

UNIVERSAL
LIBRARY

OU_158018

UNIVERSAL
LIBRARY

OSMANIA UNIVERSITY LIBRARY

Call No. 657/W 51 B Accession No. 31343

Author West O. J.

Title Book Keeping & Acctg. of Private Companies

This book should be returned on or before the date last marked below.

1980.

**BOOK-KEEPING
AND
ACCOUNTANCY
FOR
PRIVATE COMPANIES**

**BY
OWEN JAMES WEST, F.C.A., F.C.I.S.**

**FELLOW OF THE INSTITUTE OF CHARTERED ACCOUNTANTS IN ENGLAND
AND WALES**

**FELLOW OF THE CHARTERED INSTITUTE OF SECRETARIES OF JOINT
STOCK COMPANIES AND OTHER PUBLIC BODIES**

**CLERK TO THE COMMISSIONERS OF INCOME TAX AND LAND TAX FOR THE
DIVISION OF READING**

FOURTH EDITION

**LONDON
JORDAN & SONS, LIMITED
CHANCERY LANE, W.C.2
1950**

FIRST EDITION PUBLISHED *November* 1937
SECOND " " *January* 1943
THIRD " " *September* 1946
FOURTH " " *May* 1950

PRINTED AND BOUND IN ENGLAND BY
HAZELL WATSON AND VINEY LTD
AYLESBURY AND LONDON

PREFACE

THIS book has been written by request. It was the considered opinion of the Publishers and others best qualified to judge that a practical guide to the subject of Book-keeping and Accountancy was necessary in order to meet the requirements of business men, secretaries, and accountants responsible for the formation and conduct of Private Limited Companies.

The rapid development of the Private Limited Company and the increasing number of registrations each year is testimony to public appreciation of the advantages which the Private Limited Company offers compared with the Sole Trader or Partnership concern. It is known, however, that some business men are still under the impression that the registration of a Private Limited Company necessitates the keeping of a multitude of complicated books and statistical records, and for that reason they feel somewhat prejudiced against incorporation. This book should materially assist in dispelling such an erroneous impression ; at the same time the indisputable fact must be recognised that a business, however constituted, cannot be properly and remuneratively conducted without efficient book-keeping and accountancy records.

A glance at the wide range of rulings offered by account-book manufacturers is an indication of the variety of books in use and the dissimilarity between one business and another. In selecting examples of actual books used in businesses with which the author is connected, the needs of those engaged in manufacturing, distributing, and operating trades have been considered. Even as between businesses in any one of these groups there is variation in detail and readers may therefore find it advisable, when reviewing their own requirements, intelligently to *adapt* rather than automatically to *adopt* the examples given.

The construction of the Annual Accounts of a Private Limited Company for presentation to the Auditors has been dealt with in detail as it is considered desirable that the statutory duty of preparing the accounts should be carried out whenever possible by the Director, Secretary, or Accountant respon-

sible for the financial records of the company. The preparation and interpretation of Annual Accounts are complementary matters of the utmost importance in business. Usually, a person who is able to prepare accounts in a proper form is equally able to interpret the facts which accounts reveal.

No attempt has been made to meet all the requirements of those taking examinations in the subject, but when their examinations have been passed, students may find the book of some service in bridging the gap between theoretical knowledge and practical application, and of some assistance to them in retaining interest in an extremely useful and fascinating subject, a knowledge of which is an essential commercial qualification.

The author desires to record his appreciation of the assistance rendered by his colleagues Mr. R. R. Coomber, B.Sc. (Econ.), F.C.A., and Mr. R. O. Brennand, M.A. (Cantab.), LL.B.(Lond.), of the Middle Temple, Barrister-at-Law.

Finally, the writer hopes that he has adequately fulfilled the task entrusted to him and that readers will find in the following pages guidance and information which will be of practical assistance to them in the performance of their duties.

O. J. W.

NOTE TO THE FOURTH EDITION

This Edition has been revised in accordance with the Companies Act, 1948, and the explanations and examples amplified where necessary. Subsequent recommendations on Accountancy Principles made by the responsible accountancy bodies have been followed in the appropriate examples.

O. J. W.

5-6, Broad Street,
Reading.
January 1950.

