital amounting to TZS 1,105,000 and owed Mwakapande TZS 836,000; let us see other examples and their effects on the accounting equation:

1. On 3 January 2020; Habibu buys a steriliser for the shaving machines on credit from Usafi traders at a cost of TZS 240,000.

In this example, the effect is such that there is an increase in Assets (a sterilising machine) by TZS 240,000, and an increase in liabilities (accounts payable or creditors) by TZS 240,000.

The Equation (from above will now be):

TZS 2,181,000 (That is, TZS 1,941,000 + TZS 240,000) = TZS 1,105,000 + TZS 1,076,000 (That is, TZS 836,000 + TZS 240,000).

Habibu's statement of affairs will appear as follows:

**Habibu's statement of affairs as at 3 January 2020**

Details	TZS
<b>Assets:</b>	
Shaving machines	480,000
Furniture	620,000
Fittings	216,000
sterilising machine	240,000
Consumables (soap, creams, and towels)	115,000
Cash	<u>510,000</u>
<b>Total Assets</b>	<b><u>2,181,000</u></b>
<b>Capital and liabilities:</b>	
<b>Liabilities</b>	
Payable to Mwakapande	836,000
Payable to Usafi traders	240,000
<b>Total liabilities</b>	<b>1,076,000</b>
Capital	<u>1,105,000</u>
<b>Total Capital and liabilities</b>	<b><u>2,181,000</u></b>

2. On 5 January 2020 Habibu uses TZS 15,000 of the cash to purchase air freshener for the shop. In this case, there is a decrease in asset (cash) and an increase in another asset (the stock of consumables) by the same amount that is TZS 15,000.

The equation thus remains as in the previous example, that is,  
 TZS 2,181,000 = TZS 1,105,000 + TZS 1,076,000.

Habibu's statement of affairs on 5 January will appear as follows:

**Habibu's statement of affairs as at 5 January, 2020**

Details	TZS
<b>Assets:</b>	
Shaving machines	480,000
Furniture	620,000
Fittings	216,000
Sterilising machine	240,000
Consumables (soap, creams, towels, and air freshener)	130,000
Cash	<u>495,000</u>
<b>Total</b>	<b><u>2,181,000</u></b>
<b>Capital and liabilities:</b>	
<b>Liabilities</b>	
Payable to Mwakapande	836,000
Payable to Usafi traders	240,000
<b>Total liabilities</b>	<b>1,076,000</b>
Capital	<u>1,105,000</u>
<b>Total capital and liabilities</b>	<b><u>2,181,000</u></b>

When the business gets into operation by starting to serve hair cut clients, it will start to make sales (revenue). A transaction involving shaving one person for TZS 5,000 will increase revenue by TZS 5,000 and increase Assets (cash). The increase in revenue contributes towards profit generation, and since profit belongs to the owner, it increases owner's equity or capital. This will also mean that, for the accounting equation to continue to balance, the dual effects of this transaction must be taken into account. The equation will now read as follows:

$$\text{TZS } 2,186,000 = \text{TZS } 1,110,000 + \text{TZS } 1,076,000.$$

Also, assuming the business uses one disposable towel per customer served and each cost TZS 1,000, the service to the customer above would affect the equation such that assets (stock of towels) would decrease by TZS 1,000 and the expense would increase by TZS 1,000. Like it was the case with revenue, the expense affects profits (and thus the capital or owners' equity). The difference in this case is that the increase in expense decreases capital, as opposed to the way revenue affects capital, thus:



Details	TZS
Sales	5,000
Less: Cost of towel	1,000
Balance	<b>4,000</b>

The TZS 4,000 will increase owner's capital.

Details	TZS
Current capital	1,105,000
Increase from sales	4,000
New capital	<b>1,109,000</b>

Taking into account the dual effects of this transaction, the equation will now read:  
TZS 2,185,000 = TZS 1,109,000 + TZS 1,076,000.

Assuming the client was served on 6 January 2020, the statement of affairs would read as follows:

#### Habibu's statement of affairs as at 6 January 2020

Details	TZS
<b>Assets:</b>	
Shaving machines	480,000
Furniture	620,000
Fittings	216,000
Sterilising machine	240,000
Consumables (soap, creams, towels, and air freshener)	129,000
Cash	<u>500,000</u>
<b>Total</b>	<b><u>2,185,000</u></b>
<b>Capital and liabilities:</b>	
Payable to Mwakapande	836,000
Payable to Usafi traders	240,000
<b>Total liabilities</b>	<b>1,076,000</b>
<b>Liabilities</b>	
Capital	<u>1,109,000</u>
<b>Total capital and liabilities</b>	<b><u>2,185,000</u></b>

Having noted the effects of revenue and expenses on the capital element of the accounting equation, we can have an extended accounting equation which reads as follows:

$$\text{ASSETS} = \text{CAPITAL} + (\text{REVENUE} - \text{EXPENSES}) + \text{LIABILITIES}$$

Arithmetically, this equation can be re-arranged anyhow. For ease of understanding the double entry principle, the re-arrangement of the extended accounting equation is as follows:

$$\text{ASSETS} + \text{EXPENSES} = \text{CAPITAL} + \text{REVENUE} + \text{LIABILITIES}$$



### Activity 2.1

Assume your father is running a farming business. For it to run smoothly, it requires at least ten assets. List them.



### Exercise 2.1

(a) Complete the gaps in the following table.

	Assets TZS	Liabilities TZS	Capital TZS
(a)	5,000,000	720,000	?
(b)	1,120,000	196,000	?
(c)	6,720,000	?	5,000,000
(d)	7,840,000	?	6,580,000
(e)	?	4,660,000	1,590,000
(f)	?	2,520,000	7,680,000

(b) Mr Magabe started a business with total assets worth TZS 2,500,000, liabilities TZS 500,000, and capital TZS? (You are required to calculate capital and prepare the initial statement of the affairs).

The following transactions took place during the first three days:

**Day 1**, bought office machinery and paid cash TZS 600,000.

**Day 2**, purchased goods worth TZS 300,000, on credit from Kibogoyo.

**Day 3**, sold goods worth TZS 300,000 on credit to Mr Kawawa at TZS 350,000.

#### Required:

For each of the day, prepare a statement of affairs.

## Concept of double entry

In the last section, we discussed the concept of accounting equation. The accounting equation is the foundation of the concept of double entry. Double entry deals with the posting of business transactions in the books of accounts. Business transactions are posted to ledger accounts using the principles of double entry. This section will discuss the meaning of double entry and the principles of double entry. Lastly, it will discuss the importance of double entry.

## Double entry system of Book-Keeping

Double entry system of Book-Keeping records each transaction by making two corresponding entries in the books of accounts. The reason for making two corresponding entries in the books is to simultaneously take into account the two effects of each transaction on the accounting equation. The entries are therefore made so that they cancel each other to reflect the two effects on the accounting equation. By doing this, the accounting equation would balance at any point in time. Entries are made into two sides of the respective account. An account represents a specific record of asset, liability, revenue, expense or capital to record increases and decreases following rules of debit and credit.

An increase in an asset is recorded by a debit entry in the specific asset account, whereas a decrease in an asset is recorded by an entry in the credit side of the asset's account. This rule is applied in recording increases and decreases in assets as a starting point to find out the debit and credit rules for the rest of the elements in the accounting equation. For example, liabilities are on the opposite side of assets in the accounting equation; therefore, an increase in a liability will be recorded on the credit side of the specific liability account, while a decrease in a liability is recorded by a debit entry in its account.

The same reasoning will be used for the rest of the items or elements in the accounting equation. You can quickly do this in relation to the other elements before looking at the following table that summarises the entries for decreases and increases on each of the elements of the accounting equation. Mastering these rules is very important as every transaction that you are going to record in the course of your studies in Book-Keeping and Accountancy in general will follow the same rules.

The summary of the rules for debit and credit entries for different elements of the accounting equation:

	<b>ELEMENT</b>	<b>INCREASES</b>	<b>DECREASES</b>
1.	Assets	Debit	Credit
2.	Liabilities	Credit	Debit
3.	Capital (Owner's Equity)	Credit	Debit
4.	Revenue (Gain)	Credit	Debit
5.	Expenses (Losses)	Debit	Credit

1. Establish the specific items in the elements of accounting equation that are affected by the two effects of the transaction,
2. Establish the effect that is, whether it is an increase or decrease in each case, and
3. Make respective entries for recording each effect accordingly. Making a debit entry in account is called *debiting* the account and making the credit entry in an account is called *crediting* the account.

The traditional practice in establishing the entries to be made is, first, state the account to be debited, followed by the account to be credited.

## Applying the double entry rules

Take an example of the following transactions conducted by Habibu's business:

1. Paid cash TZS 25,000 on 31 January in respect of electricity bill for the month.
2. Received TZS 20,000 from a customer for a haircut of her four children.

### Required:

Show how the transactions will be recorded in the double entry system.

### For transaction 1

The transaction involves an increase in expenses (electricity) by TZS 25,000 and a decrease in asset (cash) by TZS 25,000. A debit entry will be made in the electricity expense account to record the TZS 25,000 increase in expense, and a credit entry will be made in the cash account to record the TZS 25,000 decrease in the asset.

The entries can be summarized as follows:

*Debit:* Electricity expense    TZS 25,000

*Credit:* Cash

TZS 25,000

The transaction involves an increase in asset (cash) by TZS 20,000 and an increase in revenue by TZS 20,000. A debit entry will be made in the cash account to record the TZS 20,000 increase in asset, and a credit entry will be made in the service revenue account to record the TZS 20,000 increase in revenue.

The entries can be summarized as follows:

*Debit:* Cash                      TZS 20,000

*Credit:* Service revenue

TZS 20,000

## Double entry principle

Looking at the way double entries are made in the above explanations and examples, it is now simple to understand the principle of double entry which states that “For every **debit entry** there must be a **corresponding credit entry of the same amount**, and vice versa”.

A debit entry is an entry on the debit side of an account, and a credit entry is an entry on the credit side of an account. A corresponding entry refers to an entry to the same transaction (and thus involves the same amount) for which a debit entry has been made, which however, will be made on the opposite side (credit side) of the other account affected by the same transaction.

The application of this can be established from the two transactions above:

1. *In transaction 1:* the corresponding entry for the debit of TZS 25,000 made in electricity expense account is the credit entry made in the cash account.
2. *In transaction 2:* the corresponding entry for the debit of TZS 20,000 made in cash account is the credit entry made in service revenue account.

**Alternatively**, the concept of double entry can further be understood by considering the following golden rules:

## Golden rules of double entry system

**Personal accounts** are used to record financial transactions that represent persons or a group such as debtors and creditors. Therefore, some of the accounts will be named after names of individuals like Jamal Account and Hellen Account.

**Real accounts** are used to record financial transactions representing the material assets of the business. Examples on this include Motor vehicle account, Furniture account and Machinery account.

**Nominal accounts** are used to record financial transactions representing revenues, expenses and gains or losses incurred by the business in its business operations. Examples on this includes Sales account, Purchases account, Salary account, Rent income account and Rent expense account.

There are golden rules that must be followed when posting a transaction in the ledger account. In summary, the golden rules that must be adhered to when recording transactions in personal accounts, real accounts, and nominal accounts are as follows.

### (i) *For personal accounts: debit the receiver, credit the giver*

“Debit the receiver, credit the giver”. This rule simply implies that the person who receives something in the transaction, his account should be debited, and the person who gives something in the transaction, his account should be credited.



**(ii) For real accounts: Debit what comes in, and credit what goes out**

“Debit what comes in, and credit what goes out”. This rule simply implies that whenever the asset (tangible or intangible) comes in – in the enterprise, the ledger account of that asset must be debited, and whenever the asset goes out – out of the business enterprise, the ledger account of that asset must be credited.

**(iii) For nominal accounts: Debit accounts for expenses and losses and credit accounts for incomes and gains**

“Debit all expenses and losses and credit all incomes and gains”. The implication of this rule is to debit the account of expenses and losses and to credit the accounts of revenues and gains.

**Steps to be followed when identifying and posting transactions in the ledger accounts:**

**Step 1:** In each transaction, a student must be able to identify two accounts involved in the transaction.

**Step 2:** Find out the type of account involved (Personal, real or nominal).

**Step 3:** Debit and credit appropriate ledger accounts by applying the rules of double entry.

**Step 4:** Indicate the effect of transactions, that is, an increase or decrease of an account.

**A worked out example 2.2**

For each of the transactions below, identify two accounts involved, their types, and state which account should be debited and which one should be credited.

- 2020 January
- 1 Diana started a business by depositing TZS 2,000,000 in the bank account.
  - 4 Purchased machinery worth TZS 200,000 on credit from Alpha.
  - 8 Purchased goods worth TZS 400,000 on credit from Julius.
  - 12 Sold goods for cash TZS 150,000.
  - 16 Withdrew TZS 200,000 from the bank account for business use.
  - 20 Sold goods on credit to Tandahimba LTD TZS 50,000.
  - 22 Returned goods worth TZS 15,000 to Julius because they were of the wrong type.
  - 24 Paid wages by cash TZS 30,000.
  - 26 Withdrew TZS 100,000 from the bank account for personal use.
  - 27 Purchased goods from Frida worth TZS 150,000 promising to pay for them later.

- 28 Tandahimba LTD returned goods worth TZS 5,000 because they had expired.
- 29 Received rent in terms of cash TZS 50,000.

**Solution**

Date	Accounts involved	Type of account	Debit/Credit
2020	Bank account	Real account	Debit (incomings)
January 1	Capital account	Personal account	Credit (Giver)
4	Machinery account	Real account	Debit (Incomings)
	Alpha account	Personal account	Credit (giver)
8	Purchases account	Nominal account	Debit (Expenses)
	Julius account	Personal account	Credit (giver)
12	Cash account	Real account	Debit (incomings)
	Sales account	Nominal account	Credit (Income)
16	Cash account	Real account	Debit (incomings)
	Bank account	Real account	Credit (outgoings)
20	Tandahimba LTD account	Personal account	Debit (Receiver)
	Sales account	Nominal account	Credit (income)
22	Julius account	Personal account	Debit (receiver)
	Purchases returns account	Nominal account	Debit (contra expense)
24	Wages account	Nominal account	Debit (Expenses)
	Cash account	Real account	Credit (Outgoings)
26	Drawings account	Personal account	Debit (Receiver)
	Bank account	Real account	Credit (outgoings)
27	Purchases account	Nominal account	Debit (Expenses)
	Frida account	Personal account	Credit (Giver)
28	Sales returns account	Nominal account	Debit (contra income)
	Tandahimba LTD account	Personal account	Credit (giver)
29	Cash account	Real account	Debit (Incomings)
	Rent received account	Nominal account	Credit (income)

**Note:** Types of accounts would be discussed in detail in the “*Classification of accounts*”, a section in Chapter Four.

**A worked out example 2.3**

Using tabular form, indicate the account to be debited or credited and show the effect on assets, liabilities and capital from the following transactions:

- (i) Amount received from debtor by cheque
- (ii) Purchases of a motor van on credit
- (iii) Sales of furniture for cash
- (iv) Goods sold for cash
- (v) A proprietor invested amount of cash in business
- (vi) Goods taken from the business for personal use

**Solution**

No	Transaction	Account debited and credited	Effect
(i)	Amount received from debtor by cheque	Dr. Bank account	Increase in asset
		Cr. Accounts receivable account	Decrease in asset
(ii)	Purchased a motor van on credit	Dr. Motor van account	Increase in asset
		Cr. Accounts payable account	Increase in liability
(iii)	Sales of furniture for cash	Dr. Cash account	Increase in asset
		Cr. Furniture account	Decrease in asset
(iv)	Goods sold for cash	Dr. Cash account	Increase in asset
		Cr. Sales account	Decrease in asset
(v)	A proprietor invested amount of cash in business	Dr. Cash account	Increase in asset
		Cr. Capital account	Increase in capital
(vi)	Goods taken from the business for personal use	Dr. Drawings account	Decrease in capital
		Cr. Purchases account	Decrease in asset

**Activity 2.2**

In a group, discuss the meaning of personal accounts, real accounts and nominal accounts. Present your answer to your colleagues in class.



## Exercise 2.2

Complete the following table.

Transactions	Account to be debited	Account to be credited
(a) Sold goods on credit to Peter.		
(b) Paid cash to Emma for goods purchased on credit.		
(c) A creditor, Moze was paid by cheque.		
(d) The business owner invested additional cash into business.		
(e) Peter returned goods to us.		

### Importance of double entry

The use of the double entry system is important in accounting process due to the following reasons:

#### *It makes it easier to show the two effects of each transaction*

As already discussed, the double entry system of Book-Keeping requires every transaction to be recorded twice. That is, every debit entry should have its corresponding credit entry. For this reason, the double entry system of Book-Keeping makes it easier for anyone analyzing the business transaction to understand which of the two items or accounts have been affected by the transaction.

#### *It assures arithmetic accuracy in the accounts thus minimises the possibility of errors*

Since the double entry system of Book-Keeping requires every debit to have a corresponding credit entry, the arithmetic accuracy of the books of accounts is assured. The arithmetic accuracy in the accounts is further assured by the preparation of the trial balance periodically or at the end of the accounting period.

#### *It is the basis of the balances used to prepare the financial statements*

Balances used in the preparation of the trial balance and eventually in the financial statements are extracted from ledger accounts. It should be noted that the posting of entries in the ledger accounts follows the double entry system of Book-Keeping. In this regard, double entry system ensures the preparation of the trial balance and financial statements.

***It ensures that financial records are kept properly***

Double entry ensures that financial records are kept permanently and properly in the books of accounts. This is because entries in the ledger accounts are posted using the double entry system of Book-Keeping.

**Activity 2.3**

Your friend, Zawadi has approached you to clarify an important aspect in Book-Keeping. She has heard you speaking about double entry and she believes that the use of double entry will:

1. Double the work of the bookkeeper and thus spend more resources of the enterprise;
2. Encourage recording transactions twice which is misleading as it doubles the amounts reported; thus some kind of cheating may occur.

You are required to explain to her the double entry system and show its benefit to an enterprise.

**Revision Exercise 2**

1. Complete the gaps in the following table.

	Assets TZS	Liabilities TZS	Capital TZS
(a)	1,650,000	507,000	?
(b)	?	516,000	1,032,000
(c)	1,083,000	?	855,000
(d)	3,585,000	462,000	?
(e)	2,640,000	?	2,480,000
(f)	?	1,960,000	4,400,000

2. Complete the columns to show the effects of the following transactions by inserting a (+) sign for the increase and a (-) sign for the decrease. Transaction (a) is given as an example.

	Effect upon		
	Assets	Liabilities	Capital
(a) Started business depositing TZS 3,500,000 cash in a bank account.	Bank (+)		Capital (+)
(b) Purchased a business building from D. Kamara for TZS 750,000, paying TZS 500,000 by cheque and promising to pay the balance as early as possible in the following month.			
(c) Purchased office furniture by cheque from Kipara worth TZS 250,000.			
(d) The owner injected TZS 600,000 through cheque in the business.			
(e) Sold goods to Mahinda on credit worth TZS 120,000.			
(f) Paid wages by cash amounting to TZS 50,000.			
(g) Received TZS 50,000 in cash as rent.			

3. From the items listed below, identify which ones are assets and which ones are liabilities by inserting a tick sign (✓).

	Assets	Liabilities
(a) Motor vehicles		
(b) Loan to Dainess		
(c) Bank overdraft		
(d) Creditors		
(e) Fixtures and fittings		
(f) Computers		
(g) Loan from Jamal		
(h) We owe Sauda		
(i) Khamis owes us		



4. Classify the following items into liabilities and assets:
- Premises,
  - Buildings,
  - Inventory,
  - Accounts receivable,
  - Accounts payable,
  - Machinery,
  - Cash in hand, and
  - A bank loan.
5. Complete the following table by showing the effects, the account to be debited, and the account to be credited.

S/N	Nature of transaction	Effects	Account to be debited	Account to be credited
<b>Example</b>	Bought office machinery on credit from SIDO.	Increase machinery Increase in accounts payable (SIDO)	Machinery account	SIDO account
(a)	The proprietor paid a creditor, G. Mjema, from his private funds.			
(b)	A debtor, N. Omogu, paid us in cash.			
(c)	Repaid part of a loan from P. Komba by cheque.			
(d)	Returned some of the office machinery to SIDO.			
(e)	A debtor, N. Kakonko, pays us by cheque.			
(f)	Bought a van by cash.			
(g)	Machinery sold by cash.			
(h)	Goods returned by us to Sekimweri.			