CONTENTS

	PAGE
PREFACE	iii
CHAPTER	
I. GENERAL PRINCIPLES OF ACCOUNT KEEPING .	I
Double Entry. The Journal. Modern Methods. Balancing.	
II. CASH BOOKS	6
Cash Received Book. Cash Payments Book. Bank Reconciliation Statement. Petty Cash Book. Imprest System of Petty Cash.	
III. SUBSIDIARY BOOKS	18
Purchases Day Book. Purchases and Expenses Day Book. Returns Outwards (Purchases Returns) Day Book. Sales Day Book. Returns Inwards (Sales Returns) Day Book. Bills Payable Journal. Bills Receivable Journal. Journal Proper.	
IV. SALES AND PURCHASES LEDGERS	34
Sales Ledgers. Columnar Sales Ledgers. Purchases Ledgers.	
V. SELF-BALANCING LEDGER SYSTEM	42
Sales and Purchases Ledgers. Analysed Subsidiary Books.	
VI. NOMINAL OR PRIVATE LEDGER. THE TRIAL BALANCE	53
Nominal Ledger Accounts Trial Balance.	
VII. ACCRUALS, ADJUSTING ENTRIES AND DE- PRECIATION ; STOCK-TAKING	62
Expenses Due and Accrued. Unexpired Expenditure. Income Due and Accrued. Depreciation Methods. Machinery and Plant Register.	
VIII. MANUFACTURING, TRADING, AND PROFIT AND LOSS ACCOUNTS. BALANCE SHEET.	77
Manufacturing Account. Trading Account. Profit and Loss Account. Appropriation Account. Balance Sheet.	
IX. INCORPORATION OF A PRIVATE LIMITED COMPANY	90
Steps in Conversion. Profits and Losses prior to In- corporation. Memorandum and Articles of Association. Documents to be filed with Registrar.	

CHAPTER	PAGE
X. CONVERSION OF A BUSINESS INTO A PRIVATE LIMITED COMPANY.	99
Book-keeping Entries. Closing Partnership Books. Opening Books of New Company. Initial Trading Transactions. Suitable Books of Account.	
XI. A COMPANY'S ACCOUNTS—STATUTORY PROVISIONS.	118
Financial Books. Annual Accounts. Subsidiary Companies. Signing and Circulating the Balance Sheet. Annual Report and Accounts. Statutory Books.	
XII. CAPITAL OF A COMPANY	129
Forms of Share Capital. Debentures. General Structure of Capital.	
XIII. DIVIDENDS—CAPITAL AND REVENUE—RESERVES.	134
Capital and Revenue. Bonus Shares. Reserves and Provisions.	
XIV. FINAL ACCOUNTS	139
Presentation and Interpretation. Comparative Results and Percentages. Working Capital. Reading the Accounts. Considerations on Purchase of a Business.	
XV. DEPARTMENTAL ACCOUNTS	148
Departmental Subsidiary Books. Departmental Cash Books. Departmental Transfers. Departmental Trading and Profit and Loss Accounts.	
XVI. BRANCH ACCOUNTS	161
Maximum Head Office Control. Branches as Independent Units. Incorporation of Final Accounts in Head Office Books. Combined Balance Sheet.	
APPENDIX	176
Eighth Schedule to the Companies Act, 1948. Balance Sheet: Profit and Loss Account.	
INDEX	182

BOOK-KEEPING AND ACCOUNTANCY FOR PRIVATE COMPANIES

Chapter I

THE GENERAL PRINCIPLES OF ACCOUNT KEEPING

DOUBLE ENTRY

PROMINENT business men have frequently stated that an accurate and well-organised set of account books is an essential feature of a successful business.

An efficient system does not necessarily imply elaboration ; in fact, simplicity should be the aim of every accountant in the work of inaugurating and conducting a Book-keeping System. But we arrive at the simplex through the complex, and a certain amount of study is therefore necessary.

Although there are still a number of concerns which carry on the recording of their financial entries under the loose and incomplete method of "Single-entry" book-keeping, the majority of systems now follow "Double-entry" principles.

The double-entry system is not new. It was probably during the early part of the fourteenth century that this system was conceived and adopted by the old merchants of Italy, Spain, Holland, and a few other countries. In the year 1494, however, an Italian mathematician, Frater Luca Pacioli, of Venice, wrote a mathematical book which included a treatise on Book-keeping on double-entry principles. These first principles have remained unshaken throughout the ages, and form the basis of the systems in universal use to-day.

The principles expounded by Pacioli were very simple. First, he made an Inventory of all the assets and all the liabilities of the trader, and, by deducting the total liabilities from the total assets, he arrived at the amount of the trader's capital in his business. This statement is known to-day as a "Statement of Affairs," and is an essential preliminary to the opening of a set of books on double-entry principles. In a later chapter an example of a "Statement of Affairs" will be found.

THE JOURNAL

As the day-to-day transactions took place they were entered in a Memorandum Book or Diary, and when the day's business was over the merchant transferred the entries contained in this Memorandum Book to a book called a Journal.

The Memorandum Book, having served its purpose of relieving the merchant's memory of his business transactions for the day, was kept for reference purposes only and not used as part of the double-entry system. The use of this Memorandum Book is still suggested in some text-books, and although it is in use in some small concerns where the number of transactions is limited, the reader will no doubt realise the impossibility of its adoption in a business of any size.