6. Complete the following table by showing the account to be debited and the account to be credited.

S/N	Nature of transaction	Account to be debited	Account to be credited
(a)	Bought a lorry for cash.		
(b)	Paid a creditor, T. Wanjara, by cheque.		
(c)	Repaid P. Mkombozi's loan by cash.		
(d)	Sold a lorry for cash.		
(e)	Bought a solar equipment on credit from Light Swebe LTD.		
(f)	A debtor, A. Msasu, pays us by cash.		
(g)	A proprietor puts a further amount into the business by cheque.		
(h)	A loan in cash is received from L. Washee.		
(i)	Paid rent by cash.		
(j)	Paid salary by cheque.		

# Chapter Three ►

## Books of prime entry

### Introduction

*Recording of transactions in the books of accounts is the initial and very critical stage in accounting. Correctness of the first record (prime, original entry or subsidiary books) in the books of accounts for a transaction is an important basis for having appropriate accounting records. There are six types of books of prime entry. In this chapter you will learn only five types of books of prime entry and the sixth book which is the cash book will be learnt in form two. Also, you will learn the use of books of prime entry, source documents and preparation of books of prime entry. The competencies developed in this chapter will enable you to classify and prepare books of prime entry according to the required principles.*

#### **Books of prime entry:**

*are also known as books of original entry or subsidiary books. These names can be used interchangeably.*

#### **Types of books of prime entry**

Books of prime entry are also known as journals or daybooks except for a cash book. These books are commonly termed as daybooks because they are used to record transactions on the daily basis. There are six types of books of prime entry as presented below: -

- (a) Purchases journal (or Purchases daybook),
- (b) Sales journal (or Sales daybook),

- (c) Sales returns journal (or Sales returns daybook),
- (d) Purchase returns journal (or Purchase returns daybook),
- (e) Cash book, and
- (f) General journal (journal proper).

#### **The meaning of books of prime entry**

Books of prime entry (journals) are the books of accounts that are used to record the transaction in books of accounts for the first time. In the books of prime entry, the transaction is recorded with as much detail as possible, in order to provide enough information concerning the transaction. In fact, the name journal

is adopted from a French word for diary. It is therefore, a good practice to record transactions in the books of prime entry in a chronological order. Transactions are also recorded as soon as possible from the time when they occur in order to avoid situations where they may be forgotten, or have their source documents misplaced.

For example, suppose Eliza sold three office chairs to Abraham for TZS 100,000 per office chair on credit. In this case, Eliza is expected to record that she sold three office chairs for TZS 100,000 each to Abraham on credit. Eliza is also expected to record the address and contact information of Abraham and the date of the transaction. She would also record the details of the invoice issued to Abraham.

### **The use of books of prime entry**

As already explained, there are six types of books of prime entry. As their names suggest, each book serves its own purpose. The following are brief descriptions and purpose of each of the book of prime entry:

#### **Purchases daybook (or purchases journal)**

The purchases daybook is used to record transactions related to credit purchases of goods. In other words, this journal is used to record details of goods bought by the business with the promise that payment will be made in the future. The cash purchases of goods are not recorded in this book.

#### **Sales daybook (or sales journal)**

The sales daybook is used to record transactions related to credit sales of

goods. In other words, this journal is used to record details of goods sold on credit with the promise that payment will be received in the future. The cash sales of goods are not recorded in this book.

#### **Sales returns daybook (or sales returns journal)**

This daybook is used to record details of transactions related to sales returns, or returns of goods from customers to whom goods were sold on credit (debtors). The entries made include details of the goods and the credit note, the names of customers (debtors) and the amounts involved.

#### **Purchase returns daybook (or purchase returns journal)**

The purchase returns daybook is used to record transactions related to purchase returns, or return of goods to suppliers who supplied goods on credit (creditors). The entries made include details of the goods and the credit note, the names of suppliers (creditors) and the amounts involved as well as the reason of returning the goods.

#### **Cash book**

The cash book is used to record transactions related to receipt and payment of cash as well as money placed into the bank (bank deposits) and those taken from the bank (bank withdrawals).

#### **General journal (Journal proper)**

This book of prime entry is used to record transactions related to other items, which according to their nature are not recorded in any of the above books of prime entry.

It is important to note that businesses that do not have credit sales and purchases, or do not allow returns of goods may have all transactions recorded in the general journal.

### Source documents

Since these books are of original entry, the information recorded in them is taken straight from the documents that may either have been issued by the business or by its suppliers. These documents are called source documents, since they are the source of information for recording in the books. The information from these documents is entered straight to the books of prime entry. The following are examples of common source documents used in the preparation of books of prime entry:

### Cash receipt voucher

It is a document that acts as proof that cash has been received. Money could be received from customer for cash sale of goods or services. Alternatively, cash may be received when a credit customer settles his or her accounts receivable. Usually, the cash receipt contains information regarding the date of receipt, name or details of the customer, description of the item sold, quantities and the price of the product. It also bears a signature or a stamp of the receiver of the money, and the amount received. If the money received was for settlement of accounts receivable, the receipt may also include the invoice number that identifies the sales invoice of the transaction. Figure 3.1, shows a sample of cash receipt voucher.

<b>Cash Receipt Voucher</b>				
<b>Company name and address</b>				
<b>Voucher Number:</b> .....			<b>Date:</b> .....	
S/N	DESCRIPTION	UNIT PRICE	QUANTITY	AMOUNT (TZS)
<b>TOTAL</b>				
<b>Amounts in words:</b> .....				
<b>Cash/ Cheque Number</b> .....				
<b>Received by:</b> .....		<b>Signature:</b> .....		<b>Date:</b> .....

**Figure 3.1:** A sample of a cash receipt voucher

### Payment voucher

It is a document that presents evidence that money has been paid. Money might be paid to the supplier for cash purchase of goods or services, or for settlement of accounts payable for goods previously bought on credit. The cash payment voucher may contain information regarding the date of payment, name or details of the payee, description of the item bought, quantities and the price of the product. It also bears a signature or a stamp of the approving authority, and the amount actually paid. If the money paid was for settlement of accounts payable, the payment voucher may also include the invoice number that identifies the purchase invoice of the transaction for which the payment is made. Figure 3.2, presents a sample of a payment voucher.

<b>Payment Voucher</b>		
<b>Company name and address</b>		
PV No: .....		
<b>Amount:</b>	<b>Date:</b>	
<b>Method of Payment</b>		
<b>Cash:</b>	<b>Cheque:</b>	
<b>To:</b>		
<b>The Sum of:</b>		
<b>Being:</b>		<b>Payee:</b>
<b>Approved By:</b>	<b>Paid By:</b>	<b>Signature:</b>

**Figure 3.2:** *A sample of a payment voucher*

### An invoice

It is a document prepared by the seller and sent to the buyer when goods are sold or services are rendered on credit. The invoice is usually prepared in duplicate. The seller retains the duplicate copy while the original copy is sent to the buyer. In simple terms, the invoice is the request for payment sent by the seller to the buyer regarding goods sold or services rendered on credit. There are two types of invoices, namely purchases and sales invoice. A purchases invoice is used as a source document when you prepare a purchases daybook while a sales invoice is used as a source document when you prepare a sales daybook. Figure 3.3 shows a sample of an invoice.



Company Name			
Address		Date	.....
Phone No 1	+255-000-000-000	Invoice No	.....
Phone No 2	+255-000-000-000	Due Date	.....
Fax	+255-000-000-000		
Email	sales@enterprise.com		
Website	www.enterprise.com		

Bill To:	
Name	
Address	
Tin No	
Phone No	

S/N	DESCRIPTION	UNIT PRICE	QUANTITY	AMOUNT (TZS)
Subtotal				
Taxable				
Tax rate (18%)				
Tax due				
TOTAL				

Figure 3.3: A sample of an invoice

**Credit note**

It is a document sent by the seller to the buyer to correct an overcharge on an invoice. For example, if some of the goods supplied to the buyer on credit are returned to the supplier for various reasons such as seller delivering wrong or damaged goods, then a credit note will be issued by the seller to indicate that the buyer's account has been credited. Figure 3.4, shows the sample of credit note used to return goods to the supplier.

### Credit Note

Date: .....

Supplier's  
contact

Credit note number: .....  
TIN number: .....

Company name  
and contact

S/N	Description	Quantity	Unit of measure	Price per unit	Amount in (TZS)
<b>TOTAL</b>					

Figure 3.4: A sample of a credit note

**Debit note**

It is a document prepared and sent by the seller to the buyer to adjust for an undercharge on the invoice because of various reasons. For example, if the buyer has failed to return some of the containers or packing materials that were not charged for in the invoice, the seller has to send a debit note to claim the undercharged amount. Figure 3.5, shows a sample of a debit note.

### Debit Note

Debit Note No. \_\_\_\_\_

Invoice No. \_\_\_\_\_

Debtor's name and address \_\_\_\_\_

Company name and  
address

S/N	Description	Quantity	Unit of measure	Price per unit	Amount in (TZS)
<b>TOTAL</b>					

Date: \_\_\_\_\_

\_\_\_\_\_ (Signature)

Figure 3.5: A sample of a debit note

## Statement of account

This is the document prepared and sent by the seller to the buyer at the end of every period (usually each month) acting as a reminder to the buyer to pay the outstanding balance. The statement of account contains information concerning the details on the invoices that were sent to the customer, the amount paid by the customer, and the outstanding balance. Figure 3.6, shows a sample of a statement of account.

Company name and address

**Statement of accounts**  


---

**From** Date/Month/Year **To** Date/Month/Year  


---

**Accounting Summary**

Opening balance	TZS
Invoiced amount	TZS
Amount paid	TZS
Balance due	TZS

**To:** Company name  
 Address

Date	Transaction	Details	Amount	Payment	Balance

**Figure 3.6:** *A sample of a statement of account*

## Petty cash voucher

A petty cash voucher is a document used by a petty cashier as an evidence for making small payments from petty cash fund. Most of the petty cash vouchers contain important information like date, amount payable, person to whom money is being paid to, reasons for the payment and initials of the petty cashier making the payment. Figure 3.7, shows a sample of a petty cash voucher.

## Petty Cash Voucher

### Company name and address

Date:

Voucher Number:

Description	Amount (TZS)
<b>Total</b>	

The sum of Tanzania Shillings:.....

Approved By: \_\_\_\_\_ Cash Received By: \_\_\_\_\_

**Figure 3.7:** *A sample of a petty cash voucher*

### Cheque

A cheque may be defined as a written instruction by the account holder (drawer) to their bank (drawee) to pay a specific amount of money from the drawer's account to the person written on the cheque (payee). A cheque is also used by the drawer to withdraw cash from their account. In technical (legal) terms, a cheque is an unconditional order in writing made by the account holder to the account holder's bank to pay on demand a stated amount of money to the named person or bearer. Cheques have gained popularity in the business world because of being safe, secure and convenient compared to cash payments. Figure 3.8, shows a sample of a cheque.

**KILIMO BANK** MAFIGA BRANCH

Stamp: **STAMP DUTY PAID**

Date: 25 - 09 - 2021  
DAY MONTH YEAR

PAY Msimbe David Or Order

**\*\*Twelve Million Three Hundred And Forty Five**  
SHILLINGS

**Thousand Six Hundred And Seventy Eight Only\*\***

**TZS \*\*12,345,678.00\*\***

Authorized Signatory

**Figure 3.8:** *A sample of a cheque*

### Journal voucher

A journal voucher is a source document used to provide evidence of authorisation for all transactions other than those which are evidenced by the previously mentioned source documents. These transactions include accounting adjustments, provisions and accruals, purchases and sales of fixed assets, and opening entries. Entries from the journal voucher are transferred directly to the general journal. Figure 3.9, shows a sample of a journal voucher.

<b>Journal Voucher</b>				
<b>Company name and address</b>				
<b>Date:.....</b>				
S/N	Account Name	Description	Debit	Credit
<b>Total</b>				
<b>Remark: .....</b>				
<b>Attached Document:.....</b>				
<b>Prepared by.....Posted by..... Authorized by.....</b>				

**Figure 3.9:** A sample of a journal voucher



#### Activity 3.1

Assume that your school runs a small shop selling stationeries to students and the neighbouring community. Sit in groups and with the help of your subject teacher or use internet to prepare a sample (specimen) of the following documents and clearly explain the importance of every detail appearing in each document: -

- (i) Credit note,
- (ii) Debit note,
- (iii) Statement of account,
- (iv) Receipt voucher,
- (v) Payment voucher,
- (vi) Invoice,
- (vii) Cheque, and
- (viii) Journal voucher.

## Preparation of books of prime entry

As per the accounting cycle or process introduced in Chapter One; once transactions are identified, they are entered in the books of prime entry, followed by posting the entries to various ledger accounts. A ledger is the main book of accounts in which different types of transactions are recorded. The posting is done following the double entry system which was introduced in Chapter Two. In this section, you are going to learn the four special journals and how information from source documents is entered in them, followed by the general journal.

### Purchases daybook or purchases journal

When goods are purchased on credit, the seller will prepare and send an invoice to the buyer. The buyer will record this transaction in the purchases daybook because the transaction involves credit purchases, meaning that the buyer did not pay for the goods at the time of purchase. Therefore, the purchases daybook is used to record transactions relating to credit purchases of goods. Practically, entries made in the purchases journal are summed up periodically (e.g. monthly).

### Format of the purchases daybook

The purchases daybook has six columns which are:

#### (i) Date

This column is used to write the date, the month, and the year of the transaction. Specifically, it shows when the transaction took place.

#### (ii) Particulars

This column gives a short description of the entry for the transaction recorded. It actually records the name of the supplier and the details of the items purchased.

#### (iii) Folio

This column records pages of reference in books of accounts. It indicates in what ledger and on what page the transaction has been posted.

#### (iv) Invoice number

This column records the details of the invoice number which identifies the invoice issued when a particular transaction was made. This is helpful in case of a need for verification or investigating errors in the records, since it makes it possible to retrieve the invoices (which are normally filed in a systematic manner) and match with the figures recorded in the books.



**(v) Invoice details**

This column records the details of the invoice involved in the transaction and it is especially useful where an invoice includes more than one type of goods.

**(vi) Invoice total**

This column records the total amount of money being transacted.

These columns are illustrated as follows:

**Purchases daybook**

<b>Date</b>	<b>Particulars</b>	<b>Folio</b>	<b>Invoice Number</b>	<b>Invoice Detail (TZS)</b>	<b>Invoice Total (TZS)</b>

**A worked out example 3.1**

Record the following transactions in the purchases daybook for the month of July 2020.

- 2020 July 1 Bought from Tom LTD, invoice number 043516:  
     10 bags of rice, each with 5kgs, @ TZS 10,000.  
     20 bags of sugar, each with 5kgs, @ TZS. 15,000.
- 9 Bought from Asha invoice number 03167:  
     10 boxes of pens @ TZS 2,000.  
     5 cartons of ruled papers @ TZS 30,000.
- 16 Bought goods from Katabo for TZS 60,800, invoice number 06312:
- 29 Bought from Mwanaidi, invoice number 09842:  
     15 pairs of sandals @ TZS 15,000.  
     14 boxes Kids drawing pens @ TZS 5,000.

**Solution****Purchases Daybook**

Date	Particulars	Folio	Invoice Number	Invoice Details (TZS)	Invoice Totals (TZS)
2020 July 1	Tom LTD: 10 bags of rice (5kgs), @ TZS 10,000  20 bags of sugar (5kgs), @ TZS 15,000	PL <sub>1</sub>	043516	100,000  300,000	400,000
9	Asha: 10 boxes of pens @ TZS 2,000  5 cartons of ruled paper @ TZS 30,000	PL <sub>2</sub>	03167	20,000  150,000	170,000
16	Katabo: Goods	PL <sub>3</sub>	06312		60,800
29	Mwanaidi: 15 pairs of sandals @ TZS 15,000  14 boxes of kids drawing pens @ TZS 5,000	PL <sub>4</sub>	09842	225,000  70,000	295,000
31	Total transferred to Purchases account (Dr)	GL			<b>925,800</b>

**Sales daybook or sales journals**

When the supplier sells goods on credit, he prepares and sends an invoice to the buyer. The invoice is usually prepared in duplicate and the seller remains with a copy after issuing the original invoice to the buyer. The retained copy serves as a source document that helps the seller to prepare the Sales daybook. Therefore, the sales daybook is used to record transactions related to credit sales of goods.

The columns for the sales daybook are the same as those used for purchases daybook, except that the business is now dealing with its customers rather than its suppliers.

You will actually notice that the invoices used in worked out example 3.1 do not have a defined sequence in invoice numbers. This is because they come from different suppliers. In the case of sales journal, the invoice numbers will be following a clear sequence (see example 3.2), because the entity preparing the sales journal and issuing the invoice is the same.

**A worked out example 3.2**

Kassimu made the following sales during June 2020. You are required to record the transactions in the sales journal for the month.

- 2020 June 1 Sold to Mambo LTD, invoice number 04318:  
80 packets of rice @ TZS 2,200.  
60 bags of wheat flour, each with 3kgs, @ TZS 4,500.
- 12 Sold to Kifundo Enterprise, invoice number 04319:  
15 boxes of toothpastes @ TZS 2,600.  
16 pieces of writing pads @ TZS 2,350.
- 19 Sold to Rudia stores, invoice number 04320:  
11 pairs of running shoes @TZS 6,000.  
20 shirts @ TZS 1,200.
- 25 Sold goods to Kalumanzira worth TZS 82,000 on credit and issued invoice number 04321.
- 28 Sold to Glory, invoice number 04322:  
15 pairs of sandals @ TZS 8,500.  
10 bags of rice, each with 3kgs, @ TZS 6,000.

## Solution

## Sales daybook

Date	Particulars	Folio	Invoice Number	Invoice Details (TZS)	Invoice Totals (TZS)
2020 June					
1	Mambo LTD: 80 packets of rice @ TZS 2,200 60 bags of wheat flour (3kgs) @ TZS 4,500	SL <sub>1</sub>	04318	176,000 270,000	446,000
12	Kifundo Enterprises: 15 boxes of toothpaste @ TZS 2,600 16 pieces of writing pads @ TZS 2,350	SL <sub>2</sub>	04319	39,000 37,600	76,600
19	Rudia: 11 pairs of running shoes @ TZS 6,000 20 shirts @ 1,200	SL <sub>3</sub>	04320	66,000 24,000	90,000
25	Kalumanzira: Goods	SL <sub>4</sub>	04321		82,000
28	Glory: 15 pairs of sandals @ TZS 8,500 10 bags of rice(3kgs) @ TZS 6,000	SL <sub>5</sub>	04322	127,500 60,000	187,500
30	Total transferred to sales account (Cr)	GL			882,100



## Activity 3.2

Purchases and sales daybooks are among the books of prime entry. A number of details about different sales and purchases transactions are made in these books. You have visited a retailer and advised that due to the nature of her transactions

she has to record them in the special journals, including the sales daybook and purchases daybook.

She agreed with you and even offers to give you a small fee for designing the daybooks. However, she said that, all what she wants is to keep records in the daybooks that contain limited information like the names, amounts and addresses of customers and suppliers. She does not want too many details because the details can consume more time and papers.

You are required to advise her on the details needed and the importance of such details.

### **Sales returns daybook or sales returns journal**

There is time when goods sold to the customer are returned to the seller. Goods might be returned by the customer due to several reasons including late delivery, low quality goods, different types or specifications (colour, size, etc.), damaged goods, expired goods, or excessive quantity (oversupplied).

When a customer returns goods to a supplier, the supplier prepares and issues a credit note as the acknowledgment for the receipt of goods returned. The purpose of the credit note is to inform the customer that his account has been credited to reduce the amount debited at the time of sale. In this case, a credit note serves as a source document and it is used in the preparation of the sales returns daybook. The sales return journal has the following columns:

#### **(i) Date**

This column is used to write the date, month, and year of the transaction. Specifically, it shows when the transaction took place.

#### **(ii) Particulars**

This column indicates a short description of the entry for the transaction recorded. It actually records the name of the customer, item and reason for returning the goods.

#### **(iii) Folio**

This column records pages of reference in books of accounts. It indicates in what ledger and on what page the transaction has been recorded.