The function of the Journal was the classification of the business transactions of the merchant so that they might be readily transferred or posted to his Ledger. Every transaction was considered to have a twofold aspect and recorded as such by posting each transaction twice—one aspect to the debit of an account and the other to the credit of another account. For example, goods sold to a customer were debited to the customer's account and credited to the Sales Account. Conversely, goods bought from another merchant were credited to that merchant's account and debited to Purchases Account. Cash received from a customer was debited to the Cash Account and credited to the customer's account. On the other hand, cash paid to another merchant was debited to that merchant's account and credited to the Cash Account. This twofold aspect of each transaction was shown in the Journal, indicating which account was to be debited and which account was to be credited.

The function of the Ledger was to summarise transactions in the form of accounts so as to indicate the amounts owing to or by the merchant and to classify his income and expenditure under significant headings.

As to whether a particular entry should be placed to the left-hand side (the debit) or to the right-hand side (the credit) of a ledger account is frequently a problem which presents itself to the junior. Time and practice have decreed that assets, purchases and expenses, losses and deficiencies are debit entries, whilst liabilities, sales, profits and surpluses are credit entries. Elementary book-keeping text-books explain certain rules designed to help the beginner in deciding which side of an account particular items are posted. The author has found

in practice, however, that these rules, helpful as they are to the student, are frequently quite unknown in their academic form to many book-keepers whose habit of posting items to the correct side of accounts has become their second nature.

MODERN METHODS

The journalising of every transaction separately was a method which the old merchants were able to carry out quite satisfactorily in the leisure time which may have been at their disposal in those days ; with modern business, and its vast number of transactions, the adoption of this method in its original form is a practical impossibility.

To-day we group or classify our business transactions, using separate journals or books of first entry for each group of classified items instead of one journal for all items whatever their nature might be. Thus, we have separate journals or books to record Cash, Sales and Purchases, Returns Inwards and Outwards, Bad Debts, and other journals varying in description according to the nature and size of the business. It is true that the word " Journal " has given place to the simple word " Book," or in the case of Sales and Purchases to the words " Day Books," but this is merely a change in name and does not alter the fundamental principles. The basic purpose of the Journal remains the same, namely, the orderly classification of the business transactions as and when they occur in such a manner as to enable posting to the Ledgers to be carried out speedily and accurately.

It has already been explained that in posting from the Journals, the general principle to be observed is that an entry must be posted to the debit side of one account and to the credit side of another, each entry being treated separately as was done by the old merchants, or by the modern method of posting one side of the transaction separately and the other side in total with other entries of a similar nature. For example, instead of journalising each receipt and payment of cash, the amounts received are grouped together on the debit side of the Cash Book and posted to the credit of the individual accounts in the Ledger ; payments are grouped together on the credit side of the Cash Book and debited individually to the accounts in the Ledger. In effect, the Cash Book is a ledger account itself as well as a book of first entry.

Again, the items of credit sales appearing in the Sales Journal or Day Book are each debited or charged to the individual

accounts of the customers, and the credit aspect of the transactions is posted to the Sales Account in periodical totals, daily, weekly or monthly, according to the number of the transactions and nature of the business. The age-old rule of double entry, namely, that every item must be posted twice—to the debit of one account and to the credit of another—is observed, the only difference being that by grouping items of like nature together, one aspect of the transaction is posted in total with other items of similar character.

The old-time journal has gradually developed into several journals or day books, and in the same way the ledger has also been divided. To-day we have several ledgers, such as Bought, Sales, Nominal or Private, etc., each designed to record business transactions conveniently and according to particular requirements. We also have varying types of cash books which can be regarded as cash accounts bound up into book form.

BALANCING

Having posted the transactions from the Journal to the debit and credit of the relative accounts in the Ledger, it follows that if the work has been correctly carried out, the total debits will exactly equal the total credits. Proof of this fact is obtained by preparing, as was done in Pacioli's time, a statement known to-day as the "Trial Balance," which is explained in Chapter VI.

As to the source of inspiration which prompted the old merchants to adopt the double-entry system in its simplest form, we can only conjecture, but it seems to the writer that the method was simply the weighing of figures in scales or balances. The merchant weighed his goods, and if the weight were correct the scales balanced; similarly he weighed his figures by placing equal amounts on either side of the scales, and if his work were correct his books balanced. That is precisely what we do to-day. The separate items in, say, the Sales Journal or Day Book are posted to the individual Personal Ledger accounts, and can be regarded as the separate weights placed on one side of the scales. Then the total of these figures is periodically ascertained by casting the Sales Journal or Day Book and posting to the credit side of the Sales Account, and can be regarded as the placing of one single weight on the other side of the scales.

The scales on which we do our weighing or balancing are represented by the Trial Balance, and when this balances it is

known, with certain exceptions, that the process of posting or transferring to the ledgers has been carried out accurately.

It may seem unnecessary to go into such elementary theories in a book which is intended for the use of business men, but the training of junior employees to more responsible positions in the accounts office is often simplified by a clear exposition of these elementary principles at the outset. The author has found that the scales method of explaining the theory of double-entry book-keeping brings home these first principles much better than the laborious and uninteresting methods sometimes adopted.