#### **(iv) Credit note number**

This column records the details of the credit note number which identifies the credit note issued when the return took place. This is helpful in case of a need for verification

or investigating errors in the records, since it makes possible to retrieve the credit notes (which are normally filed) and match with the figures recorded in the books.

#### (v) Credit note details

This column records the details of the credit note involved in the return and is especially useful where a credit note includes more than one type of goods returned.

#### (vi) Credit note total

This column records the amount of money being transacted, that is, the price of the goods returned.

These columns are illustrated as follows:

**Sales returns daybook**

Date	Particulars	Folio	Credit Note Number	Credit Note Details (TZS)	Credit Note Total (TZS)

#### A worked out example 3.3

Kassimu sells goods on credit to various customers who normally return goods for various reasons. The following returns were received for the month of June 2020 and credit notes were issued accordingly:

June	2	Mambo LTD returned 10 packets of rice @ TZS 2,200 because they were spoiled. Credit note number 01280 was issued.
	8	Rudia returned the following goods and a credit note number 01281 was issued:
		3 pairs of running shoes @ TZS 6,000 because they were oversize.
		2 shirts @ TZS 1,200 because they were of the wrong colour.
	18	Kifundo Enterprises returned the following goods and credit note number 01282 was issued:
		3 boxes of toothpaste @ TZS 2,600 because they were of the wrong type.
		2 pieces of writing pads @ TZS 2,350 because they were damaged.

You are required to prepare a sales returns daybook.



## Solution

## Sales returns daybook

Date	Particulars	Folio	Credit Note Number	Credit Note Details (TZS)	Credit Note Totals (TZS)
June 2	Mambo LTD: 10 packets of rice @ TZS 2,200 <i>Spoiled</i>	SL <sub>1</sub>	01280		22,000
8	Rudia: 3 pairs of running shoes @ TZS 6,000 <i>Oversize</i> 2 shirts @ TZS 1,200 <i>Wrong colour</i>	SL <sub>2</sub>	01281	18,000  2,400	20,400
18	Kifundo Enterprises: 3 boxes of tooth paste @ TZS 2,600 <i>Wrong type</i> 2 pieces of writing pads @ TZS 2,350 <i>Damaged</i>	SL <sub>3</sub>	01282	7,800  4,700	12,500
30	Total transferred to sales returns account (Dr)	GL			54,900



## Exercise 3.1

1. Describe how a sales invoice may also be considered as a purchases invoice.
2. Mention any three reasons why a buyer may return goods to a supplier.

### Purchases returns daybook or purchases returns journal

When a business person buys goods from a supplier, some cases may occur where the buyer needs to return the goods to the seller. This could happen due to reasons that may be similar to the ones mentioned in the previous discussion on sales returns. When the buyer returns the goods to the supplier, the supplier prepares a credit note to inform the buyer that he has credited his account. The credit note indicates that the claim or debt against the buyer's account has been reduced since the adjustment on the overcharged amount on the invoice has been rectified. Full explanations or reasons for returning the goods must be well stated on the credit note.

Sometimes, a business person can return goods to the supplier along with a debit note as an indication that the supplier's account has been duly debited. However, it should be noted that the use of a debit note for this purpose is not common these days. Actual confirmation of the return is best achieved when the seller accepts the returned goods and issues a credit note. The best practice is therefore to use a credit note as an evidence for returns of goods and a source document for entering the returns in the journal. Transactions relating to the returns of goods are recorded in the purchase returns daybook.

The columns for the purchase return daybook are the same as columns for the sales return daybook.

#### A worked out example 3.4

Record the following transactions in the purchases returns daybook for the month of July 2020.

- |      |   |   |
|------|---|---|
| July | 8 | Returned to Tom LTD and received credit note number 06569:<br>2 bags of rice (5kgs), @ TZS 10,000 because they had expired.<br>4 bags of sugar (5kgs), @ TZS 15,000 because they had expired.             |
| 18   |   | Returned to Asha and received credit note number 03447:<br>4 boxes of pens @ TZS 2,000 because they were of the wrong specification.<br>1 carton of ruled papers @ TZS 30,000 because it was not ordered. |
| 29   |   | Returned to Katabo and received credit note number 02940:<br>Goods worth TZS 14,800 were spoiled.   |

## Solution

## Purchase returns daybook

Date	Particulars	Folio	Credit Note Number	Credit Note Details (TZS)	Credit Note Totals (TZS)
July 8	Tom LTD: 2 bags of rice (5kgs), @ TZS 10,000 4 bags of sugar (5kgs), @ TZS 15,000	PL <sub>1</sub>	06569	20,000 60,000	80,000
18	<i>Expired</i> Asha: 4 boxes of pens @ TZS 2,000 <i>Wrong specification</i> 1 carton of ruled paper @ TZS 30,000	PL <sub>2</sub>	03447	8,000 30,000	38,000
29	<i>Not ordered</i> Katabo: <i>Goods spoiled</i>	PL <sub>3</sub>	02940		14,800
31	Total transferred to purchases returns account (Cr)	GL			132,800



## Activity 3.3

One of the arguments that emerged in your 'after class' discussion on Monday this week was why the source documents for entries in the purchase return daybook and sales return daybook are not the debit note and credit note respectively. You volunteered to ask this question to your Book-Keeping teacher and instead of giving you an answer, he instructed you to read and clarify this matter to your fellow students before the next class, which takes place on Thursday afternoon.

Write brief notes clarifying the matter to your class.

## **General journal**

The general journal is a book of prime entry used to record business transactions that are not recorded in special journals. The other name of the general journal is the journal proper, and these names can be used interchangeably. Examples of entries recorded in the general journal are entries for:

- (a) Purchases or disposal of business assets,
- (b) Correction of Book-Keeping errors,
- (c) Adjustments of balances prior to the preparation of financial statements,
- (d) Closing entries, and
- (e) Opening entries used in determining capital (owners' equity) of an ongoing business that did not use double entry before.

We will briefly see examples of the purchase of assets and opening entries. The remaining items will be covered later in form three.

The general journal specifies the double entries (debit and credit entries) required to be made in respect of different transactions following the rules of debit and credit. As noted above, it is possible for the general journal to be used to record all kinds of transactions conducted by the business. This is because it gives direct guidance of the accounts and sides to which entries should be posted. However, in case a business decides that it uses only a general journal, but happens to have some dealings on credit (sales, purchases, and returns), it will need to have some memorandum records (schedules) of the details of such dealings. For this reason, entries in the general journal should be focused towards a general ledger. In other words, it is not common to find a general journal entry made in relation to an individual account of a debtor or a creditor.

## **Functions of a general journal**

A general journal has the following functions:

- (a) It acts as a diary where business transactions are recorded as soon as they occur.
- (b) It gives the directions on which accounts should be debited and credited in respect of each transaction following the rules of double entry.
- (c) It provides brief narrations of each transaction recorded. This is very important because as opposed to the special journals, this journal records different types of transactions.
- (d) Since the transactions are recorded chronologically and include brief narrations, it is easy for a person to review and identify any possible errors that may have been made when recording.

### Format of the general journal

Date	Details	Folio	Debit	Credit
	The name of the account to be debited.		xxx	
	The name of the account to be credited.			xxx
	<i>A brief narration of the transaction.</i>			

From the format of the journal proper presented above, the following should be noted: -

- The journal instructs what accounts should be debited and credited.
- The name of the account that is supposed to be debited appears first followed by the name of the account that needs to be credited.
- A narration must be given to explain the details of the transaction.

#### A worked out example 3.5

##### Recording in the general journal: Purchase of non-current asset on credit

Non-current assets refer to properties that the business owns such as furniture, equipment and buildings. These assets are usually used for more than one accounting period. When a business purchases these types of assets, their recording in the general journal will follow the double entry rules. For example, a furniture is purchased on 16 January 2020, for TZS 550,000 on credit from Jerome.

The transaction involves an increase in asset (furniture) and an increase in liabilities (amount payable to Jerome, the creditor). Following the double entry rules, the recording in the journal will be presented as follows:

##### General journal

Date	Details	Folio	Debit	Credit
16/1/2020	Furniture account		550,000	
	Accounts Payable			550,000
	<i>Being the purchase of furniture on credit from Jerome</i>			

### Opening entries

Opening entries refer to the initial entries used to record business transactions when the business is being established or starting a new accounting period. Sometimes the

business will have balances of different items while missing others. For example a business may have balances of assets and liabilities but missing the balance of capital in its records. In this case, the value of a capital can be calculated using the accounting equation that is:

$$\text{ASSETS} = \text{CAPITAL} + \text{LIABILITIES}$$

The values of each asset and liabilities together with the calculated value of capital are then recorded in the general journal showing debit entries for assets and credit entries for liabilities and capital. Once this is done, subsequent increases and decreases in assets, liabilities and capital are made in the usual way as for any other business following the rules of debit and credit.

### A worked out example 3.6

Mlingoti Shop had the following values for assets and liabilities as at 1 May 2020.

Assets: Motor Van TZS 7,400,000; Fixtures TZS 3,600,000; Inventory TZS 8,400,000.

Accounts receivable – Halima TZS 190,000; Jackson TZS 90,000; Bank TZS 1,720,000; Cash TZS 130,000.

Liabilities: Accounts payable – Queen TZS 258,000; Edgar TZS 820,000.

### Solution

The total of assets is  $7,400,000 + 3,600,000 + 8,400,000 + 190,000 + 90,000 + 1,720,000 + 130,000 = \mathbf{21,530,000}$

While the total of liabilities is  $258,000 + 820,000 = \mathbf{1,078,000}$ . From the accounting equation we know that:

$$\text{ASSET} = \text{CAPITAL} + \text{LIABILITIES}$$

Since we already know the value of assets and liabilities of Mlingoti, we can determine the value of the capital through rearrangement of this equation such that:

$$\text{CAPITAL} = \text{ASSETS} - \text{LIABILITIES}$$

Therefore:  $\text{CAPITAL} = 21,530,000 - 1,078,000 = \mathbf{20,452,000}$



After obtaining the value of capital, the journal proper can now be prepared as follows:

## Journal Proper

Date	Details	Folio	Debit (TZS)	Credit (TZS)
2020 May 1	Motor Van		7,400,000	
	Fixtures		3,600,000	
	Inventory		8,400,000	
	Accounts receivable: Halima		190,000	



## Exercise 3.2

Kelele shop has been in operation for 5 years. On 31 June 2021 the shop owner, Mr. Kimya Kichache gave you a list of assets and liabilities as follows:

	<b>TZS</b>
Shop Kiosk	1,500,000
Fixtures	700,000
Stock of goods	2,600,000
Cash at bank	500,000
Cash in hand	200,000
Loan from Kichwa Kigumu	300,000
Amounts due to Mwingi for a supply of goods	500,000

**Required:**

- Identify the assets and liabilities of Kelele shop.
- Prepare a journal proper for the items as on 31 June 2021.

## Cash book

A cash book is a book of prime entry used to record transactions that involve a movement of cash that is, receiving or paying cash by the business. Since cash is an asset for the business, receipts of cash are recorded by a debit entry in the cash book (increase in assets) and payment of cash is recorded by a credit entry in the cash book (decrease in asset). The cash book has a unique characteristic because apart from being classified as a book of prime entry, it also forms part of a general ledger. This is because some small businesses that operate strictly on cash basis find it easy to skip journals and instead enter all transactions (receipts and payments) in the cash book. When they complete the corresponding entries to the other ledger accounts; they refer to that as posting.

There are four types of cash books namely single column, two column cash book, three column cash book and petty cash book. In this book, you will learn only one type of cash book known as a single column cash book. Simply, the single column cash book is the cash account and bank account that you will encounter when posting transaction in ledger account in the following Chapter. Other types of cash books namely two column cash book, three column cash book and petty cash book will be studied in form two.



### Activity 3.4

Your friend would like to know why sales daybooks, purchases daybooks, purchase returns, sales returns, cash books and journal proper are called books of prime entry. Write a brief summary of your response to him. In your response, please point out why it is important for an enterprise to use books of prime entry to record its daily transactions.



## Revision Exercise 3

1. Mention six types of books of prime entry.
2. List six source documents used in the preparation of books of prime entry.
3. Briefly explain the importance of preparing journals.
4. Record the following transactions in the purchases daybook and show total purchases for the month.

2020 July 1 Bought from Kateme LTD:

20 bags sugar, each with 5kgs, @ TZS 15,000.

15 bags of wheat flower, each 6kgs, @ TZS 8,000.

10 Bought from Salehe:

12 dozen of exercise books @ TZS 1,600.

2 cartons of duplicating paper @ TZS 24,000.

14 Bought goods from Jengua for TZS 48,800.

25 Bought from Kiharusi:

10 pairs of shoes @ TZS 12,000.

14 boxes shoe polish @ TZS 7,000.

5. Record the following transactions in the sales daybook of Mpili and show total sales for the month.

2019 Feb. 4 Sold to Ambwene:

15 boxes of biscuits @ TZS 9,500.

6 cases of beer @ TZS 30,000.

9 Sold to Mangi:

30kgs milk powder worth @ TZS 6,000.

60 cartons soap @ TZS 2,000.

12 Sold goods worth TZS 17,000 to Halima.

19 Sold goods to Njiwa TZS 7,500.

19 Sold goods to Paula TZS 1,200.

25 Sold to Mwanahela:

5 sets of table knives, each set has 6 pieces at TZS 1,000 per knife.

- 200 frying pans set @ TZS 10,000.  
100 sufuria at @ TZS 5,500.
- 27 Sold a shirt to Okelo TZS 15,000.
- 28 Sold goods to Kaseke:  
700 bags cement of 50kg @ TZS 15,500.  
120 garden forks @ TZS 4,500.  
50 pairs of shoes worth @TZS 13,000.
- 29 Sold goods to Haruna worth TZS 11,600.
6. Enter the following transactions in Joanita's purchases daybook, purchase returns daybook, and show total purchases and returns for the month.
- 2020 May Bought 10 bags of beans, each 5kgs, @ TZS 10,000 from  
1 National Distributors LTD.
- 4 Bought 4 gallons of cooking oil for @ TZS 15,000 from  
GEFCO.
- 5 Returned one bag of beans to National distributors LTD.  
because it weighed less.
- 8 Bought 10 dozens of bed sheets from Kilimanjaro Textile @  
TZS 22,000.
- 10 Returned to GEFCO one gallon of cooking oil as it was not the  
quality ordered.
- 15 Purchased from GEFCO 100 dozen of baby milk @ TZS  
16,000.
- 20 Returned one dozens of bedsheets to Kilimanjaro Texttiles as  
they were of poor quality.
- 25 Returned 5 dozens of baby milk to GEFCO that were spoilt in  
transit.
- 26 Purchased 20 dozens of bed sheets from Kilimanjaro Textile  
@ TZS 25,000.
- 28 Returned 5 dozens of bed sheets to Kilimanjaro textiles in 26  
May as they were not of the size ordered.

7. Write up a sales returns daybook and show the total sales returns for the month.

2020 June 1 Received goods from Mzizima store:  
 20 boxes of coloured chalks @ TZS 15,000.  
 10 boxes of counter books @ TZS 20,000

*Wrong specifications.*

10 Received goods from Mzinga shop:  
 20 cartons of water @ TZS 6,000.  
 25 boxes of biscuits @ TZS 5,000.

*Expired*

25 Received goods from Mzalendo store  
 5 bags of rice @ TZS 30,000.  
 2 bags of wheat flour @ TZS 20,000.

*Less weight*

8. Mawingu started a business several years ago. She did not keep proper books of accounts. On 1 January 2020 she decided to start keeping records following the double entry system. From her previous memorandum records, she was able to come up with the following assets and liabilities:

	TZS
Cash in hand	50,000
Cash at bank	1,624,000
Furniture	410,000
Machinery	720,000
Accounts receivable: Lulu	316,000
Bunda	129,000
Accounts payable: Mangwana	217,000
Mkudesimba	128,000

**Required:**

From the above information prepare a journal proper and calculate the amount of capital as on 1 January 2020.

9. Following the information extracted from James trader's books who sells a variety of goods on credit, prepare a purchases daybook for the month ending 31 January 2020.

January 1 Bought goods from MOTCO Co. LTD:

2 boxes of pens worth TZS 7,500 per box.

4 Television sets valued at TZS 370,000 per set.

7 Bought from Magda Textile mills:

3 bales of Khanga at TZS 30,000 a bale.

2 pieces of Vitenge @TZS 10,000 per piece.

24 Bought from Coca Cola industries LTD:

10 crates of sprite worth TZS 10,000 per crate.

8 crates of Fanta worth TZS 10,000 per crate.

10. Umoja wa Vijana Co. LTD sells the following items to the society.

2021 March 1 Sold to Judestina:

3 Pairs of shoes @ TZS 32,000 per pair.

2 pairs of trousers @ TZS 17,000.

4 Sold to Unguja secondary school:

100 pieces of scaff @ TZS 2,500 a scaff.

70 students' identity cards @ TZS 3,000 per identity card.

300 Geography textbooks @ TZS 12,000

18 Sold to Watoto Wadogo Sports Club:

50 footballs @ TZS 15,000

20 T-shirts @ TZS 9,000

Enter the above details into the sales daybook for the month of March.



11. Record the following transactions in Chipukizi society's sales daybook, purchase daybook, sales returns, purchases return and journal proper then show the total at the end of month.

2020 April 1 Sold 90 duplicating ream paper to Hawa @ TZS 9,000 per ream.

2 Bought from Ujamaa LTD:

10 bags of 5kg wheat flour @TZS 7,000.

3 buckets of 10 litres of cooking oil for TZS 150,000.

6 Hawa returned 7 duplicating ream of papers damaged in transit.

8 Returned to Ujamaa LTD.

2 bags of 5kg wheat flour, under weight

9 Sold to Peace and Love Group:

20 pairs of shoes @ TZS 12,000.

30 pairs of socks @TZS 1,000 per pair.

14 Bought from Mwanza traders:

20 pieces white bed sheets @ TZS 15,000.

14 pieces of mattress covers @ TZS 17,000.

16 Returned to Mwanza traders.

02 pieces of white bed sheets not of the colour ordered.

18 Issued a credit note to Peace and Love group for goods returned:

4 pairs of shoes not of the size ordered.

1 pair socks not of the colour ordered.

20 Bought furniture from Viwawa Co. LTD, worth TZS 200,000 on credit.

12. Mpenda Roho started a business several years ago. He did not keep proper books of accounts. On 1 January 2020 he decided to start keeping records following the double entry system. From his previous memorandum records, he was able to come up with the following assets and liabilities:

	TZS
Cash in hand	300,000
Cash at bank	1,200,000
Accounts receivable - R. Bakora	240,000
C. Mkubwa	200,000
Accounts payable - A. Malenga	480,000
B. Swala	640,000
Inventory	250,000
Equipment	580,000
Shop fixtures and fittings	3,800,000
Motor vehicle	13,050,000
Premises	15,600,000

**Required:**

Enter the above balances in a journal proper and calculate the amount of capital.

13. Show journal entries necessary to record the following transactions:

2020 April 1 Bought fixtures on credit from Ushirika Co. LTD TZS 135,000.

3 Bought Motor van on credit from Nyumbu Co. LTD TZS 75,000,000.

5 Bought additional fixtures on credit from Keko Traders TZS 2,150,000.

8 Purchased premises from DNA LTD on credit TZS 15,000,000.

14. Enter the following transactions into the sales journal of Akilimali for the month of January, 2020

2020 January 1 Sold goods to Mama Eli, invoice number 06136:

16 national radio @ TZS 25,000.

25 record players @ TZS 12,000.

7 Sold goods on credit to Pombe worth TZS 20,000, invoice number 06137:

- 10 Sold goods to Nusuhela, invoice number 06138:  
60 footballs @ TZS 115,000.  
100 pairs sport shoes @ TZS 50,000.  
90 packets of socks @ TZS 2,000.
- 15 Sold goods on credit to Judith TZS 270,000 and issued invoice number 06139.
- 25 Sold goods to Fred, invoice number 06140:  
65 accountancy books @ TZS 15,000.  
10 dozens ball point pencils @ TZS 36,000.  
40 dozens staff ledger @ TZS 2,500.
- 27 Sold goods to Bwiikizo Enterprise worth TZS 920,000 and issued invoice number 06141.
- 29 Sold goods to Wajamaa Traders, invoice number 06142:  
15 bags of wheat flour, each with 50kgs,  
@TZS 67,500.  
25 bags of sugar, each with 50kgs, at @TZS 72,000.
- 31 Sold goods to Rubale Shop, invoice number 06143:  
60 curtains at @TZS 25,000.  
80 bed sheets at @TZS 20,000.