Chapter II

CASH BOOKS

THE necessity for keeping a complete and accurate record of cash transactions cannot be too strongly emphasised, and as all businesses involve the receipt and payment of money, a book-keeping system cannot be conceived where the use of the Cash Book can be dispensed with. Indeed, it has been frequently found that, apart from certain memorandum data, it is the only record kept in many small businesses. This fact is not mentioned as a suggestion which should be followed, but merely to illustrate that, even in concerns where a certain amount of laxity is expected, the proprietors realise the indispensability of the Cash Book.

In the keeping of cash records, it is recommended that all receipts of money should be banked intact, and all amounts, other than the usual petty expenditure, paid by cheque. The practice of applying cash received to pay for purchases and expenses should be avoided. The advantage of paying all receipts of cash into the bank is obvious ; it enables a ready agreement to be made between the amounts banked and the trading receipts of the business, and minimises the risk of failing to record expenditure. The payment of small amounts can be made through the medium of the petty cash float, as explained later.

If this principle is observed, the Cash Book corresponds in detail with the Bank Pass Book and should be agreed as frequently as is necessary and possible.

In practice many different types of cash books are found, each being framed according to the nature of the business and the volume and value of the transactions. It is futile to attempt to dogmatise on a general form, and it should be the duty of the accountant or secretary to study carefully the particular requirements of the business with which he is connected in order to devise a type and form of Cash Book most suitable for the rapid and clear recording of the transactions.

The receipts and payments of cash are usually shown in one book in the case of small concerns, the receipts on the left-hand page and the payments on the right. There are, however, advantages in recording the receipts and payments in separate books, particularly where the volume of receipts varies greatly from the volume of payments. In a particular company with which the author is connected, the recording of receipts is carried out by an assistant, and the records of payments by cheque kept by the secretary, because it is not considered advisable for an assistant to have access to details of the cheques drawn. In large concerns separate books are almost invariably used.

Where discounts are received and allowed it is found convenient to record the amounts in separate columns ruled by the side of the Cash Received and Cash Paid Columns in the Cash Book. The alternative is to journalise the discounts separately or collectively, but this method entails unnecessary labour.

In order to form a practical guide to readers, a few typical cash-book rulings are given, which have been taken from cash books in actual use in various trades. For the purpose of illustration, it has been found convenient to deal with the receipts and payments separately. The reader will remember, however, that both the receipts and payments may be included in one book where possible and where there is no objection from an administrative point of view.

CASH TRADE

The following ruling for the recording of cash received may be suitably adapted for use where all business is transacted on a cash basis, no credit being given.

This ruling is suggested where it is required to analyse the receipts as between departments, travellers' territories, or other suitable classification. If such division is not necessary, the analysis columns can be dispensed with, and one total sales column substituted.

It has been assumed for the purpose of brevity that the sales are made up and banked weekly, although in most businesses bankings are made more frequently.

The Sundries Column is used to record cash received other than for sales, such as money received in respect of share, debenture or loan capital, transfer fees, sales of fixed assets,

*Dr.**CASH*

Date.	Particulars.	Fol.	Amounts Banked.		
19—			£	s.	d.
Jan. 1	To Balance brought forward .	✓	470	10	6
„ 2	„ Cash Sales as per summary	1	43	6	1
„ 9	„ do. .	4	149	8	4
„ 16	„ do. .	7	74	10	0
„ 23	„ do. .	10	82	7	3
„ 30	„ do. .	16	112	3	6
„ 31	„ Loan from Director .	N L. 10	500	0	0
„ 31	„ Transfer Fees . .	N.L. 42	12	6	
			£1,432	18	2

etc., and other items which require to be posted to a separate ledger account in the Nominal or Private Ledger. In order that the total cross-casts of the analysis columns may agree with the total of the Amounts Banked Column, it is suggested that the opening balance of cash at bank (if any), which forms the first entry in the Amounts Banked Column, should be extended to the Sundries Column.

The use of cash registers is advocated, where possible. These machines afford an invaluable internal check on cash and give an accurate record of the details and daily cash totals. In other cases details of the cash sales are recorded in Cash Sales Books and summarised daily. These totals, taken from the Till Rolls, Cash Sales Book, or Cash Sales Summary, are the figures to be entered in the General Cash Received Book as illustrated.

The folio column should be used to record the reference to the Cash Sales Book, Cash Sales Summary, or Till Rolls, the latter being numbered. Similar reference to the folio of the Cash Book is shown in the Cash Sales Book, Cash Sales Summary, or on the Till Rolls.

The items shown in the "Sundries" column are posted to the credit of the relative accounts in the Nominal or Private Ledger, reference to which is made in the folio column.

The total of the cash sales for the month is posted to the credit of the Sales Account in the Private or Nominal Ledger and similarly cross-referenced.

RECEIVED (Cash Trade)

Sales Analysis columns for division as between departments, travellers, etc.									Sundries.		
£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.
									470	10	6
20	7	8	13	4	6	9	13	11			
51	7	4	90	0	7	8	0	5			
26	7	6	30	4	6	17	18	0			
41	2	0	19	9	8	21	15	7			
49	17	8	36	10	0	25	15	10			
									500	0	0
									12	6	
189	2	2	£189	9	3	£83	3	9	£971	3	0

Total Cash Sales £461 15s. 2d.

N.L.1

CASH AND CREDIT TRADE

The essential feature of the Cash Book of a business where credit is given is the separation of the cash received from customers in payment of their accounts and the cash received in respect of ready-money sales. This is simply a question of the convenient ruling of the Cash Book and an example is shown. One Sales Ledger has been assumed; where more than one Sales Ledger is in use the Cash Received Book should be ruled accordingly and an example is given in Chapter V.

As and when a customer pays his account, the amount received is entered in the Details Column and the discount in the Discount Column. The cash received and discounts allowed are extended to the Sales Ledger Column and posted to the credit of the customer's account in the Sales Ledger.

The daily or weekly cash sales totals are entered in the Details Column and extended to the Cash Sales Analysis Column.

At banking time the amounts shown in the Details Column are simply added and the total extended to the Amounts Banked Column. When the amount banked refers to cash sales only, the figures are entered in the Amounts Banked Column direct and not in the Details Column.

At the end of the period, usually monthly, the total of the Discount Column is posted to the debit of the Discount Account in the Nominal or Private Ledger. The Cash Sales total is posted to the credit of the Sales Account, as already explained.

*Dr.**CASH*

Date.	Particulars.	Fol.	Details.		
19—			£	s.	d.
Jan. 1	To Balance brought forward . . . ✓				
" 2	" Cash Sales . . .	12	54	7	6
" 8	" M. Bradbury . . .	10	18	11	0
" 8	" T. Smith . . .	31	2	12	2
" 9	" Cash Sales . . .	14			
" 16	" do. . .	18	184	10	8
" 16	" J. Williams . . .	28	40	6	0
" 16	" E Hicks. . .	43	19	11	0

PAYMENTS

It has already been emphasised that all payments, other than petty cash payments, should be made by cheque. The illustrations and explanations given are based on that principle, and a simple ruling follows :

CHEQUE

Date.	Particulars.	V.	L/F.	Cheque.		
19—				£	s.	d.
Jan. 3	By M Brown, Ltd. . .	1	10	47	10	0
" 4	" Wages . . .	2	N L.2	28	4	0
" 4	" Petty Cash . . .	3	3	3	10	0
" 6	" J. Oslo & Co. . .	4	14	118	15	0
" 7	" O. Richards . . .	5	31	35	2	0
" 31	" Balance carried forward			668	12	2
				£901	13	2

In this case one Bought Ledger, a Private or Nominal Ledger, and a Petty Cash Book are assumed. In larger businesses more than one Bought Ledger will be required and in Chapter V a suitable form of Cash Payments Book is

RECEIVED (*Cash and Credit Trade*)

Amounts Banked.	Discounts.	Sales Ledger. (Cash and Discount)	Cash Sales.	Sundries.
£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.
260 8 6				260 8 6
	9 6	19 0 6	54 7 6	
75 10 8	3 4	2 15 6		
321 6 4			321 6 4	
			184 10 8	
	2 3 0	42 9 0		
	10 6	20 1 6		
244 7 8				
£901 13 2	£3 6 4	£84 6 6	£560 4 6	£260 8 6

N L.36

N.L.2

shown. Each item is extended to the appropriate analysis column and posted to the debit of the relative account in the Bought Ledger or Private or Nominal Ledger as the case may be. The petty cash cheques are posted to the debit side of the Petty Cash Book.

PAYMENTS

Cr.

Bought Ledger.		Petty Cash.	Private or Nominal.
Discount.	Cash.		
£ s. d.	£ s. d.	£ s. d.	£ s. d.
2 10 0	47 10 0		28 4 0
		3 10 0	
6 5 0	118 15 0		
18 0	35 2 0		
			668 12 2
£9 13 0	£201 7 0	£3 10 0	£696 16 2

N.L.10

The narrow column headed "V" is recommended for the purpose of recording the number of the voucher or receipt for each payment. The receipts should be numbered consecutively and filed for reference purposes.