# Chapter Four

## Ledgers

### Introduction

*The posting of accounts to a ledger follows the principle of double entry system of Book-Keeping that was covered in chapter two. Posting of accounts to the ledger involves posting the accounts to both subsidiary and general ledgers. In this chapter, you will learn the concept of a ledger, posting entries to a ledger and balancing of accounts. The competencies developed in this chapter will enable you to post entries from various books of prime entries to respective ledger accounts and thereafter balance the ledger accounts.*

### Concept of a ledger

This section presents the meaning of a ledger, types of ledgers, the importance of ledgers, the classification of accounts and the posting of entries to the ledger.

### Meaning and format of a ledger

#### (a) Meaning of a ledger

A ledger is like a diary but is used to record money transaction only. It is a book for keeping track of expenses, profits, and other financial matters. It is, therefore, a record in which accounts are kept. The ledger is often referred to as the main book of accounts. This is because balances that are used for the preparation of financial statements are generated from ledgers. Entries of different transactions are posted to ledgers from the books of

prime entries. The posting is done to specific accounts in the ledgers.

#### (b) Format of a ledger

A ledger contains specific records called accounts. An account is a record which shows increases and decreases of a specific asset, liability, revenue, expense, or capital item in the ledger. To be able to take care of both increases and decreases, the ledger account has two sides, namely the left-hand side, which is called the debit side (abbreviated as Dr) and the right-hand side which is called the credit side (abbreviated as Cr). For the purpose of capturing important details, each ledger account must have a name or title. Additionally, each side of the ledger account has the following columns:

**(i) Date**

This column is used to write the date, month, and the year of the transaction.

**(ii) Particulars**

This column indicates a short description of the entry for the transaction recorded. In the ledger account, this column indicates the name of the account to which the corresponding entry has been made for the transaction.

**(iii) Folio**

This column records pages of reference in books of accounts.

**(iv) Amount**

This column records the amount of money being transacted.

The format of the ledger account is as presented below.

Debit (Dr)				Name of the account				Credit (Cr)			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount

**Types of ledgers**

There are two main types of ledgers:

**Subsidiary ledger**

A subsidiary ledger is a ledger that contains accounts of individuals for the purpose of recording transactions between the entity and each individual. The most common subsidiary ledgers are sales ledger and purchases ledger. However, different enterprises may have some other subsidiary ledgers depending on the volume of transactions and the need for details on different classes of transactions. The sales and purchases ledgers are explained as follows:

**Sales ledger**

A sales ledger is a subsidiary ledger used to record transactions regarding credit customers also known as debtors. Therefore, the sales ledger comprises of individual accounts of debtors. The other name for debtors' accounts is an accounts receivable. The sales ledger can also be referred to as the accounts receivable ledger or the debtors' ledger.

**Purchases ledger**

A purchases ledger is a subsidiary ledger used to record transactions with creditors or suppliers of goods or services on credit. A purchases ledger comprises of individual accounts

of creditors. The other name for creditors' accounts is accounts payable. The purchases ledger can also be referred to as the accounts payable ledger or the creditors' ledger.

### **General ledger**

The general ledger contains different accounts that do not record transactions relating to individuals. Instead, it deals with total amounts from special journals for example sales and purchases journals, or postings from the general journal to accounts that represent each class of transactions, namely revenue, expenses, assets, liabilities and owners' equity (capital). Posting of entries to the general ledger follows the double entry principle and forms the basis of balances used in preparing financial statements. A general ledger includes the cash book, which in some cases is also regarded as a book of prime entry. This was discussed in Chapter Three. A general ledger may also include other ledgers such as the private ledger.

### **Private ledger**

There are ledgers that directors would not want their staff to see due to different reasons including technical know-how. These types of ledgers are called private ledgers. A private ledger is a ledger used to keep confidential information of the proprietor. In this regard, the proprietor would not like the office staff or outsiders to see them. Examples of private ledgers are a capital ledger, and a drawings ledger.

### **Importance of ledgers**

Every enterprise needs to post financial transactions in ledgers as they play important roles as follows:

#### ***They enable double entry to be completed***

The double entry principle requires every transaction to be recorded twice. That is, every debit entry must have its corresponding credit entry. The posting of entries in ledger accounts follows the principle of double entry. Since a ledger account has a debit and a credit side, where debit and credit entries are posted, that facilitates double entry completion.

#### ***They are used in the classification of accounts***

Usually, accounts are classified into two categories. These are personal and impersonal (real and nominal) accounts. The preparation of ledgers enables the book-keeper to classify accounts easily according to their nature.

#### ***Information extracted from a balanced ledger can be used for statistical purposes***

Balances extracted from ledger accounts can be used as inputs for further analysis and projections concerning the firm. These balances can also be used for statistical

purposes where they can be used as inputs by researchers who are researching on business enterprises or the industry where the enterprise is operating.

### *They are used to keep financial records permanently*

Financial transactions posted on ledger accounts are permanent and cannot be altered. This enables the owner and any other third parties such as auditors and government authorities to make a reference of any transaction that was recorded in the ledger accounts. Government authorities, for example, may need to review the financial records of the enterprise if it is investigating a particular transaction relating to illegal business.

### *They are used in the preparation of a Trial balance*

A ledger balance forms a basis for the preparation of a trial balance. In simple terms, there is no trial balance if there are no general ledger accounts.

### *They provide information that is used as inputs when preparing the income statement and the statement of financial position*

Financial information that is used as inputs in the preparation of financial statements (income statement and the statement of financial position) originates from ledgers. Therefore, the information extracted from ledgers makes the preparation of financial statements possible.

## **Classification of accounts**

This is the process of grouping accounts with similar nature and characteristics. The posting of entries from both general and special journals involves opening different ledger accounts. Different types of ledger accounts influence the way such accounts affect the financial statements. It is, therefore, important at this stage to discuss different types of accounts. There are two types of accounts, namely personal accounts and impersonal accounts.

### **(a) Personal accounts**

These types of accounts record transactions relating to persons. Legally, there are two types of persons; a natural person and an artificial person. A natural person is a person who was born biologically. Examples of natural persons are: Juma, Asha, and Anna. On the contrary, an artificial person is the one formed under the law and empowered to perform activities (including business) in their own name, within the powers given to them by the law. Examples of artificial persons are: Coca-Cola Company, Tanzania Institute of Education and Kijiko Sports Club. That is to say, in the eyes of the law,



an artificial person is treated in the same manner as a natural person. Therefore, such entries are recorded under the category of accounts known as personal accounts.

### (b) Impersonal accounts

These are types of accounts that record all other transactions except those recorded in personal accounts. In other words, they do not record transactions relating to persons or firms. Impersonal accounts are further classified into real accounts and nominal accounts as explained below:

#### *Real accounts*

These accounts record transactions relating to assets and liabilities in the general ledger, that is, other than personal accounts. These accounts are real because they are not closed at the end of the accounting period, but have their balances carried forward to the next period. Examples of real accounts include accounts for assets such as land and buildings, machinery, furniture and fittings, motor vehicles, accounts receivable, cash at the bank and cash in hand. Others include, liabilities such as accounts payable, bank overdrafts and bank loans.

#### *Nominal accounts*

Nominal accounts record transactions relating to expenses and revenues. Expenses are costs incurred for running a business. Examples of such expenses are rent, salaries, purchases, carriage, advertising, discounts allowed and bad debts. Moreover, revenues are gains of a business. Examples of revenues are: sales, discount received, interest received, and commission received. Accounts falling under this category are closed at the end of the accounting period with their figures transferred to the income (profit or loss) statement.

#### A worked out example 4.1

No.	Name of account	Classification
1	Anna	Personal account
2	Furniture	Real account
3	Sales	Nominal account
4	Losses	Nominal account
5	Cash	Real account
6	Capital	Personal account
7	Buildings	Real account

**Activity 4.1**

Indicate whether the following accounts are nominal, real, or personal accounts.

No.	Name of Account	Classification
1	Abela	
2	Drawings	
3	Advertising	
4	Fixtures	
5	Purchases returns	
6	Motor Van	
7	Profit	
8	Purchases	
9	ABC Co. LTD	

**Posting entries to a ledger**

Posting of entries to a ledger follows the double entry principle of Book-Keeping. For the case of a general journal, the journal entry would have already specified the name of the accounts and amounts to be debited and credited for each transaction.

In case of special journals, the journal entries do not give direct guidance on accounts to be debited and credited. This means that for special journals, the following have to be identified before posting:

**The account to which the entry is made**

In case of special journals, the account will be dictated by the nature of the journal and the name used in the journal entry as follows:

**(a) The nature of the account**

The posting will be made depending on what element of the accounting equation is affected by the transaction. It is therefore important to identify whether the account to be posted is for assets, liabilities, revenue, expenses or owner's equity (capital).

**(b) The effect of the transaction**

Once it is known which element is affected by the transaction, we need to establish whether the transaction involves an increase or a decrease in that element. This will help to decide whether the account identified in (a) above will be debited or credited.

### Posting from the sales journal

The sales journal records credit sales of goods to customers. These transactions lead to an increase in revenue (sales) and an increase in assets (receivables). Like all the other special journals, posting entries from the sales journal is done in two stages as follows:

#### *Stage one: Posting to a subsidiary ledger*

Posting to a subsidiary ledger involves posting the entries to the individual accounts of each customer who appears in the journal. The entries are made on the debit side of the respective accounts (personal accounts of each customer) since the transactions involved are the increases in assets (receivables from each respective customer).

#### *Stage two: Posting to the general ledger*

The general ledger posting involves a periodic (weekly, monthly, etc.) record of the total from the journal. These are posted to the sales account and the receivables account as they represent increases in revenues (sales) and receivables respectively. Therefore, the receivable accounts will be debited while the sales accounts will be credited.

The entries made are therefore:

**Debit:** Account receivables

**Credit:** Sales account

### Posting from the sales returns journal

The sales returns journal records returns of goods from credit customers. These transactions lead to a decrease in revenue (sales are decreased by sales returns) and a decrease in assets (receivables). Like all the other special journals, posting entries from the sales returns journal is done in two stages as follows:

#### *Stage one: Posting to a subsidiary ledger*

Posting to a subsidiary ledger involves posting the entries to the individual accounts of each customer in the journal. The entries are made on the credit side of the respective accounts (personal accounts of each customer) since the transactions involved decrease the assets (receivables from each customer).

#### *Stage two: Posting to the general ledger*

The general ledger posting involves the periodic (weekly, monthly, etc.) totals of the journal. These are posted to the sales returns account and the receivable account as they represent decreases in revenues (sales, through returns) and receivables respectively.

The entries made are therefore:

**Debit:** sales returns account

**Credit:** receivables account

**A worked out example 4.2**

Kassimu made the following sales during the month of June.

2020 June 1 Sold to Mambo:

80 packets of rice @ TZS 2,200.

60 bags of wheat flour, with 3kgs, @ TZS 4,500.

12 Sold to Kifundo Enterprise:

15 boxes of toothpastes (50grms), @ TZS 2,600.

16 pieces of writing pads @ TZS 2,350.

19 Sold to Rudia stores:

11 pairs of running shoes @TZS 6,000.

20 school shirts @ TZS 1,200.

25 Sold goods to Kalumanzira worth TZS 82,000 on credit.

28 Sold goods to Glory:

15 pairs of sandals @ TZS 8,500.

10 bags of rice, with 3kgs, @ TZS 6,000.

From the sales transactions above, the following goods were returned:

June

2 Mambo returned 10 packets of rice @ TZS 2,200 because they were spoiled.

8 Rudia stores returned:

3 pairs of running shoes @ TZS 6,000 because they were oversize.

2 school shirts @ TZS 1,200 because they were of the wrong colour.

18 Kifundo Enterprises returned:

3 boxes of toothpaste (50grms), @ TZS 2,600 because they were of the wrong type.

2 pieces of writing pads @ TZS 2,350 because they were damaged.

You are required to enter the transactions in the sales journal and sales returns journal and then post the entries to the relevant subsidiary ledger and the general ledger accounts.

### Solution

The first step is the preparation of the sales daybook or sales journal.

#### Sales daybook

Date	Particulars	Folio	Invoice Number	Invoice Details (TZS)	Invoice Totals (TZS)
2020 June 1	<b>Mambo:</b> 80 packets of rice @ TZS 2,200  60 bags of wheat flour (3kgs), @ TZS 4,500	SL <sub>1</sub>		176,000  270,000	446,000
12	<b>Kifundo Enterprises:</b> 15 boxes of toothpaste (50grms), @ TZS 2,600  16 pieces of writing pads @ TZS 2,350	SL <sub>2</sub>		39,000  37,600	76,600
19	<b>Rudia stores:</b> 11 pairs of running shoes @ TZS 6,000  20 school shirts @ TZS 1,200	SL <sub>3</sub>		66,000  24,000	90,000
25	<b>Kalumanzira:</b> Goods	SL <sub>4</sub>			82,000
28	<b>Glory:</b> 15 pairs of sandals @ TZS 8,500  10 bags of rice (3kgs), @ TZS 6,000	SL <sub>5</sub>		127,500  60,000	187,500
30	<i>Total transferred to the sales account (Cr)</i>	<b>GL</b>			<b>882,100</b>

The second step is the preparation of the sales returns daybook or sales returns Journal.

### Sales returns daybook

Date	Particulars	Folio	Invoice Number	Invoice Details (TZS)	Invoice Totals (TZS)
2020 June 2	<b>Mambo:</b> 10 packets of rice @ TZS 2,200	SL <sub>1</sub>			22,000
8	<i>Spoiled</i> <b>Rudia stores:</b> 3 pairs of running shoes @ TZS 6,000	SL <sub>3</sub>		18,000	
	<i>Oversize</i> 2 school shirts @ TZS 1,200			2,400	20,400
18	<i>Wrong colour</i> <b>Kifundo Enterprises:</b> 3 boxes of toothpaste (50grms), @ TZS 2,600	SL <sub>2</sub>		7,800	
	<i>Wrong type</i> 2 pieces of writing pads @ TZS 2,350			4,700	12,500
	<i>Damaged</i>				
30	<i>Total transferred to sales returns account (Dr)</i>	GL			54,900

The third step is to post the entry in the subsidiary ledger and the general ledger.

### Sales ledger

**Dr** **Mambo account (1)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
1/6/2020	Sales		446,000	2/6/2020	Sales returns		22,000

**Dr** **Kifundo enterprises account (2)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
12/6/2020	Sales		76,600	18/6/2020	Sales returns		12,500

**Dr** **Rudia stores account (3)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
19/6/2020	Sales		90,000	8/6/2020	Sales returns		20,400

**Dr** **Kalumanzira account (4)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
25/6/2020	Sales		82,000				

**Dr** **Glory account (5)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
28/6/2020	Sales		187,500				

### General ledger

**Dr** **Sales account** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
				30/6/2020	Accounts Receivable		882,100



Dr		Sales returns account				Cr	
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
30/6/2020	Accounts Receivable		54,900				

Dr		Accounts Receivable				Cr	
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
30/6/2020	Sales		882,100	30/6/2020	Sales returns		54,900



## Exercise 4.1

1. Kichwa runs a food stuff kiosk in Kilimani. During the month of September 2021, his business sold goods on credit as follows:

2021 September	1	Sold to Kakwa: 50 Kilograms of rice @TZS 1,000. 100 Kilogrmas of beans @TZS 2,000.
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15 Sold to Mafundo:  
200 kilograms of maize @TZS 500.  
1,000 Kilograms of millet @TZS 800.

20 Sold to Vumi goods for TZS 100,000 on credit.

25 Sold the following goods to Omari:

1,000 Kilograms of rice	@TZS 1,500.
200 Kilograms of sugar	@TZS 2,500.
500 Kilograms of salt	@TZS 100.

The customers above returned some of the goods due to various reasons as follows:

2021 September 5 Kakwa:  
20 Kilograms of beans  
10 Kilograms of rice  
*Wrong quality*

- 21 Mafundo  
100 Kilograms of millet  
*Excess quantity*
- 30 Omari:  
100 Kilograms of rice  
100 Kilograms of sugar  
*Damaged packages*

You are required to:

- (a) Enter the transactions in the sales journal and sales returns journal.
- (b) Post the entries in the relevant ledger and general ledger accounts.

2. During the month of October 2021 Mr Ngapo sold the following items on credit to the customers.

- 2021 October 4 Sold to Sanko & Co:  
10 Television sets @TZS 350,000.  
16 Television remote controls @ TZS 10,000:
- 17 Sold to Mpela hungers LTD:  
20 Television decoders @ TZS 99,000.  
80 computers (laptops) @ TZS 400,000.
- 21 Sold to Paul Matelephone LTD:  
18 screen protectors @ TZS 3,000.  
29 Flash disks @ TZS 8,000.

You are required to use the information provided above to prepare a sales journal and post it to the general ledger and other ledgers.

3. During the month of October 2021, the following items were returned by different customers due to various reasons.

- 2021 October 26 Sanko & Co. returned the followings:  
2 Television sets @TZS 350,000, due to wrong brand.  
5 Television remote controls @ TZS 10,000, due to technical faults.
- 30 Mpela hungers LTD, returned the followings:  
8 Television decoders @ TZS 99,000, broken.  
6 computers (laptops) @ TZS 400,000, wrong type.

You are required to use the given details to prepare a sales returns journal and post it to the respective ledgers and general journal.

### Posting from the purchases journal

The purchase journal records the purchases of goods bought on credit from suppliers. These transactions lead to an increase in expenses (purchases) and an increase in liabilities (payables). Like all the other special journals, posting entries from the purchases journal is done in two stages as follows:

#### *Stage one: Posting to subsidiary ledger*

Posting to a subsidiary ledger involves posting the entries to the individual accounts of each supplier in the journal. The entries are made on the credit side of the respective accounts (personal accounts of each supplier) since the transactions involved are the increases in liabilities (payables to each supplier).

#### *Stage two: Posting to the general ledger*

The general ledger posting involves the periodic (weekly, monthly, etc.) totals of the journal. These are posted to the purchases account and the payables account as they represent increases in expenses (purchases) and liabilities (payables) respectively. The entries made are therefore:

**Debit:** purchases account

**Credit:** payables account

### Posting from the purchases returns journal

The purchases returns journal records transactions related to goods returned to suppliers that were purchased on credit. These transactions lead to a decrease in expenses (purchases are decreased by purchases returns) and a decrease in payables. Like all the other special journals, posting entries from the purchases returns journal is done in two stages as follows:

#### *Stage one: Posting to a subsidiary ledger*

Posting to a subsidiary ledger involves posting the entries to individual accounts of each supplier in the journal. Entries are made on the debit side of respective accounts (personal accounts of each supplier) since these transactions decrease liabilities (payables to each supplier).

#### *Stage two: Posting to the general ledger*

The general ledger posting involves, the periodic (weekly, monthly, etc.) totals of the journal. These are posted to the purchases returns account and the payables account as they represent a decrease in expenses (purchases are decreased by purchases return) and payables respectively. The entries made are therefore:

**Debit:** payable account

**Credit:** purchases returns account

### A worked out example 4.3

Record the following transactions in the purchases daybook and the purchase returns daybook and then post the items to the relevant subsidiary account and general ledgers in the purchases ledgers. Then transfer the transactions to the purchases account and purchase returns in the general ledger.

2020 July 1 Bought from Tom LTD:

10 bags rice, each weighing 5kgs, @ TZS 10,000.

20 bags of sugar, each weighing 10kgs,  
@ TZS 15,000.

9 Bought from Asha:

10 dozen of books @ TZS 2,000.

5 cartons of ruled papers @ TZS 30,000.

16 Bought goods from Katabo for TZS 60,800.

29 Bought from Mwanaidi:

15 pairs of sandals @ TZS 15,000.

14 boxes drawing pens @ TZS 5,000.

The following goods were returned during the month:

July 8 Tom LTD returned:

2 bags of rice, each weighing 5kgs @ TZS 10,000 because  
they had expired.

4 bags of sugar, each weighing 10kgs @ TZS 15,000 because  
they had spoiled.

18 Asha returned:

4 dozen of books @ TZS 2,000 because were of the wrong  
specification.