CHEQUE

Date.	Particulars.	V.	Cheque.	Film Hire.	Carriage.	Advertis- ing.	Entertain- ment Tax.
19—			£ s d.	£ s. d.	£ s. d.	£ s. d.	£ s d.
Jan. 1	By A.D.C. Ltd. . .	1	27 10 0	27 10 0			
" 2	" Billposters, Ltd. . .	2	15 15 0			15 15 0	
" 3	" Customs and Excise . .	3	45 10 0				45 10 0
" 4	" British Rlys. . .	4	5 15 0		5 15 0		
" 4	" Pembroke Ltd. . .	5	3 17 6				
" 5	" Forward & Co., Ltd. ; Talking Apparatus	6	354 0 0				
" 5	" W. Jeffries : Rent to Christmas	7	50 0 0				
" 6	" L. Saunders : Audit Fee	8	26 5 0				
" 6	" Wages and Petty Cash	9	63 8 7				
			592 1 1	27 10 0	5 15 0	15 15 0	45 10 0

N.L.2 N.L.5 N.L.8 N.L.14

The items to be entered in the Private or Nominal Ledger Column will depend on the system adopted in dealing with the Bought Ledger. The Private or Nominal Ledger Column is normally used for recording payment of items not connected with the purchase of goods for resale, e.g., expenses (capital and revenue), repayment of loans, purchase of assets, etc. In some book-keeping systems, the Bought Ledger is used to record the personal accounts of those to whom expenses, etc., are paid, e.g., the landlord's account for rent, the Rating Authority for rates, and so on, in which case the payments for these expenses are extended to the Bought Ledger Column, and posted to the debit of the particular personal account in the Bought Ledger. This system of recording the personal aspect of expenses in the Bought Ledger has much to commend itself, and will be explained in a later chapter.

The cheques drawn for petty cash are extended to the Petty Cash Column so that a periodical total agreement of petty cash spent, as detailed in the Petty Cash Book, may be effected.

In certain classes of businesses of an operating nature, e.g., Cinema or Omnibus business, where the purchase and sale of goods are not involved, the records for expenses are treated on a cash basis. The usual Bought Ledger is dispensed with and no record is made in the books of account until the amounts are paid. The items are then entered in the Cash Book and

PAYMENTS

Heat, Light, Power.	Rent, Rates, Insurance.	Salaries and Wages.	Petty Cash.	Post, Telephone, Office Expenses.	Chocolates and Cigarettes.	Repairs and Renewals.		L/F.	Sundry Unclassi- fied Items.
						Equip- ment.	Buildings.		
£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.		£ s. d.
						3 17 6			
	50 0 0							N.L.60	354 0 0
		43 8 0	20 0 7					N.L.38	26 5 0
	50 0 0	43 8 0	20 0 7			3 17 6			380 5 0

N.L.20 N L 26 P C.43 N.L.32

posted direct to the debit of the relative expense accounts in the Private or Nominal Ledger.

When this method is adopted, the Cash Book should be suitably ruled with columns headed according to the various expenses, and the totals of these columns posted periodically (generally monthly) to the debit of the relative Private or Nominal Ledger Accounts. This method saves an enormous amount of time as compared with the alternative method of posting each payment separately. Certain occasional expenditure not warranting a separate column should be extended to the Sundries Column for separate posting.

A ruling of the payments side of a Cinema Company's Cash Book in actual use is illustrated.

In order that this method may be successfully applied, it is essential that the invoices should be carefully filed and checked with the statements at the end of each month, so as to avoid the overlooking of accounts at payments time. This system works quite well where all accounts are fully paid at the end of each month. Provided the filing of the invoices has been properly carried out, the clearing of the payments file ensures that all accounts have been paid. Where, however, financial or other reasons do not permit the settling in full of all accounts at payments time, the Bought Ledger system is recommended.

THE BANK RECONCILIATION

The recommended method of paying all receipts of cash into the bank and paying all accounts by cheque having been adopted, it necessarily follows that the Amounts Banked Column and Cheque Column of the Cash Book should agree with the Bank Pass Book.

The agreement of the Cash Book with the Pass Book should be made at regular intervals, the frequency of which depends upon the volume of transactions.

It is often found on checking the Pass Book that certain items, such as bank charges and commissions, have not been recorded in the Cash Book. These items, if approved, should be entered in the Cash Book and extended to the relative analysis columns. It is also generally found that certain cheques drawn towards the end of the month have not been presented at the bank for payment until the succeeding month. Conversely, the cash received on the last day of the month may be banked on the first day of the next month and shown in the Pass Book accordingly.

As a result, the balance as shown by the Cash Book may not agree with that shown by the Pass Book, notwithstanding the fact that the Cash Book has been correctly entered and balanced. In order to agree the balance according to the Cash Book with that shown by the Pass Book, it is necessary to prepare what is known as a Bank Reconciliation Statement. An illustration follows.

BANK RECONCILIATION AS AT 31ST JANUARY, 19—

	£	s	d.
Balance in hand at Bank, as per Cash Book . . .	1,516	10	8
<i>Add</i> Cheques outstanding . . .	210	8	4
	78	3	4
	12	0	0
	300	11	8
<i>Less</i> Lodgment credited on 1st February . . .	£1,817	2	4
	195	7	3
Balance in hand at Bank, as per Pass Book . . .	£1,621	15	1

In the case of a bank overdraft the outstanding cheques would be deducted and the outstanding lodgments added in order to make the reconciliation.

The reconciliation may be stated by starting with the Pass

Book balance and working down to the Cash Book balance, but the result will, of course, be the same.

It has already been mentioned that the receipts and payments of cash may be kept in separate books where the system or size of the books makes this necessary. In such cases it follows that the periodical balancing of the cash will involve the use of the two books. For this reason it is generally found more convenient to make a summary on the following lines, rather than to balance the Cash Books in the usual way.

SUMMARY—31ST JANUARY, 19—

	£	s.	d.
Balance in hand at Bank on 31st December as per Cash Book	1,584	3	6
Cash banked as per Cash Received Book	1,025	8	3
Cheques drawn as per Cash Payments Book	£2,609	11	9
	1,093	1	1
Balance in hand at Bank on 31st January as per Cash Book	£1,516	10	8

The Bank Reconciliation shown above can conveniently follow on at the end of this summary, making one complete statement.

In the event of a bank overdraft at the beginning the statement would commence with the opening overdraft, the total cheques drawn during the month added and the total bankings deducted.

PETTY CASH

In all businesses a certain amount of expenditure will occur which is not paid for by cheque owing to the nature of the expenditure or the smallness of the amount. For this reason the keeping of a Petty Cash Book on the correct principles is an essential part of a Book-keeping System.

The analytically ruled Petty Cash Book is in almost universal use to-day, being the most suitable type for recording expenses of a recurring nature.

The following illustration shows analysis columns of general application. The reader should bear in mind that while the suggested headings are general ones, the grouping of the expenditure will depend upon the nature and requirements of the particular business, and the Petty Cash Book should be headed accordingly.

PETTY CASH

Date.	Fol.	Cash Received.	Particulars.	V.	Total.	Fares.
		£ s. d.			£ s. d.	£ s. d.
19—						
Jan. 1	22	10 0 0	Balance in hand . . .	✓		
" 2			Stationery . . .	1	1 5 0	
" 4			Postage . . .	2	1 10 0	
" 6			Repairs to Doors . . .	3	3 17 6	
" 7			A. C. Brown's A/c . . .	4	10 8	
" 8			Fares . . .	5	1 6	1 6
" 8			Office Cleaning . . .	6	1 5 0	
" 8			Office Teas . . .	7	2 6	
			Balance c/d . . .	✓	8 12 2 1 7 10	1 6
		£10 0 0			£10 0 0	N.L.10
Jan. 8	✓	1 7 10	Balance b/d . . .			
" 9	30	8 12 2	Cheque . . .			

The only items normally entered in the left-hand (Cash Received) Column are the periodical petty cash cheques which are drawn from time to time to replenish the float.

A study of the illustration will show that each payment is recorded in the total column and extended to the appropriate analysis column.

The narrow column headed " V " is recommended for the purpose of recording the number of the petty cash voucher or receipt for each payment. The receipts should be numbered consecutively and filed for reference purposes.

The totals of the various analysis columns are posted at the end of the period (week or month) to the debit of the relative accounts in the Nominal or Private Ledger, thus saving a considerable amount of time as compared with the alternative method of posting each item separately.

The Ledger Column is used to record expenditure which cannot be grouped under the other headings and which requires posting to a separate account in the Ledger. This column can also be used to record the payment of an account in the Bought Ledger should the smallness of the amount not warrant the drawing of a cheque. A Folio Column is provided to record the ledger reference.

RULING

Printing and Stationery.	Postage.	Repairs and Renewals.	Sundry Office Exes.	Heat, Light, Cleaning.	L. Fol.	Ledger.
£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.		£ s. d.
1 5 0	1 10 0	3 17 6			31	10 8
			2 6	1 5 0		
£1 5 0	£1 10 0	£3 17 6	2 6	£1 5 0		10 8
N.L.21	N.L.22	N.L.23	N.L.3	N.L.9		

THE IMPREST SYSTEM

The Imprest system of keeping the Petty Cash is usually adopted so as to afford a guide to the amount of petty cash spent. The method is very simple. The petty cashier is given a certain float on which to work, say £10, and when this sum is nearly spent, a further sum is given to bring the float up to the original amount of £10, so that at any moment of time the petty cashier can be called upon to produce cash or vouchers to the imprest amount of £10. In the illustration the amount of £8 12s. 2d. was spent during the week and on the first day of the following week a cheque for the same amount was drawn and the proceeds handed over to the petty cashier, thus bringing the float up to £10 again, as shown.

In connection with the conduct of the petty cash, the inadvisability of placing a low-paid junior employee in charge of the petty cash should be considered. The keeping of the petty cash is responsible work involving the constant handling of cash, and the temptation afforded to a low-paid employee is obvious. Most cases of petty cash defalcations which have come to the author's notice during audit would probably never have occurred if the person in charge had been a senior employee, or the work had been carried out under proper supervision.

Chapter III

THE SUBSIDIARY BOOKS

As mentioned in Chapter I, the old method of journalising every business transaction separately has given place to the modern method of classifying or grouping entries according to their nature in separate journals or day books prior to the posting of the items to the relative accounts in the Ledgers.