1 carton of ruled papers @ TZS 30,000 because it was not  
ordered.

29 Katabo returned:

Goods worth TZS 14,800 were spoiled.

**Solution**

The first step is the preparation of the Purchases daybook or purchases journal.

**Purchases daybook**

Date	Particulars	Folio	Invoice Number	Invoice Details (TZS)	Invoice Totals (TZS)
2020 July 1	Tom LTD: 10 bags of rice @ TZS 10,000 20 bags of sugar @ TZS 15,000	PL <sub>1</sub>		100,000 300,000	400,000
9	Asha: 10 dozen books @ TZS 2,000 5 cartons of ruled paper @ TZS 30,000	PL <sub>2</sub>		20,000 150,000	170,000
16	Katabo: Goods	PL <sub>3</sub>			60,800
29	Mwanaidi: 15 pairs of sandals @ TZS 15,000 14 Boxes of drawing pens @ TZS 5,000	PL <sub>4</sub>		225,000 70,000	295,000
31	Total transferred to purchases account (Dr)	GL			925,800

The second step is the preparation of the Purchases returns daybook or purchases returns journal.

### Purchase returns daybook

Date	Particulars	Folio	Invoice Number	Credit note (TZS)	Credit note Totals (TZS)
July 8	Tom LTD: 2 bags of rice @ TZS 10,000 4 bags of sugar @ TZS 15,000	PL <sub>1</sub>		20,000 60,000	80,000
18	<i>Spoiled</i> Asha: 4 dozen books@ TZS 2,000 <i>Wrong specification</i> 1 carton of ruled paper @ TZS 30,000	PL <sub>2</sub>		8,000 30,000	38,000
29	<i>Not ordered</i> Katabo: <i>Goods spoiled</i>	PL <sub>3</sub>			14,800
31	Total transferred to purchases returns account (Cr)	GL			132,800

### Posting to the subsidiary ledger

The third step is to post the entry in the subsidiary ledger and general ledger.

### Purchases ledger

Dr				Tom LTD account (1)				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
8/7/2020	Purchase returns		80,000	1/7/2020	Purchases		400,000				

Dr				Asha account (2)				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				
18/7/2020	Purchase returns		38,000	9/7/2020	Purchases		170,000				

Dr				Katabo account (3)				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				
29/7/2020	Purchase returns		14,800	16/7/2020	Purchases		60,800				

Dr				Mwanaidi account (4)				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				
				29/7/2020	Purchases		295,000				

### Posting to the general ledger

Dr				Purchases account				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				
31/7/2020	Accounts Payable		925,800								

Dr				Purchases returns account				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				
				31/7/2020	Accounts payable		132,800				

Dr				Accounts Payable				Cr			
Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount				
31/7/2020	Purchases Returns		132,800	31/7/2020	Purchases		925,800				



### Posting from the general journal

Posting from the general journal follows what the journal entries have specified in terms of accounts and amounts to be debited and credited for each individual transaction. The postings are made straight to the general ledger, but they do not include individual accounts of creditors and debtors. This is because the individual accounts would be handled by special journals and their respective postings to subsidiary ledgers. In case of entities that do not maintain special journals, posting from the general journal are made to general ledgers, and the enterprise would maintain a separate memorandum record of credit dealings with suppliers and customers. It is also important to note that the posting of transactions from the general journal includes the posting from the cash book (cash account, and bank account). Cash and bank accounts are also books of prime entry.

#### A worked out example 4.4

Enter the following transactions in the general journal and post the entries to the general ledger up to 30 January 2020.

- 2020 January
- 1 Diana started a business by depositing TZS 2,000,000 into a bank account.
  - 4 Purchased machinery worth TZS 200,000 on credit from Alpha.
  - 8 Purchased goods worth TZS 400,000 on credit from Julius.
  - 12 Sold goods worth TZS 150,000 by cash.
  - 16 Withdrew TZS 200,000 from the bank account for business use.
  - 20 Sold goods to Tandahimba LTD worth TZS 50,000 on credit.
  - 22 Returned goods worth TZS 15,000 to Julius because they were of the wrong type.
  - 23 Paid Julius TZS 200,000 by cheque.
  - 24 Paid wages TZS 30,000 by cash.
  - 26 Withdrew TZS 100,000 from the bank account for personal use.
  - 27 Purchased goods from Frida worth TZS 150,000 promising to pay for them later.
  - 28 Tandahimba LTD returned goods worth TZS 5,000 because they had expired.
  - 29 Received rent in terms of cash TZS 50,000.
  - 30 Received payment in terms of cheque from Tandahimba LTD TZS 20,000.

**Solution**

The first step is the preparation of the general journal or journal proper.

**Journal entries**

<b>Date</b>	<b>Particulars</b>	<b>Debit (TZS)</b>	<b>Credit (TZS)</b>
1-Jan-20	Bank account Capital account <i>Being capital deposited in the bank</i>	2,000,000	2,000,000
4-Jan-20	Machinery account Accounts Payable <i>Being a machine bought on credit</i>	200,000	200,000
8-Jan-20	Purchases account Accounts Payable <i>Being goods purchased on credit</i>	400,000	400,000
12-Jan-20	Cash account Sales account <i>Being goods sold for cash</i>	150,000	150,000
16-Jan-20	Cash account Bank account <i>Being cash withdrawn from bank</i>	200,000	200,000
20-Jan-20	Accounts Receivable Sales account <i>Being goods sold on credit</i>	50,000	50,000
22-Jan-20	Accounts Payable Purchases returns account <i>Being goods returned to supplier</i>	15,000	15,000
23-Jan-20	Accounts Payable Bank account <i>Being cheque issued to pay a creditor</i>	200,000	200,000
24-Jan-20	Wages account Cash account <i>Being wages paid in cash</i>	30,000	30,000
26-Jan-20	Drawings account Bank account <i>Being cash drawn by proprietor</i>	100,000	100,000

27-Jan-20	Purchases account Accounts Payable <i>Being goods purchased on credit</i>	150,000	150,000
28-Jan-20	Sales returns account Accounts Receivable <i>Being goods returned by a customer</i>	5,000	5,000
29-Jan-20	Cash account Rent income account <i>Being rent received in cash</i>	50,000	50,000
30-Jan-20	Bank account Accounts Receivable <i>Being a cheque received in respect of receivables</i>	20,000	20,000

The second stage is the posting of entries to general ledgers.

**Dr** **Cr**  
**Bank account (1)**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
1/1/2020	Capital	2	2,000,000	16/1/2020	Cash	6	200,000
30/1/2020	Accounts receivable	8	20,000	23/1/2020	Accounts payable	4	200,000
				26/1/2020	Drawings	11	100,000

**Dr** **Cr**  
**Capital account (2)**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
				1/1/2020	Bank	1	2,000,000

**Dr** **Cr**  
**Machinery account (3)**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
4/1/2020	Accounts payable	4	200,000				

**Dr** **Accounts Payable (4)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
23/1/2020	Bank	1	200,000	4/1/2020	Machinery	3	200,000
22/1/2020	Purchases	9	15,000	8/1/2020	Purchases	5	400,000
	returns			27/1/2020	Purchases	5	150,000

**Dr** **Purchases account (5)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
8/1/2020	Accounts payables	4	400,000				
27/1/2020	Accounts payables	4	150,000				

**Dr** **Cash account (6)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
12/1/2020	Sales	7	150,000	24/1/2020	Wages	10	30,000
16/1/2020	Bank	1	200,000				
29/1/2020	Rent received	13	50,000				

**Dr** **Sales account (7)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
				12/1/2020	Cash	6	150,000
				20/1/2020	Accounts Receivable	8	50,000

**Dr** **Accounts receivable (8)** **Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
20/1/2020	Sales	7	50,000	28/1/2020	Sales returns	12	5,000
				30/1/2020	Bank	1	20,000

**Dr Purchases returns account (9) Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
				22/1/2020	Accounts Payable	4	15,000

**Dr Wages account (10) Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
24/1/2020	Cash	6	30,000				

**Dr Drawings account (11) Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
26/1/2020	Bank	1	100,000				

**Dr Sales returns account (12) Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
28/1/2020	Accounts Receivable	8	5,000				

**Dr Rent received account (13) Cr**

Date	Particulars	Folio	Amount	Date	Particulars	Folio	Amount
				29/1/2020	Cash	6	50,000



**Exercise 4.2**

Enter the following transactions in the general journal and post entries in the books of accounts of Mkwaju.

- 2021 October 1 Started a business with TZS 200,000 in the bank.
- 3 Bought goods on credit from Juma for TZS 15,300 and from Ndayi for TZS 41,620.
- 4 Sold goods for cash TZS 19,100.

- 6 Banked TZS 10,000.
- 8 Sold goods on credit to Mang'ara TZS 13,740.
- 9 Mkwaju withdrew TZS 10,000 for personal use.
- 10 Sold goods on credit to Ramadhani for TZS 4,800.
- 12 Mangara returned goods worth TZS 6,500.
- 15 Returned to Juma goods worth TZS 5,000.
- 18 Bought office furniture from Samwi for TZS 50,000 on credit.
- 20 Sold goods by cash for TZS 20,000.
- 29 Mkwaju injected an additional TZS 50,000 into the business in cash.
- 30 Paid Juma the balance due.
- 30 Mangara paid the amount due in cash.
- 30 Banked all cash balances remaining with only TZS 2,000 cash.

### Balancing of accounts

The ledger postings are not made for their own sake. They are made for the purpose of obtaining balances that are needed for different uses in the business. A balance of an account is the difference between the total of the entries in the debit side of the account and the total of credit entries in an account at any particular date or time. Balancing of an account involves calculating the balance and recording it on the appropriate side of the account. The balances of accounts in the subsidiary ledger are used for the management of payables and receivables. The balances of accounts in the general ledger at the end of a particular accounting period are used for the preparation of financial statements.

To balance an account, we need to undertake the following steps:

- (a) Calculate the total amounts of money on the debit side and credit side of the account.
- (b) Calculate the difference between the totals obtained in step (a) above. The difference is actually the account balance or balancing figure.
- (c) Insert the difference obtained in step (b) above on the side that had a lower amount of total in step (a) above. The balance is labelled 'balance carried forward' or in short 'balance c/f', to indicate that the balance is carried forward to the next date/ month/ year. At the beginning of the next period, the balance will be labelled 'balance brought forward or in short 'balance b/f'. Another way to label the balances is to use the traditional 'balance carried down' or in short 'balance c/d' and 'balance brought down, or in short 'balance b/d'.

- (d) Write the totals of each side which should now be the same for both sides because of the 'balancing figure' or simply the balance inserted in step (c) above.



### Activity 4.2

After completing the posting of entries to the ledger, it is important that each ledger account must be balanced. You have attended a class on balancing of accounts and your teacher, Ms. Mwendamseke has assigned you a task to explain the account balancing process and its importance to two of your classmates who had emergencies and were not able to attend the class.

Write a brief note that you will use in making the clarification to them.

### A worked out example 4.5

You are given the following transactions of Jamal for the month of January 2020. Record the transaction in the general journal and post the entries to respective accounts. In your answer clearly show the balance at the end of the month and the opening balance for the month of February 2020.

- 1 Started a business by depositing TZS 13,500,000 cash in the bank account.
- 2 Bought a business building from D. Kamara for TZS 7,500,000, paying TZS 5,000,000 by cheque and promising to pay the balance as early as possible next month.
- 4 Purchased office furniture worth TZS 250,000 by cheque.
- 5 Purchased goods on credit from Madina TZS 500,000.
- 8 Jamal injected more capital in the business in terms of cheque TZS 600,000.
- 10 Sold goods worth TZS 120,000 to Mahinda on credit.
- 11 Purchased goods from ABC LTD worth TZS 240,000 on credit.
- 12 Sold goods worth TZS 130,000 by cash.
- 14 Returned goods to Madina worth TZS 150,000 because they were faulty.
- 15 Mahinda returned goods worth TZS 10,000.
- 18 Paid Madina TZS 350,000 by cheque.
- 20 Received cash from Mahinda TZS 80,000.
- 24 Paid wages by cash TZS 50,000.
- 26 Jamal drew TZS 200,000 from the business account for private use.
- 28 Received rent in cash TZS 50,000.
- 31 Paid ABC LTD TZS 210,000 by cheque.



**Solution**

The first step is to journalise the entries in the general journal or journal proper.

**Journal entries**

<b>Date</b>	<b>Details</b>	<b>Dr (TZS)</b>	<b>Cr (TZS)</b>
1-Jan-20	Bank account Capital account <i>Being capital deposited in the bank</i>	13,500,000	13,500,000
2-Jan-20	Building account Bank account Accounts payable <i>Being building acquired for 7,500,000 with 5,000,000 cheque being issued</i>	7,500,000	5,000,000 2,500,000
4-Jan-20	Furniture account Bank account <i>Being cheque issued to buy furniture</i>	250,000	250,000
5-Jan-20	Purchases account Accounts payables <i>Being goods purchases on credit</i>	500,000	500,000
8-Jan-20	Bank account Capital account <i>Being capital introduced by cheque</i>	600,000	600,000
10-Jan-20	Accounts receivable Sales account <i>Being goods sold on credit</i>	120,000	120,000
11-Jan-20	Purchases account Accounts payable <i>Being goods purchased on credit</i>	240,000	240,000
12-Jan-20	Cash account Sales account <i>Being goods sold by cash</i>	130,000	130,000
14-Jan-20	Accounts payable Purchases returns account <i>Being goods returned to suppliers</i>	150,000	150,000
15-Jan-20	Sales returns account Accounts receivable <i>Being goods returned by customers</i>	10,000	10,000

18-Jan-20	Accounts payable account Bank account <i>Being cheque issued to pay creditors</i>	350,000	350,000
20-Jan-20	Cash account Accounts receivable <i>Being receivables collected in cash</i>	80,000	80,000
24-Jan-20	Wages account Cash account <i>Being wages paid in cash</i>	50,000	50,000
26-Jan-20	Drawings account Cash account <i>Being cash withdrawn for personal use</i>	200,000	200,000
28-Jan-20	Cash account Rent income account <i>Being rent income received in cash</i>	50,000	50,000
31-Jan-20	Accounts payable Bank account <i>Being cheque issued to pay creditors</i>	210,000	210,000

### Ledger posting and balancing of accounts

The second stage is to post the entries to respective accounts and balance them.

Dr				Bank account (1)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount	Date	Details	Folio	Amount
1/1/2020	Capital	2	13,500,000	2/1/2020	Building	3	5,000,000				
8/1/2020	Capital	2	600,000	4/1/2020	Furniture	5	250,000				
				18/1/2020	Accounts payable	4	350,000				
				26/1/2020	Drawings	13	200,000				
				31/1/2020	Accounts payable	4	210,000				
				31/1/2020	Balance c/d		8,090,000				
			<u>14,100,000</u>				<u>14,100,000</u>				
1/2/2020	Balance b/d		8,090,000								

Dr Capital account (2)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount
31/1/2020	Balance b/d		<u>14,100,000</u>	1/1/2020	Bank	1	13,500,000
				1/8/2020	Bank account	1	600,000
			<u>14,100,000</u>				<u>14,100,000</u>
				1/2/2020	Balance b/d		14,100,000

Dr Building account (3)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount
2/1/2020	Bank	1	5,000,000	31/1/2020	Balance c/d		<u>7,500,000</u>
2/1/2020	Accounts payable	4	2,500,000				
			<u>7,500,000</u>				<u>7,500,000</u>
1/2/2020	Balance b/d		7,500,000				

Dr Accounts payable (4)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount
14/1/2020	Purchase	10	150,000	2/1/2020	Building	3	2,500,000
	Returns						
18/1/2020	Bank	1	350,000	5/1/2020	Purchases	6	500,000
31/1/2020	Bank	1	210,000	11/1/2020	Purchases	6	<u>240,000</u>
31/1/2020	Balance c/d		<u>2,530,000</u>				
			<u>3,240,000</u>				<u>3,240,000</u>
				1/2/2020	Balance b/d		2,530,000

Dr Furniture account (5)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount
4/1/2020	Bank	1	<u>250,000</u>	31/1/2020	Balance c/d		<u>250,000</u>
1/2/2020	Balance b/d		250,000				

Dr Purchases account (6)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount
5/1/2020	Accounts payable	4	500,000	31/1/2020	Balance c/d		<u>740,000</u>
11/1/2020	Accounts payable	4	240,000				
			<u>740,000</u>				<u>740,000</u>
1/2/2020	Balance b/d		740,000				

Dr Accounts Receivables (7)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount
10/1/2020	Sales	8	<u>120,000</u>	15/1/2020	Sales returns	11	10,000
				20/1/2020	Cash	9	80,000
				31/1/2020	Balance c/d		<u>30,000</u>
			<u>120,000</u>				<u>120,000</u>
1/2/2020	Balance b/d		30,000				

Dr Sales account (8)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount
31/1/2020	Balance c/d		<u>250,000</u>	10/1/2020	Accounts receivable	7	120,000
				12/1/2020	Cash	9	130,000
			<u>250,000</u>				<u>250,000</u>
				1/2/2020	Balance b/d		250,000

Dr Cash account (9)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount
12/1/2020	Sales	8	130,000	24/1/2020	Wages	12	50,000
20/1/2020	Accounts Receivable	7	80,000	31/1/2020	Balance c/d		<u>210,000</u>
28/1/2020	Rent received	14	50,000				
			<u>260,000</u>				<u>260,000</u>
1/2/2020	Balance b/d		210,000				

**Dr Purchases returns account (10) Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
31/1/2020	Balance c/d		<u>150,000</u>	14/1/2020	Accounts payable	4	<u>150,000</u>
				1/2/2020	Balance b/d		150,000

**Dr Sales returns account (11) Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
15/1/2020	Accounts Receivable	7	<u>10,000</u>	31/1/2020	Balance c/d		<u>10,000</u>
1/2/2020	Balance b/d		10,000				

**Dr Wages account (12) Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
24/1/2020	Cash	9	<u>50,000</u>	31/1/2020	Balance c/d		<u>50,000</u>
1/2/2020	Balance b/d		50,000				

**Dr Drawings account (13) Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
26/1/2020	Bank	1	<u>200,000</u>	31/1/2020	Balance c/d		<u>200,000</u>
1/2/2020	Balance b/d		200,000				

**Dr Rent received account (14) Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
31/1/2020	Balance c/d		<u>50,000</u>	28/1/2020	Cash	9	<u>50,000</u>
				1/2/2020	Balance b/d		50,000

### Concept of normal balances

The accounts balancing process has different results. Each of the results has its implication on the balance of the account being balanced. The implications will decide whether the account has a debit balance or a credit balance. To understand this concept, think of a weighing scale used in shops. The weighing scale has two sides, namely the reference side and the measurement side. When the shopkeeper wants to measure, say, one kilogram (1kg) of rice, he or she will put a 1kg mass on the reference side of the scale.

Thereafter, she will start adding rice on the measurement side, that is, on the tray side. As long as the weight of rice is less than 1kg, the balance will always be on the reference side. Thus, more rice would need to be added until the two sides balance. On the other hand, if too much rice is put (more than 1kg), the balance will be on the measurement side (with the tray). The shopkeeper will have to reduce the rice up to a stage where the two sides balance. To summarise the three possible outcomes and implications on the balance of the accounts, the following table is used:

### A summary of balances

Results	Account balance
(a) Debit entries total exceeds the credit entries total.	Debit balance
(b) Credit entries total exceeds the debit entries total.	Credit balance
(c) Debit entries total equals the credit entries total.	NIL balance

Accounts for different elements of the accounting equation have normal balances which are derived from the debit and credit rules. Accounts for those elements that are increased by debit entries are expected to have a debit balance as their normal balances. Similarly, accounts for those elements that are increased by credit entries are expected to have a credit balance as their normal balances. We can summarise the normal balances by extending the table that we used to summarise the rules of debit and credit in Chapter Two. We will now have a column for normal balances as follows:

A summary of double entry rules and normal balances:

ELEMENT	INCREASES	DECREASES	NORMAL BALANCE
Assets	Debit	Credit	Debit
Liabilities	Credit	Debit	Credit
Capital (Owner's Equity)	Credit	Debit	Credit
Revenue (Gain)	Credit	Debit	Credit
Expenses	Debit	Credit	Debit

This concept of normal balances is important when one is given a list of balances and is required to summarise them into a trial balance or prepare financial statements. However, it must be made clear that there are some cases where accounts will have (at least temporarily) balances that are not obeying their normal balances.



### Activity 4.3

Show the effect and normal balances of the following accounts by writing correct action.

	Name of Account	Increase	Decrease	Normal balance
(i)	Motor van			
(ii)	Inventory			
(iii)	Loan from Bank			
(iv)	Account payable			
(v)	Capital			
(vi)	Drawings			
(vii)	Sales			
(viii)	Commission received			
(ix)	Purchases			
(x)	Carriage outwards			



### Revision Exercise 4

1. Mkomwa started a business on 1 May 2020 with a capital of TZS 2,000,000 in cash.

		TZS
May 2	Bought goods by cash	1,000,000
3	Bought furniture by cheque	200,000
4	Sold goods by cash	500,000
5	Paid advertising charges by cash	50,000
8	Cash sales	1,200,000
10	Bought goods by cash	500,000
15	Paid rent by cash	100,000
18	Purchased goods by cash	80,000
20	Paid wages by cheque	40,000
25	Sold goods in cash	30,000

#### Required:

Record the above transactions in the general journal. Post the entries to the ledger, and balance the accounts at the end of the month, and carry down the balances.

2. Sambo started a business on 1 June 2020 with a capital in cash TZS 3,000,000

		TZS
June 3	Bought goods by cash	2,200,000
4	Sold goods by cash	2,700,000
5	Paid carriage by cheque	85,000
10	Cash sales	1,200,000
15	Bought goods by cash	2,500,000
18	Paid rent by cash	120,000
20	Paid for advertising in cash	750,000
22	Sold goods in cash	1,500,000
25	Cash sales	2,000,000
26	Paid wages by cheque	60,000
27	Purchased goods by cash	50,000
28	Sold goods in cash	35,000

#### Required:

Record the above transactions in the general journal; post the entries to the ledger, and balance the accounts at the end of the month, finally carry down the balances.



3. You are given the following transactions of Kulindajana.

		TZS
2020 January 1	started a business with a capital in cash	100,000
2	purchased goods by cash	60,000
2	paid carriage by cash	10,000
10	sold goods by cash	80,000
12	received cash from Eddy	40,000
15	paid electricity bill by cash	10,000
18	cash purchases	40,000
20	paid cash to Shamira	60,000
26	cash drawing	15,000
30	bought a calculator by cash	20,000

**Required:**

Record the transactions above in the general journal; post the entries to the ledger; balance the accounts at the end of the month, and carry down the balances.

4. Indicate whether the following accounts are nominal, real, or personal accounts.

No.	Name of Account	Classification
1	Premises	
2	Discount on sales	
3	Mashaka	
4	Yanga Sports club	
5	Insurance	
6	Stock	
7	Commission received	
8	Accounts receivable	
9	Motor vehicles	
10	Wages	
11	Machinery	
12	Carriage	
13	Equipment	
14	Returns inward	
15	Msomi	

5. Arthur and Alpha Co. started a business on 1 February 2021 with a capital in cash of TZS 1,500,000 and undertook the following transactions during the month.

	TZS
February 2 Bought new shelves for shop by cash	200,000
4 Bought goods on credit from N. Swebe	700,000
5 Bought more goods on credit from Jordan	500,000
10 Sold goods for cash	300,000
15 Sold goods on credit to Karafuu Co. LTD	500,000
16 Paid N. Swebe	400,000
19 Paid sundry expenses by cash	50,000
21 Paid wages by cash	100,000

**Required:**

Record the above transactions in the general journal; post the entries to the ledger; balance the accounts at the end of the month, and carry down the balances.

# Chapter Five ►

## Trial balance

### Introduction

*The total of all debit entries made in the general ledger accounts for a particular period will be equal to the total of all credit entries made in the general ledger accounts during the same period. In this chapter, you will learn the concept of a trial balance and preparation of a trial balance. The competencies developed in this chapter will enable you to prepare a balanced trial balance from a given list of general ledger balances.*

### The concept of a Trial balance

This section presents the meaning of a Trial balance, the advantages and its limitations.

### The meaning of a Trial balance

A trial balance can be defined as a list of balances extracted from general ledger accounts at a particular date. In simple words, a trial balance is a snapshot or a picture of ledger accounts balances at a specific date. The trial balance is prepared using debit and credit balances extracted from ledger accounts. We learnt in Chapter Two that the entries in general ledger accounts are posted following the double entry system of Book-Keeping which requires every transaction to be recorded twice. This means that at any

time, the trial balance should balance. In other words, if the posting of the entry in the ledger accounts is done correctly, the total of debit balances and the total of credit balances must be equal.

### Advantages of a Trial balance

A trial balance has the following advantages to an enterprise:

*Provides a summary of balances used in the preparation of financial statements*

**Financial statements** are financial reports produced at the end of the accounting period. Examples of a financial statements are an income statement and a statement of financial position.

Debit and credit balances extracted from general ledgers are listed on the trial balance. Then these balances are used as inputs in the preparation of **financial statements**. In simple terms, balances are extracted from ledgers to a trial balance, then from a trial balance to financial statements. One does not need to go back to each general ledger account to find balances for the purpose of preparing financial statements.

### *Helps to detect errors that could have occurred in the posting process*

The trial balance is prepared using debit and credit balances extracted from general ledger accounts. Since the entries in the general ledger accounts are posted following the double entry principle which requires every transaction to be recorded twice, the trial balance should balance at any time. Therefore, if the trial balance does not balance, it means that errors have been made in the posting process. In view of this, the trial balance is used to detect errors made during the posting process.

### *Checks the correctness of double entries made to the accounts*

If entries made to ledger accounts were wrongly done, the trial balance will not balance. In this regard, the trial balance is used to check the correctness of the double entries made to the accounts.

### *Checks whether computations of the ledger accounts balances were performed correctly*

Double entries might be done properly but mistakes can occur when computations regarding the figures posted are done. Mistakes in the calculation will result into incorrect balances extracted from the ledger accounts. This will prevent the trial balance from balancing. Therefore, the trial balance checks whether computations (calculations) of the figures on the trial balance were performed correctly.

### *Helps an enterprise to keep its records systematically*

The trial balance is a summary of debit and credit balances extracted from general ledgers. In the trial balance, balances from general ledger accounts are listed systematically.

## **Limitations of a Trial balance**

Even though a trial balance is important to the entity, it also has its limitations. The main limitation of the trial balance is that it cannot detect all errors found in ledger accounts. This means that the agreement of the totals of debit and credit balance are not enough to conclude that there was no error made when posting the transactions to

general ledger accounts. This is because some errors may still exist even though the totals of the credit and debit balances agree. For example, a wrong amount is posted for a transaction such that both debit and credit entries are posted using wrong amount, or a posting is done to a wrong account. In such cases, the trial balance would still agree while there are errors in the posting process.

Additionally, the trial balance does not:

- (i) Prove that all transactions have been recorded,
- (ii) Find the missing entry from the journals or in the ledger,
- (iii) Protect the repetition of postings,
- (iv) Prove that the ledger is correct,
- (v) Protect off-setting errors, and
- (vi) Protect errors of commission as well as errors of omission.

In short, a trial balance does not guarantee you that recording of entries will be error-free.



### Activity 5.1

Mr Hatujuani is a businessman who does not appreciate the preparation of trial balances. He believes that once ledger balances are established, he can go straight to the preparation of financial statements.

You are required to write a brief note explaining to him the importance of a trial balance for his business.

## Preparation of a Trial balance

A trial balance is prepared from debit and credit balances extracted from general ledger accounts. When preparing the trial balance, two basic steps must be followed:

**The first step** involves identifying the debit and credit balances in the general ledger. Performing this step depends on the data available. There are cases where a list of general ledger balances is given, and there are cases where one is given transactions and has to process them all the way (journalising, posting to general ledger, balancing the accounts and extracting the trial balance). We will have a look at both situations using examples.

**The second step** in preparing the trial balance is the actual listing of the balances in the trial balance. This is usually done by listing the debit balances on the debit side of the trial balance and the credit balances on the credit side of the trial balance.

## The format of the trial balance

**Name of a business owner or a proprietor**

**Trial balance as at.....**

S/N	Name of account	Debit (TZS)	Credit (TZS)
1			
2			
:			

### Explanation of a Trial balance

At the top of a trial balance, we write a name of the business owner or a name of the enterprise preparing it. This indicates to whom that trial balance belongs. Also, at the top below the name of the business owner, the word, “A trial balance as at (date, month, and year)” must be shown. This is important since it shows the actual date at which balances used were extracted from the general ledger. This is because a change in date by even a single day could bring a lot of changes in the trial balance since the posting of transactions to the general ledger is a continuous exercise.

### Important columns of the Trial balance are:

**Details:** It is the column in which we list or record names of ledger accounts from which the balances have been extracted.

**Debit balances:** It is the column in which we list or record the debit balances extracted from general ledger accounts.

**Credit balances:** It is the column in which we list or record the credit balances extracted from general ledger accounts.

## A worked out example 5.1

**Preparing a Trial balance from a given list of balances**

You are given the following list of balances extracted from a general ledger of Asam Traders at 30/11/2020, from which you are required to extract a trial balance.

**Balances from Asam Traders' General ledger**

Details	TZS
Sales	172,720,000
Purchases	83,896,000
Rent and rates expenses	3,296,000
Lighting and heating expenses	412,800
Salaries and wages	40,720,000
Insurance expenses	1,608,000
Building	67,360,000
Furniture	864,000
Accounts receivable (Debtors)	24,672,000
Electricity expense	326,400
Accounts payable (Creditors)	11,984,000
Balance at bank	11,160,000
Equipment	20,000,000
Motor van	11,680,000
Motor running expenses	3,278,400
Capital	83,400,000
Stock at 1 December 2020	1,169,600
Stock at 30 November 2021	978,550
Discount received	2,339,200

In this case, the first step is to identify which of the balances are debit and credit balances. To do this, we make use of the concept of normal balances that we discussed in Chapter Four. All that is needed so as to identify for each balance the element of accounting equation affected and label the balance as a debit or credit balance applying the normal balance concept.

This can be summarised as follows:

Name of account	Element	Normal balance
Sales	Revenue	Credit
Purchases	Expense	Debit
Rent and rates expenses	Expense	Debit
Lighting and heating expenses	Expense	Debit
Salaries and wages	Expense	Debit
Insurance expenses	Expense	Debit
Building	Asset	Debit
Furniture	Asset	Debit
Accounts receivable (Debtors)	Asset	Debit
Electricity expense	Expense	Debit
Accounts payable (Creditors)	Liability	Credit
Balance at bank	Asset	Debit
Equipment	Asset	Debit
Motor van	Asset	Debit
Motor running expenses	Expense	Debit
Capital	Capital	Credit
Stock at 1 December 2020	Asset	Debit
Stock at 30 November 2021	Asset – not part of the trial balance	Debit
Discount Received	Revenue	Credit



Following this, the trial balance can be done by obeying the principle that identifies debit and credit balances as follows:

**Asam Traders'**  
**Trial balance as at 30 November 2021**

Names of account	Debit (TZS)	Credit (TZS)
Sales		172,720,000
Purchases	83,896,000	
Rent and rates expenses	3,296,000	
Lighting and heating expenses	412,800	
Salaries and wages	40,720,000	
Insurance expenses	1,608,000	
Building	67,360,000	
Furniture	864,000	
Accounts receivable (Debtors)	24,672,000	
Electricity expense	326,400	
Accounts payable (Creditors)		11,984,000
Balance at bank	11,160,000	
Equipment	20,000,000	
Motor van	11,680,000	
Motor running expenses	3,278,400	
Capital		83,400,000
Stock at 1 January 2020	1,169,600	
Discount Received		2,339,200
<b>Totals</b>	<b>270,443,200</b>	<b>270,443,200</b>



**Exercise 5.1**

1. Why is stock at 30 November 2021 not part of the trial balance?
2. What are the other names for debtors and creditors?
3. What is meant by drawings? Explain why drawings have a normal balance of debit?

**A worked out example 5.2****Preparing a Trial balance from a given list of transactions**

Record the following transactions in the general journal, ledger accounts of Jamal for January 2020, balance off the ledger accounts, and extract a trial balance as at 31/1/2020.

- 1 Started a business by depositing cash in the bank account TZS 13,500,000.
- 2 Purchased a business building from Kamara for TZS 7,500,000, paying TZS 5,000,000 by cheque and promising to pay the balance as early as possible next month.
- 4 Purchased office furniture by cheque from John TZS 250,000.
- 5 Purchased goods on credit from Madina TZS 500,000.
- 8 Jamal injected in the business TZS 600,000 by cheque.
- 10 Sold goods to Mahinda on credit worth TZS 120,000.
- 11 Purchased goods on credit from ABC LTD worth TZS 240,000.
- 12 Sold goods by cash worth TZS 130,000.
- 14 Returned goods to Madina worth TZS 150,000 because they were faulty.
- 15 Mahinda returned goods worth TZS 10,000.
- 18 Paid Madina TZS 350,000 by cheque.
- 20 Received cash from Mahinda worth TZS 80,000.
- 24 Paid wages by cash TZS 50,000.
- 26 Jamal drew TZS 200,000 from the business account for private use.
- 28 Received TZS 50,000 cash for rent.
- 31 Paid ABC LTD TZS 210,000 by cheque.

In this kind of a situation, the first step will be a fairly long one, involving the application of the double entry principle to make entries in the general journal, post the entries to the general ledger, and balance the ledger accounts. The second step will involve extracting the debit and credit balances from general ledger accounts for the trial balance. We can see all these in the solution that follows.

## Solution

## Journal entries

Date	Details	Dr	Cr
1-Jan-20	Bank account Capital account <i>Being capital deposited in the bank by the owner</i>	13,500,000	13,500,000
2-Jan-20	Building account Bank account Accounts Payable <i>Being for a building acquired for TZS 7,500,000 with TZS 5,000,000 cheque issued</i>	7,500,000	5,000,000 2,500,000
4-Jan-20	Furniture account Bank account <i>Being a cheque issued to buy furniture</i>	250,000	250,000
5-Jan-20	Purchases account Accounts Payable * <i>Being goods purchased on credit</i>	500,000	500,000
8-Jan-20	Bank account Capital account <i>Being additional capital paid by cheque</i>	600,000	600,000
10-Jan-20	Accounts Receivable* Sales account <i>Being goods sold on credit</i>	120,000	120,000
11-Jan-20	Purchases account Accounts Payable <i>Being goods purchased on credit</i>	240,000	240,000
12-Jan-20	Cash account Sales account <i>Being goods sold in cash</i>	130,000	130,000

14-Jan-20	Accounts Payable	150,000	
	Purchases returns account		150,000
	<i>Being goods returned to suppliers</i>		
15-Jan-20	Sales returns account	10,000	
	Accounts Receivable		10,000
	<i>Being goods returned by customers</i>		
18-Jan-20	Accounts Payable	350,000	
	Bank account		350,000
	<i>Being cheque issued to pay creditors</i>		
20-Jan-20	Cash account	80,000	
	Accounts Receivable		80,000
	<i>Being receivables collected in cash</i>		
24-Jan-20	Wages account	50,000	
	Cash account		50,000
	<i>Being wages paid in cash</i>		
26-Jan-20	Drawings account	200,000	
	Bank		200,000
	<i>Being cash withdrawn for personal use</i>		
28-Jan-20	Cash account	50,000	
	Rent income account		50,000
	<i>Being rent income received in cash</i>		
31-Jan-20	Accounts Payable	210,000	
	Bank account		210,000
	<i>Being a cheque issued to pay creditors</i>		

\* **Note:** at this stage, you are not recording the account of an individual person, but collective accounts are used, which are known as accounts payable and receivable in order to simplify the posting of accounts balances to the trial balance.

## Posting to the general ledger

Dr				Cr			
Bank account (1)							
Date	Details	Folio	Amount	Date	Details	Folio	Amount
1/1/2020	Capital	2	13,500,000	2/1/2020	Building	3	5,000,000
8/1/2020	Capital	2	600,000	4/1/2020	Furniture	5	250,000
				18/1/2020	Accounts Payable	4	350,000
				26/1/2020	Drawings	13	200,000
				31/1/2020	Accounts Payable	4	210,000
				31/1/2020	Balance c/d		8,090,000
			<u>14,100,000</u>				<u>14,100,000</u>
1/2/2020	Balance b/d		8,090,000				

Dr				Cr			
Capital account (2)							
Date	Details	Folio	Amount	Date	Details	Folio	Amount
31/1/2020	Balance c/d		<u>14,100,000</u>	1/1/2020	Bank	1	13,500,000
				1/8/2020	Bank	1	600,000
			<u>14,100,000</u>				<u>14,100,000</u>
				1/2/2020	Balance b/d		14,100,000

Dr				Cr			
Building account (3)							
Date	Details	Folio	Amount	Date	Details	Folio	Amount
2/1/2020	Bank	1	5,000,000	31/1/2020	Balance c/d		<u>7,500,000</u>
2/1/2020	Accounts Payable	4	2,500,000				
			<u>7,500,000</u>				<u>7,500,000</u>
1/2/2020	Balance b/d		7,500,000				

Dr				Accounts Payable (4)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount				
14/1/2020	Purchase	10	150,000	2/1/2020	Building	3	2,500,000				
	Returns										
18/1/2020	Bank	1	350,000	5/1/2020	Purchases	6	500,000				
31/1/2020	Bank	1	210,000	11/1/2020	Purchases	6	<u>240,000</u>				
31/1/2020	Balance c/d		2,530,000								
			<u>3,240,000</u>								
				1/2/2020	Balance b/d		2,530,000				

Dr				Furniture account (5)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount				
4/1/2020	Bank	1	<u>250,000</u>	31/1/2020	Balance c/d		<u>250,000</u>				
1/2/2020	Balance b/d		250,000								

Dr				Purchases account (6)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount				
5/1/2020	Accounts Payable	4	500,000	31/1/2020	Balance c/d		<u>740,000</u>				
11/1/2020	Accounts Payable	4	240,000								
			<u>740,000</u>								
1/2/2020	Balance b/d		740,000								

Dr				Accounts Receivables (7)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount				
10/1/2020	Sales	8	<u>120,000</u>	15/1/2020	Sales returns	11	10,000				
				20/1/2020	Cash	9	80,000				
				31/1/2020	Balance c/d		30,000				
			<u>120,000</u>				<u>120,000</u>				
1/2/2020	Balance b/d		30,000								

Dr				Sales account (8)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount				
31/1/2020	Balance c/d		<u>250,000</u>	10/1/2020	Accounts Receivable	7	120,000				
				12/1/2020	Cash	9	130,000				
			<u>250,000</u>				<u>250,000</u>				
				1/2/2020	Balance b/d		250,000				

Dr				Cash account (9)				Cr			
Date	Details	Folio	Amount	Date	Details	Folio	Amount				
12/1/2020	Sales	8	130,000	24/1/2020	Wages	12	50,000				
20/1/2020	Accounts Receivable	7	80,000	31/1/2020	Balance c/d		<u>210,000</u>				
28/1/2020	Rent received	14	50,000								
			<u>260,000</u>				<u>260,000</u>				
1/2/2020	Balance b/d		210,000								

**Dr** **Purchases returns account (10)** **Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
31/1/2020	Balance c/d		<u>150,000</u>	14/1/2020	Accounts Payable	4	<u>150,000</u>
				1/2/2020	Balance b/d		150,000

**Dr** **Sales returns account (11)** **Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
15/1/2020	Accounts Receivable	7	<u>10,000</u>	31/1/2020	Balance c/d		<u>10,000</u>
1/2/2020	Balance b/d		10,000				

**Dr** **Wages account (12)** **Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
24/1/2020	Cash	9	<u>50,000</u>	31/1/2020	Balance c/d		<u>50,000</u>
1/2/2020	Balance b/d		50,000				

**Dr** **Drawings account (13)** **Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
26/1/2020	Bank	1	<u>200,000</u>	31/1/2020	Balance c/d		<u>200,000</u>
1/2/2020	Balance b/d		200,000				

**Dr** **Rent received account (14)** **Cr**

Date	Details	Folio	Amount	Date	Details	Folio	Amount
31/1/2020	Balance c/d		<u>50,000</u>	28/1/2020	Cash	9	<u>50,000</u>
				1/2/2020	Balance b/d		50,000



After posting entries in ledger accounts and balancing off those accounts, the next step is the preparation of the trial balance. The trial balance is prepared using the debit and credit balances extracted from ledger accounts. Therefore, the trial balance is prepared as follows:

**Jamal**

**Trial balance as at 31 January 2020**

S/No	Name of account	Debit (TZS)	Credit (TZS)
1	Bank	8,090,000	
2	Capital		14,100,000
3	Building	7,500,000	
4	Accounts Payable		2,530,000
5	Furniture	250,000	
6	Purchases	740,000	
7	Accounts Receivable	30,000	
8	Sales		250,000
9	Cash	210,000	
10	Purchases returns		150,000
11	Sales returns	10,000	
12	Wages	50,000	
13	Drawings	200,000	
14	Rent received		50,000
<b>Total</b>		<b><u>17,080,000</u></b>	<b><u>17,080,000</u></b>



**Activity 5.2**

A trial balance is used as a tool to check the arithmetical accuracy of recording and posting double entries. Sometimes the balancing of the trial balance does not justify that everything was done correctly. Make a discussion with your colleague and write down possible reasons that may cause the trial balance to agree even if some of the entries posted in the general ledgers are not correct.



**Exercise 5.2**

1. Investigate and explain what causes a capital balance to increase and decrease.
2. What is another name for sales returns?
3. What is another name for purchases returns?
4. Why are sales returns credited to the receivables account?
5. Why are purchases returns debited to the payables account?



## Revision Exercise 5

Enter the transactions in questions 1 - 5 in the general journal, post the entries to the general ledger accounts, balance the accounts at the end of the respective months and extract a trial balance as at the end of the month in each case.

## 1. Chipe's transactions in the month of January 2021

	TZS
2021 January 1 Chipe commenced a business with a capital in cash	5,000,000
2 Purchased goods by cash	2,500,000
2 Bought goods on credit from Shilingi Store	1,500,000
3 Sold goods by cash	2,900,000
5 Purchased goods by cash	2,000,000
7 Paid Shilingi Store amount owing by cash	1,000,000
8 Bought packing material by cash	50,000
10 Paid advertising charges by cash	80,000
15 Sold goods by cash	3,200,000
17 Sold goods on credit to Maliatabu	1,200,000
20 Paid rent in cash	50,000
21 Purchased goods by cash	80,000
22 Paid wages in cash	60,000
25 Received cash from Maliatabu for settlement amount dues	800,000

## 2. Mtuweta commenced a business on 1 of June 2021 with a capital in cash 2,000,000.

	TZS
June 2 Bought goods by cash	1,200,000
3 Bought furniture by cash	200,000
5 Paid transport charges by cash	25,000
6 Cash sales	1,700,000
8 Bought goods by cash	1,500,000
10 Purchased goods by cash	500,000
12 Paid rent by cash	80,000
15 Sold goods by cash	2,100,000
18 Sold goods by cash	300,000
20 Paid carriage in cash	15,000
22 Paid wages in cash	36,000

3. Kazukamwe started a business on 1 June 2021 with a capital in cash of 3,000,000

	<b>TZS</b>
June 2 Bought furniture by cash	100,000
3 Bought goods by cash	2,200,000
4 Sold goods by cash	2,700,000
5 Paid carriage in cash	85,000
10 Cash sales	1,200,000
15 Bought goods by cash	2,500,000
18 Paid rent by cash	120,000
20 Paid for advertising in cash	750,000
22 Sold goods by cash	1,500,000
25 Cash sales	2,000,000
26 Paid wages in cash	60,000
27 Purchased goods by cash	50,000
28 Sold goods by cash	35,000

4. You are given the following transaction of Naomi.

	<b>TZS</b>
2021 January 1 Commenced a business with a capital in cash	100,000
5 Purchased goods by cash	50,000
7 Paid electricity by cash	10,000
8 Bought goods on credit from Zonte	40,000
15 Purchased furniture by cash	20,000
20 Sold goods on credit to Sukununu	50,000
27 Drew cash for his private use	15,000
28 Paid cash to Zonte	25,000
31 Received cash from Sukununu	40,000

5. Amanda commenced a business with a capital in cash 150,000 on 1 March 2021

	<b>TZS</b>
March 2 Bought goods and paid cash	50,000
4 Paid rent in cash	10,000
5 Sold goods on credit to Andunje	60,000
10 Paid salary in cash	5,000
15 Received cash from Andunje	40,000
18 Bought a radio on credit from Abunuwasi	30,000

20	Paid cash to Abunuwasi	20,000
24	Cash purchases	35,000
26	Cash sales to date	60,000
28	Cash drawings	10,000
29	Paid water bill in cash	15,000

6. Mr. Mloka, who is very weak in Book-Keeping, has provided you with the following trial balance which does not balance. You are required to redraft it and make it balance.

**Trial balance as at 30 June 2020**

<b>Name of account</b>	<b>Debit (TZS)</b>	<b>Credit (TZS)</b>
Inventory at start	13,280,000	
Carriage outwards		4,200,000
Carriage inwards	2,460,000	
Returns inwards		3,080,000
Returns outwards	6,820,000	
Purchases	176,860,000	
Sales		329,840,000
Inventory at close		11,560,000
Salaries and wages	27,800,000	
Insurance	1,232,000	
Motor expenses	3,820,000	
Office expenses	2,824,000	
Lighting and heating expenses		5,788,000
General expenses		5,490,000
Buildings		124,500,000
Motor van	26,800,000	
Fixtures and fittings	3,800,000	
Accounts receivable		85,120,000
Accounts payable	69,220,000	
Cash at bank		10,212,000
Drawings	24,000,000	
Capital		115,386,000
<b>Total</b>	<b>358,916,000</b>	<b>695,176,000</b>

7. You are required to prepare a trial balance as at 31 December 2020 from the following balances

	<b>TZS</b>
Capital	126,360,000
Drawings	12,000,000
Cash at bank	5,166,000
Inventory at start	23,680,000
Carriage inwards	2,000,000
Carriage outwards	3,100,000
Sales returns	2,050,000
Purchases returns	3,220,000
Purchases	161,740,000
Sales	248,560,000
Salaries	35,765,000
Rent	3,040,000
Insurance	780,000
Motor expenses	6,640,000
Office expenses	2,160,000
Postage expenses	1,660,000
General expenses	3,140,000
Premises	35,400,000
Motor vehicle	18,000,000
Machinery	8,500,000
Accounts receivable	38,960,000
Accounts payable	17,310,000

# Chapter Six



## Elementary financial statements

### Introduction

*The business owner, other persons and institutions may need to know about the performance of a business by determining its profit or a loss and its financial position. In this chapter, you will learn the concept of financial statements, an income statement, a statement of financial position and how to prepare the two basic financial statements. The competencies developed in this chapter will enable you to prepare both the income statement and the statement of financial position accurately.*

### **The concept of financial statements**

This section presents the meaning, purposes, and common users of financial statements.

### **The meaning and purpose of financial statements**

#### **(a) Meaning of financial statements**

Financial statements are statements that are prepared periodically to present the results of the business for the period. The two basic financial statements are an income statement and a statement of financial position. The income statement, which is also known as a statement of profit or loss, is prepared in order to determine a profit or a loss made by the business in a particular accounting period. On the contrary, the

statement of financial position which is also known as a balance sheet, is prepared in order to determine the financial position of a business by considering the value of assets, liabilities and capital as at certain date.

Some businesses, for example, companies, are required by law to prepare financial statements. For sole proprietors, financial statements may not be legally required but the needs of the owners would be met through the use of financial statements, especially in evaluating performance of the business for the period. There are also other users who would benefit from the financial statements of a business. This is because their understanding of financial and operational affairs of the business can be useful in making informed decisions.

**(b) Purposes of financial statements**

Detailed descriptions on the purposes of preparing financial statements are to:

***Show profitability of the business***

Many businesses are established for the purpose of making profits. Therefore, it is important to measure whether this objective has been achieved. This is because, owners will have an opportunity to evaluate whether the management has met their targets or not. It will also assist owners in making decision on whether to continue with the business or not.

***Show the financial position of the business*****Non-productive assets:**

These are assets existing in the business but not fully utilised to generate revenue. For example, a large office building in excess of the business requirements may represent a non-productive asset.

When a business gets into a difficult financial position, for example, being overburdened by liabilities, it may face the risk of closure due to inability to pay debts. On the one hand, when the business has a large proportion of its assets on **non-productive assets**, this creates a possibility of a failure of the business in the future. On the other hand, a good proportion of productive assets forecasts a bright future for the business.

***Help in assessing the efficiency of business operations***

Efficiency of business operations is useful in ensuring that the business achieves its profit-making objective. Examples of efficiency measures include assets utilisation and turnover of stocks. Assets utilization is usually used to measure how well the company is using its available assets to make money. Alternatively, turnover of stocks is usually used to measure how many times a company has sold and replaced its inventory during a given period. Figures used to calculate ratios for these measures are usually obtained from financial statements. When there is an unsatisfactory level of efficiency, the business can plan ways to improve its performance.

***Facilitate compliance with tax laws***

Amounts of different taxes payable by the business are computed from the figures obtained from financial statements. For example, Value Added Tax (VAT) is calculated as a percentage of a figure of sales that is subject to taxation. Similarly, profit made by a business for a period is used in calculating the income tax to be paid by the business. Both profit and sales figures used in calculating these tax figures can be easily obtained from the business financial statements of a company under consideration.

***Facilitate planning and evaluation***

Planning and evaluation are among the main functions of management. Financial statements are useful in evaluating the performance of a business for the period

through comparing the targets established at the beginning of the year with the actual results that are obtained from the financial statements. Moreover, the performance of the current year can form the basis for setting plans for the next year.

### ***Establish the riskiness of the business***

Different persons dealing with the business, for example, banks, customers, and suppliers will need to be sure about the risk associated with the business. In this context, a risk may be defined as the probability that actual results will differ from the expected results. Traditionally, a risk has been defined in terms of the possibility of danger, loss, injury or other negative outcomes. For example, customers would want to be assured of steady supplies of goods while banks and suppliers would want to be sure of the ability of the business to settle their debts. Since financial statements provide the results of a business performance, they are usually considered as a reliable source of information. The information will help stakeholders to have answers for their questions including the risks associated with the business.

### **Common users of financial statements**

The information presented in the financial statements is useful to different users of financial statements depending on what the information is needed for. The following is a list of common users of financial statements and the reasons for seeking such information.

### **Managers**

Managers are supervisors of enterprises on a daily basis. They are interested in the information presented in the financial statements to know the performance of the business. The financial statements may also be useful for managers in making future plans.

### **Owners of a business**

These are the people who invested their money or other resources into a business with the objectives of making a profit. Therefore, they will be interested in the information presented on the financial statements because it enables them to evaluate their business with reference to the targeted profit.

### **Prospective investors or buyers of the business**

**Investor:** A person (or entity) who puts her money into a business in order to become one of the owners for the purpose of getting a share of the profit generated.

These are people who are interested in committing their money to invest or purchase part or the whole business in order to benefit from the profit generated. Before the prospective investor or buyer purchases a business he/she would want to see its financial statements to evaluate its ability to make profits. This information is very important in making informed decision on whether to invest in the business commenced or not.



### Tax inspectors

Tax officers from tax authorities like the Tanzania Revenue Authority (TRA) and the Zanzibar Revenue Board (ZRB) would want to see the financial statements of an enterprise to ensure proper calculations of the amount of tax to be paid by the enterprise.

### Bankers

Different banks that an entrepreneur may approach for loans and other services would want to know the performance trend of the business in order to make decisions on whether to lend or not. The bank would, for example, want to see the financial statements to assess whether the business will be able to repay the loan that it is applying for.

### Creditors

Creditors are suppliers of goods or services who sell goods or provide services on credit. Creditors are interested in the information presented in the financial statements because they want to assess the ability of debtors to pay for the goods and services supplied on credit when due.

### Debtors

Debtors are enterprises or individuals who purchase goods or services on credit. Debtors do not use much financial statements of their creditors but sometimes they need them (especially cash flow statements) so as to check the capability of these creditors to do regular supply of goods especially when dealing with tender businesses.

### An income statement

An income statement is a statement prepared at the end of accounting period to calculate the profit or loss made. The statement calculates a profit or a loss for the period by comparing (matching) revenue earned during the period and expenses incurred during the same period. It is therefore in the income statement where the matching principle, as highlighted in Chapter One is applied.

### Calculation of profit or loss

The purpose of preparing an income statement is to calculate the amount of profit or loss. Profit or loss for a merchandising business is calculated in two stages. The first stage compares the amount of net sales and cost of goods sold and obtains the gross profit or loss. The second stage compares the gross profit (obtained from first stage) and other incomes with different expenses incurred in operating the business during the period. The result is the profit or loss for the period.

### Terms used in an income statement

Terms used in an income statement are explained as follows:

#### Net sales

The figure of net sales is mainly made by two aspects which are sales and sales returns. The sales figure is the credit balance transferred from the sales account in the general ledger. It is the total of all sales (both credit and cash) made during the period under consideration.

Sales returns are those goods that were previously sold to a customer but were later returned due to different reasons. Therefore, the net sales is calculated by taking sales less the sales returns also known as returns inwards.

### *Net purchases*

The figure for net purchases is obtained after taking into consideration several aspects. The first aspect is the debit balance found in the account of purchases itself. This figure is the total purchases (cash and credit) done in the whole accounting period. The second aspect considered is the carriage inwards costs. These are costs of transferring or transporting the purchased goods from where they were procured to the premises of the enterprise which procured them. In simple terms, the cost of goods purchased is the total of the cost paid to purchase such goods plus the transportation cost of bringing those goods to the enterprise's premises. For example, the supplier sold goods for TZS 100,000 and TZS 10,000 is incurred by the buyer to transport such goods from the supplier's premises to his/her premises. In this case, the cost of purchasing those goods is not only TZS 100,000 but is TZS 110,000 (TZS 100,000 + TZS 10,000).

The last aspect included in the calculation of the net purchases figure is the purchases returns or returns outwards. Purchase returns refer to those goods which were previously purchased by the entity but

were later returned to the supplier due to several reasons. It should be noted that the figure for purchases shows the total amount (credit and cash) of purchases made without deducting those goods which were returned to the supplier. Therefore, to arrive at a net purchase figure, purchases returns must be deducted from the purchases figure. The complete equation of net purchases is stated as net purchases is equal to purchases plus carriage inwards less purchases returns.

### *Opening inventory and closing inventory*

An opening inventory is the inventory of goods held by the entity at the beginning of the accounting period. On the contrary, a closing inventory is the inventory of goods held by the entity at the end of the accounting period. For instance, suppose the accounting period of the enterprise starts on 1 January and ends on 31 December. The opening inventory of such an enterprise would be considered as the inventory held by that enterprise on 1 January while the closing inventory would be considered as the inventory held by that enterprise on 31 December. Similarly, the closing inventory held by that enterprise on 31 December would be the opening inventory of the enterprise in the following year.

### *Cost of goods available for sale*

The figure of the cost of goods available for sale is the sum of the figure of opening inventory and the figure of net purchases.

**Cost of goods sold**

The figure for the cost of goods sold is the difference between the figure of the cost of goods available for sale and closing inventory. In other words, the cost of goods sold is obtained by deducting the cost of closing inventory from the cost of goods available for sale.

**Gross profit**

The figure for gross profit is obtained by deducting the cost of goods sold from the net sales figure. Gross profit is the profit obtained by the enterprises from trading activities only without including other operation expenses.

**Gross Loss**

The figure for gross loss is obtained by deducting net sales from the cost of goods sold. Gross loss is the excess of cost of goods sold over net sales.

**Profit or loss for the period**

Profit or loss can be computed by taking the total revenue minus the total expenses for the period. The excess of total revenue over total expenses is usually termed as a profit. Alternatively, the excess of total expenses over total revenue is termed as a loss.

**Calculation of a gross profit**

A gross profit is the difference between the sales and the cost of goods sold. The figure of the sales is the balance of the sales account in the general ledger at the end of a period. However, it may happen that some of the goods sold during the

period were returned. The figure to be used in the income statement in this case will be that of the net sales, that is, sales less the sales returns. The sales returns figure is obtained from the sales returns account in the general ledger.

As for the figure of the cost of goods sold, the main ingredient is the value of the purchases. In some cases, the figure of net purchases will be used instead. For the same reasons as discussed in the case of sales returns, if there are some goods which were returned to suppliers, there will be a need to deduct them from the purchases figure. In addition to the figure of purchases (net purchases), this figure can be adjusted with the cost incurred by the business to transport the goods to its premises. This cost is also known as carriage inwards. The figure for this cost is the balance of carriage inwards account found in the general ledger.

**Effect of inventory on gross profit calculation**

In the absence of an inventory, the net purchases figure is the cost of goods sold. This would also mean that a gross profit equals to net sales less net purchases. However, many businesses, except those selling highly perishable goods, would have an inventory of goods at the end of the period or beginning of the period or both. To understand the implications of an inventory on the calculation of the cost of goods sold, we will use a basic computational example and apply data in different stages.

**A worked out example 6.1****No inventory situation**

Agatha groceries have the following results for the year 2020

Net sales TZS 54,620,000

Net purchases TZS 29,885,000

Calculation of a gross profit for the period would be:

Gross profit = Net sales – cost of goods sold

Cost of goods sold = Net purchases

Gross Profit = TZS 54,620,000 – TZS 29,885,000  
= TZS 24,735,000

**A worked out example 6.2****Presence of an inventory at the end of the period**

Suppose in the example above, Agatha had an inventory worth TZS 4,683,000 in store at the end of the year.

If there is an inventory at the end, it simply means that not all the goods purchased during the period were sold. The cost of goods sold will therefore be calculated by deducting the figure of the ending inventory from the net purchases figure.

In the case of Agatha, the cost of goods sold will be calculated as follows:

Cost of goods sold = Net purchases – ending inventory  
= TZS 29,885,000 – 4,683,000  
= TZS 25,202,000

It follows that Gross profit = TZS 54,620,000 – TZS 25,202,000  
= TZS 29,418,000

**A worked out example 6.3****Presence of an inventory at the beginning of the period**

Suppose in the example above, Agatha also had an inventory worth TZS 3,246,000 in the store at the beginning of the year. If there is an inventory at the beginning, it means that the cost of goods sold also include the cost of goods that were in store at the beginning of the period. Calculation of the cost of goods sold will therefore include the figure at the opening inventory.

In the case of Agatha, the cost of goods sold would be calculated as follows:

$$\begin{aligned}\text{Cost of goods sold} &= \text{Beginning inventory} + \text{Net purchases} - \text{ending inventory} \\ &= \text{TZS } 3,246,000 + \text{TZS } 29,885,000 - \text{TZS } 4,683,000 \\ &= \text{TZS } 28,448,000\end{aligned}$$

$$\begin{aligned}\text{It follows that, Gross profit} &= \text{TZS } 54,620,000 - \text{TZS } 28,448,000 \\ &= \text{TZS } 26,172,000\end{aligned}$$

It should therefore be possible to follow the income statement format below, and in any case calculate the cost of goods sold and gross profit in different situations.

#### A worked out example 6.4

##### Calculation of net purchases and cost of goods sold

When there is no opening stock, the cost of goods sold is obtained by taking total purchases, less purchases returned and the closing stock.

$$\text{Cost of goods sold} = (\text{Total Purchases} - \text{Purchases Returns}) - \text{Closing stock}$$

For example:

	TZS
Total purchases	10,000,000
Less: Purchases Returns	<u>2,000,000</u>
<b>Net Purchases</b>	8,000,000
Less: Closing stock	<u>3,000,000</u>
<b>Cost of goods sold</b>	<u>5,000,000</u>

**Format of the income statement**

(Name of the sole proprietor, e.g. John)

**An income statement for the year ending.....**

Details	TZS	TZS	TZS
Sales		xxxx	xxxx
Less: Sales returns		____(xx)	
Net sales			
Less: Cost of goods sold:			
Opening inventory		xxxx	
Add: Purchases	xxx		
Carriage inwards	____xxx		
	xxx		
Less: Purchases returns	____(xx)		
Net purchases		____xxxx	
Cost of goods available for sale		xxxx	
Less: Closing inventory		____(xxx)	
Gross profit			____(xxx)
			xxx
Add: other income:			
Commission received		xxx	
Discount received		____xxx	____xxxx
Total income			xxxx
Less: Expenses:			
Wages		(xx)	
Salaries		(xx)	
Rent		(xx)	
Stationeries		(xx)	
General expenses		(xx)	
Lighting expenses		____(xx)	
Total expenses			____(xxx)
Profit or loss for the year			xxx

## A worked out example 6.5

Using a trial balance below, prepare an income statement for Mbelwa Enterprise for the year ending 31/12/2020.

**Mbelwa Enterprise**

**Trial balance as at 31/12/2020**

Details	Debit balances	Credit balances
Capital		100,000,000
Purchases	60,000,000	
Sales		72,000,000
Inventory 1/1/2020	10,000,000	
Telephone expenses	800,000	
General operating expenses	4,000,000	
Wages and salaries	1,600,000	
Furniture	10,000,000	
Accounts receivable	2,000,000	
Insurance	8,000,000	
Cash	75,600,000	
<b>Total</b>	<b>172,000,000</b>	<b>172,000,000</b>

Closing inventory is TZS 15,000,000

**Solution****Mbelwa Enterprise****An income statement for the period ending 31/12/2020**

Details	TZS	TZS
Sales		72,000,000
Less: Cost of goods sold:		
Opening inventory	10,000,000	
Add: purchases	<u>60, 000,000</u>	
Cost of goods available for sale	70, 000,000	
Less: Closing inventory	<u>(15, 000,000)</u>	<u>(55,000,000)</u>
Gross profit		17,000,000
Less: Expenses:		
Telephone bill	(800,000)	
General operating expenses	(4,000,000)	
Wages and salaries	(1,600,000)	
Insurance	<u>(8,000,000)</u>	
Total expenses		<u>(14,400,000)</u>
Profit for the year		2,600,000

**Activity 6.1**

1. Use online sources to search three financial statements of Tanzanian companies such as Tanzania Oxygen Company, Tanga Cement Company, CRDB Bank or any other three companies. Then study the financial statements focusing on sales, net sales, cost of goods sold, and profits. Write short notes explaining the information studied from the financial statements of the companies.
2. Working together with your fellow students, prepare a list showing different persons who might be interested in the information presented in an income statement. Explain why the persons you have identified might be interested in such information.



## A statement of financial position

Unlike the income statement that reports a financial performance (profit or loss) for a period, a statement of financial position shows a financial position of an enterprise at a specific date or particular point in time. The specific date in this case is the end of the accounting period. The statement of a financial position is therefore prepared by enterprises to present its financial position as at the date indicated on that statement.

The statement of financial position of the enterprise shows the relationship between assets, liabilities and capital; and this relationship holds true at any point in time. You will recall that, the basic accounting equation states that assets are equal to liabilities plus capital. The statement of financial position, therefore, aims at showing how this equation stands at the end of the accounting period considering the amount in each of these elements. The statement of financial position is referred to as such because it shows the assets of an enterprise and how such assets have been financed, that is, proportions of liabilities and capital.

## Preparing the statement of financial position

When preparing a statement of a financial position, the value of each category of assets and liabilities are usually taken from the general ledger balances. To make it easy for the readers to understand well the financial position of the company, usually there is an orderly manner used in presenting assets and liabilities, rather than listing them randomly. To understand this, the common methods used to present assets and liabilities are discussed in the following sections.

## Methods of presenting assets and liabilities

**Liquidity:** It is a measure of the ability of a business to meet its financial obligations as they fall due. One of the indicators of liquidity is time spent to convert its assets into cash.

There are two methods that are commonly used to present assets and liabilities in the statement of a financial position. The methods are such that the assets and liabilities are listed according to the length of time taken to pay the debts (in case of liabilities) or, in case of an asset, the length of time it will take for it to be turned into cash. The length of time it takes for an asset to be turned into cash is an indicator of **liquidity**. Cash is considered to be the most liquid asset. This means that assets that take a shorter time to be converted into cash are considered to be more liquid than those that take a longer time.

The first method that is commonly used in presenting the assets and liabilities is to simply list the assets and liabilities in order of liquidity. The second method involves the grouping of assets and liabilities by considering whether they are current or non-current items.

### **Listing in order of liquidity**

This method is mostly used by financial institutions such as banks. Using this approach, the business lists its assets such that they start from the most liquid assets or liabilities to the least liquid ones. Alternatively, the assets and liabilities can be listed starting with the least liquid to the most liquid ones. Under this method, liabilities will be listed starting with those that take the shortest time to be settled to the ones that take the longest time to be settled, and vice versa.

#### **A worked out example 6.6**

Listing of assets and liabilities from the most liquid to the least liquid can be elaborated as follows:

##### ***Assets***

Cash in hand

Cash at bank

Accounts receivable

Inventory

Furniture

Plant and machinery

Building

Land

##### ***Liabilities***

Bank overdraft

Accounts payable

Long term loans

**A worked out example 6.7**

Listing of assets and liabilities from the least liquid to the most liquid ones can be elaborated as follows:

***Assets***

Land

Building

Plant and machinery

Furniture

Inventory

Accounts receivable

Cash at bank

Cash in hand

***Liabilities***

Long term loans

Accounts payable

Bank overdraft

**Grouping assets and liabilities into current and non-current classification**

Classification of assets and liabilities into current and non-current is usually done with reference to the accounting period under consideration. Under this classification, the following groups of assets and liabilities will be considered.

***Current assets***

Current assets include cash and other assets that are held primarily for the purpose of trading. Usually, it is expected that they will be realised in the entity's normal operating cycle, and within the next accounting period. In other words, current assets are either cash (at bank or in hand) or others that would be converted into cash within the next accounting period under the normal operations of the business. Examples of current assets include inventory, accounts receivable, cash at bank and cash in hand.

### **Non-current assets**

Non-current assets are all assets other than current assets, which are expected to be used in supporting business operations for more than one year or accounting period. Examples of non-current assets include land, building, furniture, vehicles, plants and machinery owned by the business.

### **Current liabilities**

Current liabilities are those liabilities that need to be paid within one year or accounting period. For this reason, current liabilities are also known as short term debts. Examples of current liabilities include creditors or accounts payable and bank overdrafts.

### **Non-current liabilities**

Non-current liabilities are all liabilities other than current liabilities that become due (they are supposed to be paid) beyond one year or twelve months. For this reason, non-current liabilities are also known as long term debts. Examples of non-current liabilities include bank loans and a term loan from a friend.



#### **Exercise 6.1**

1. Explain methods of presenting assets and liabilities in a statement of financial position.
2. How do you calculate gross profit in the presence of an inventory at the end of the period?
3. How do you calculate gross profit in the presence of an inventory at the beginning and end of the period?

### The format of a statement of financial position

A format of a statement of financial position of a sole proprietor is presented hereunder.

(Name of the sole proprietor)

#### A statement of financial position as at ....

Details	TZS	TZS	TZS
<b>ASSETS:</b>			
<i>Non-current assets</i>			
Land		XXX	
Building		XXXX	
Plant and machinery		XXX	
Furniture		<u>XXX</u>	XXXX
<i>Current assets</i>			
Inventory:		XXX	
Accounts receivable		XXX	
Cash at bank		XXX	
Cash in hand		<u>XX</u>	<u>XXX</u>
<b>Total assets</b>			<u>XXXX</u>
<b>CAPITAL AND LIABILITIES:</b>			
Capital at start		XXX	
Add: Profit for the year		<u>XX</u>	
		XXX	
Less: Drawings		<u>(XXX)</u>	
Net Capital as at the end			XXXX
<i>Non-current liabilities</i>			
Bank loan	XXX		
Loan from somebody	<u>XXX</u>	XXX	
<i>Current liabilities</i>			
Accounts payable	XXX		
Bank overdraft	<u>XX</u>	<u>XXX</u>	
<b>Total liabilities</b>			XXX
<b>Total capital and liabilities</b>			<u>XXXX</u>

## A worked out example 6.8

You are given the following trial balance extracted from a general ledger of Sauda as on 30 September 2020. You are required to prepare an income statement for the year ending 30 September 2020, and a statement of financial position as on that date.

Details	Debit (TZS)	Credit (TZS)
Inventory: 1 October 2019	27,872,000	
Carriage outwards	1,407,000	
Carriage inwards	2,479,000	
Sales returns	1,031,800	
Purchases returns		2,284,700
Purchases	126,248,100	
Sales		254,868,000
Salaries and wages	41,138,000	
Warehouse rent	2,479,000	
Insurance	908,520	
Motor expenses	1,279,700	
Office expenses	276,040	
Lighting and heating expenses	598,980	
General expenses	164,150	
Premises	61,640,000	
Motor vehicle	8,978,000	
Fixtures and fittings	1,273,000	
Account receivable	28,515,200	
Accounts payable		21,172,000
Cash at bank	3,421,020	
Drawings	14,740,000	
Capital		46,124,810
<b>Totals</b>	<b>324,449,510</b>	<b>324,449,510</b>

Inventory on 30 September 2020 was TZS 30,002,600

## Solution

## Sauda

## Income statement for the year ended 30 September 2020

Details	TZS	TZS	TZS
Sales		254,868,000	
Less Returns		<u>(1,031,800)</u>	
Net Sales			253,836,200
Less: cost of goods sold:			
Opening inventory		27,872,000	
Add: Purchases	126,248,100		
Carriage inwards	<u>2,479,000</u>		
	<b>128,727,100</b>		
Less: Purchases returns	<u>(2,284,700)</u>		
Net Purchases		<u>126,442,400</u>	
Cost of goods available for sale		<b>154,314,400</b>	
Less: closing inventory		<u>(30,002,600)</u>	<u>(124,311,800)</u>
Gross profit			129,524,400
Less: expenses:			
Salaries and wages		(41,138,000)	
Warehouse rent		(2,479,000)	
Carriage out		(1,407,000)	
Insurance		(908,520)	
Motor expenses		(1,279,700)	
Office expenses		(276,040)	
Lighting and heating		(598,980)	
General expenses		<u>(164,150)</u>	
Total expenses			<u>(48,251,390)</u>
<b>Profit for the year</b>			<b>81,273,010</b>

## Sauda

## A statement of financial position on at 30 September 2020

Details	TZS	TZS
<b>ASSETS:</b>		
<b>Non-current assets</b>		
Premises	61,640,000	
Fixtures and fittings	1,273,000	
Motor vehicle	<u>8,978,000</u>	71,891,000
<b>Current assets</b>		
Inventory	30,002,600	
Accounts receivable	28,515,200	
Bank	<u>3,421,020</u>	<u>61,938,820</u>
<b>Total assets</b>		<u><b>133,829,820</b></u>
<b>CAPITAL &amp; LIABILITIES:</b>		
Capital	46,124,810	
Add: Profit for the year	<u>81,273,010</u>	
	127,397,820	
Less: Drawings	<u>(14,740,000)</u>	112,657,820
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable		21,172,000
<b>Total Capital and liabilities</b>		<u><b>133,829,820</b></u>



## Activity 6.2

Collect two copies of financial statements from newspapers and other sources, including websites that you may be able to reach and:

1. Identify the items that you are not able to understand in the financial statements then discuss with your fellow students.
2. Demonstrate how the accounting equation balances.





## Revision Exercise 6

1. From the following particulars extracted from books of a trader, prepare an income statement for the year ending 30 September 2020.

	<b>TZS</b>
Sales	31,000,000
Sales returns	1,275,000
Purchases	24,640,000
Purchases returns	1,750,000
Carriage inwards	215,000
Warehouse wages	2,000,000
Inventory on 1 October 2019	6,500,000
Inventory on 30 September 2020	4,720,000

2. From the following particulars extracted from the books of a trader, prepare an income statement for the year ending 30 September, 2020.

	<b>TZS</b>
Sales	54,250,000
Sales returns	2,800,000
Purchases	49,000,000
Purchases returns	6,475,000
Carriage inwards	4,200,000
Warehouse wages	3,500,000
Inventory at 1 October 2019	1,750,000
Inventory at 30 September 2020	2,750,000

3. You are required to prepare an income statement for the year ending 31/3/2020 from the following details of Magoti.

<b>Details</b>	<b>TZS</b>
Inventory at 1/4/2019	18,685,000
Inventory at 31/3/2020	21,983,000
Sales	279,000,000
Purchases	111,600,000
Carriage outwards	4,250,000

Sales returns	4,840,000
Purchases returns	3,600,000
Wages and salaries	5,400,000
Rent expense	9,000,000
Rent income	10,800,000
Discount allowed	1,260,000
Discount received	1,440,000
General expenses	16,200,000
Insurance	1,800,000
Telephone expenses	2,980,000
Water expenses	1,825,000

4. The following balances were extracted from books of Kafanabo for the year ending 31 December 2020. Use the information provided to prepare his statement of financial position as on 31 December 2020.

<b>Details</b>	<b>TZS</b>
Capital at 1 January 2020	76,525,000
3 year loan from Karagwe Bank	50,500,000
Sales	130,800,000
Furniture	9,500,000
Building	38,650,000
Profit for the year	11,067,500
Land	15,625,000
Purchases	75,250,000
Drawings	6,600,000
Salaries	37,750,000
Bank overdraft	10,095,000
Wages	25,250,000
Accounts payable	22,800,000
Motor vehicle	15,750,000
Fixtures and fittings	55,250,000
Inventory on 31 December 2020	6,125,000
Accounts receivable	23,487,500
Rent	5,250,000

5. The following trial balance was extracted from books of Tyson on 30 April 2021. Prepare his income statement for the year ending 30 April 2021 and the statement of financial position as at that date.

Details	Dr (TZS)	Cr (TZS)
Sales		154,320,000
Purchases	75,867,200	
Inventory 1 May 2020	16,531,200	
Carriage outwards	2,391,200	
Carriage inwards	3,880,800	
Sales returns	7,732,800	
Purchases returns		6,426,000
Salaries and wages	11,336,400	
Motor expenses	16,396,800	
Rent	18,547,200	
Rates	6,144,000	
Sundry expenses	13,442,400	
Motor vehicle	34,880,000	
Fixture and fittings	9,920,000	
Accounts receivable	17,492,400	
Accounts payable		15,654,000
Cash at bank	29,651,200	
Cash in hand	1,144,000	
Drawing	14,460,000	
Capital		103,417,600
<b>Total</b>	<b>279,817,600</b>	<b>279,817,600</b>

Inventory on 30 April 2021 was TZS 17,997,600.

6. From the following Nzowa's trial balance, prepare her income statement for the year ending 31 December 2020 and a statement of financial position as on that date.

Details	Dr (TZS)	Cr (TZS)
Opening inventory	22,624,000	
Carriage inwards	5,580,000	
Purchases returns		5,796,000
Sales returns	3,690,000	
Carriage outwards	3,600,000	
Purchases	213,732,000	
Sales		334,800,000
Salaries and wages	69,516,000	
Rent and rates	5,472,000	
Insurance	2,404,000	
Motor expenses	11,952,000	
Office expenses	3,888,000	
Lighting expenses	2,988,000	
General expenses	9,652,000	
Premises	115,000,000	
Motor vehicles	32,400,000	
Fixtures and fittings	6,300,000	
Accounts receivable	60,128,000	
Accounts payable		51,158,000
Cash at bank	28,676,000	
Drawings	21,600,000	
Capital		227,448,000
	<b>619,202,000</b>	<b>619,202,000</b>

The inventory on 31 December 2020 was TZS 58,920,000.

7. The following trial balance was extracted from books of Bwiikizo LTD, on 30 May 2021. Prepare his income statement for the year ending 30 May 2021 and the statement of financial position as on that date.

Details	Dr (TZS)	Cr (TZS)
Sales		134,320,000
Purchases	85,867,200	
Inventory 1 May 2020	16,531,200	
Carriage outwards	7,591,200	
Carriage inwards	6,880,800	
Sales returns	7,732,800	
Purchases returns		12,426,000
Salaries and wages	41,336,400	
Motor expenses	30,796,800	
Rent	18,547,200	
Rates	10,617,600	
Sundry expenses	30,242,400	
Motor vehicle	14,880,000	
Fixture and fittings	19,920,000	
Accounts receivable	17,492,400	
Accounts payable		15,654,000
Cash at bank	16,651,200	
Cash in hand	3,144,000	
Drawing	14,460,000	
Capital		180,291,200
	<b>342,691,200</b>	<b>342,691,200</b>

Inventory on 30 May 2021 was TZS 14,449,940.

# Glossary

<b>Account</b>	This is a summarised record of a business transaction. It can be presented on a page of a ledger book.
<b>Assets</b>	These are economic resources controlled and used by an enterprise to support the generation of revenue.
<b>Books of prime entry</b>	Are also known as books of original entry or subsidiary books used to record the transaction in books of the accounts for the first time. These names can be used interchangeably.
<b>Business Capital</b>	Any legal activity undertaken with the aim of making profit. Amount of resources contributed by an owner or other financing sources to start or expand a business.
<b>Concept</b>	Basic general idea regarding something.
<b>Credit</b>	The right-hand side of an account.
<b>Creditor</b>	This is a supplier who sells to us on credit and we promise to pay at a later date. Another name is Account payable or simply “payables”.
<b>Debit</b>	The left-hand side of an account.
<b>Debtor</b>	This is a customer who buys from us on credit and promises to pay at a later date. Another name is Account receivable or simply “receivables”.
<b>Discounts</b>	Are reductions from the usual price of something and may be associated with timely payment.
<b>Double entry</b>	The system or principle of Book-Keeping whereby each business transaction is supposed to be recorded twice.
<b>Drawings</b>	Goods or money taken by the owner from a business for personal or private use.
<b>Entry</b>	An item recorded in a journal or a ledger account.
<b>Expenses</b>	These are costs of operating business.
<b>Financial statements</b>	Financial reports produced at the end of the accounting period. Examples of a financial statements are an income statement and a statement of financial position.
<b>Fittings</b>	Items that are attached to a property other than a nail or a screw, for example, picture or mirror, and plumbing (water system).
<b>Fixtures</b>	Items that are attached or fixed to the property, for example, ceiling fan, ceiling lights, and built-in shelves.
<b>Folio</b>	A page of reference in a book of accounts.
<b>Income</b>	These are receipts or gains of a business.
<b>Interest</b>	Is money paid regularly or at specific intervals at a particular rate for the use of money lent or borrowed.

<b>Inventory</b>	Goods which are held by the business for resale. For a manufacturing firm, they may be finished goods, partly finished goods or raw materials awaiting conversion or processing into finished goods which will then be sold.
<b>Investor</b>	A person (or entity) who puts her money into business in order to become one of the owners for the purpose of getting a share of the profit generated.
<b>Invoice</b>	It is a document prepared by a seller and sent to a buyer when goods are sold or services are rendered on credit.
<b>Journal</b>	A book of prime entry where transactions are initially recorded before they are posted to ledger accounts.
<b>Ledger</b>	The main book of an account which is used to record business transaction using the double entry principle of Book-Keeping.
<b>Liability</b>	A claim against resources of an enterprise.
<b>Liquidity</b>	It is a measure of the ability of a business to meet its financial obligations as they fall due. One of the indicators of liquidity is time spent to convert its assets into cash.
<b>Loss</b>	The excess of expenses over revenue.
<b>Non-productive assets</b>	These are assets existing in the business but not fully utilized to generate revenue. For example, a large office building in excess of the business requirements may represent a non-productive asset.
<b>Occupation</b>	This is a person's principal work or business used as a means of earning a living.
<b>Overdraft</b>	Loan facility provided by a bank to an account holder to withdraw and pay bills when the account balance is insufficient.
<b>Owner's equity</b>	Capital contributed by an owner to start or expand a business.
<b>Posting</b>	The transferring of entries from a book of prime entry to the relevant ledger accounts.
<b>Profit</b>	The excess of revenue over expenses.
<b>Purchases</b>	Goods bought for resale.
<b>Receipt</b>	A printed acknowledgment of the amount of cash received in a transaction that involves transfer or payment of cash.
<b>Revenue</b>	Sum of income generated in the normal course of business operations (such as income from sales of goods) before the deduction of expenses.
<b>Services</b>	Intangible goods that are sold or bought.
<b>Sole-proprietor</b>	Single owner of a business.
<b>Statement of affairs</b>	A statement which lists all assets and liabilities (together with their financial value) to enable one calculate value of capital.
<b>Transaction</b>	This is a business event that has financial value capable of being recorded in books of accounts using double entry system of Book-Keeping.
<b>Wages</b>	Payment made to casual workers for the work done.

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