The cash transactions have been dealt with in the previous chapter, where it was shown how the cash items are classified in the cash books. We will now deal with transactions not involving the immediate passing of cash.

PURCHASES DAY BOOK

In a business which involves the buying and selling of goods, the Purchases Day Book is an indispensable part of the book-keeping system, unless the business is of such a nature that all purchases are paid for immediately they are received and no credit is required. In such cases the entries are made on the payments side of the Cash Book and posted direct to the Purchases Account in the Private or Nominal Ledger.

For the purposes of this chapter we will assume that we are dealing with the normal business which requires the usual monthly terms. It will, therefore, be necessary to have a Purchases Day Book of suitable form for the purpose of recording the details of the goods bought. These details are obtained from the invoices after they have been checked with the goods received.

Generally speaking there are two methods of keeping the Purchases Day Book. Under the first method the items entered are purchases pure and simple, i.e., goods bought in raw or manufactured state for resale. Under the second method the Purchases Day Book is used, not only to record the purchases, but also expenses of the business, as explained on pages 12 and 13.

The question which is the better method will depend upon the nature and size of the business, and no hard-and-fast rule can be laid down. Both methods will be explained, and the reader must decide which is the more suitable to the business with which he is connected.

The following is a simple ruling of a Purchases Day Book used to record purchases only :

PURCHASES DAY BOOK

Date.	Inv. No.	Name.	L/F	Details.			Total.		
19—				£	s.	d.	£	s.	d.
Jan. 2	1	M. Brown, Ltd.		35	4	5			
" 4	2	" " "		41	7	8			
" 16	3	" " "	10	34	7	6			
" 3	4	J. Oslo & Co.		11	8	7	110	19	7
" 15	5	" " "		54	3	2			
" 17	6	" " "		28	8	6			
" 31	7	" " "	14	33	4	1	127	4	4
" 10	8	O. Richards		18	4	8			
" 20	9	" " "	31	3	17	5	22	2	1
							£260	6	0
							N.L.20		

These details are entered up, usually monthly, from the invoices, and the total owing to each concern agreed with the statement received at the end of the month. It should be remembered that any trade discount allowed should be deducted from the invoices before they are entered in the Purchases Day Book. Cash discount should not be deducted as this is dealt with when payment is made and entered in the Cash Book.

One Purchases Ledger has been assumed in the example. Readers are referred to Chapter V for a suitable Purchases Book ruling in cases where more than one Purchases Ledger is in use. The method of dividing the purchases ledgers where the volume of accounts justifies is recommended so that the accuracy of each ledger may be proved separately at balancing time on the lines indicated in Chapter V.

The monthly totals of goods supplied by the individual firms are posted to the credit of the respective personal

PURCHASES AND EXPENSES

Date.	Inv. No.	Name.	L/F.	Details.	Total.
19—				£ s. d.	£ s. d.
Jan. 2	1	Appleton Bros. : Sundry Purchases		30 11 6	
" 8	2	" "		11 4 8	
" 17	3	" "		5 7 4	
" 31	4	" "	8	14 5 8	61 9 2
" 4	5	M. Brown, Ltd. : Sundry Purchases		67 8 3	
" 10	6	" "		32 1 7	
" 22	7	" "	10	11 3 9	110 13 7
" 31	8	A. Dean : Rent	6		25 0 0
" 31	9	Ealing Electric Co. : Electric Light	12		7 8 0
" 10	10	H. James : Repairs to Roof		3 8 2	
" 13	11	" to Boiler	34	7 10 0	10 18 2
" 24	12	Letterpress Co. : Stationery	23		1 8 2
" 28	13	Weber & Co. : New Safe	8		25 0 0
					<u>£241 17 1</u>

accounts in the Purchases Ledger, whilst the total of the Purchases Day Book is posted, usually monthly, to the debit of the Purchases Account in the Private or Nominal Ledger, thus completing the double entry.

Theoretically, a description of the goods should be entered in the Purchases Day Book and any trade discounts allowed shown as a deduction. It is submitted, however, that unless there are special circumstances, the writing out in the Purchases Day Book of a description of the goods, as shown by the invoices, is a waste of time and serves no useful purpose where the invoices are numbered and properly filed for reference when necessary. The Invoice Number Column shown in the illustration records the consecutively numbered invoices.

Where there is more than one department in a business, it is advisable to divide the purchases as between the depart-

DAY BOOK

Purchases.	Rent and Rates.	Heating, Lighting, and Cleaning.	Repairs and Renewals.	Printing, Stationery, and Tel.	L/F.	Sundries.
£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.		£ s. d.
61 9 2						
110 13 7						
	25 0 0					
		7 8 0				
			10 18 2			
				1 8 2		
					N.L.41	25 0 0
£172 2 9	£25 0 0	£7 8 0	£10 18 2	£1 8 2		£25 0 0
N.L.9	N.L.20	N.L.24	N.L.20	N.L.38		

ments, and this can be done quite simply by using a purchases book with extension columns to accommodate the items referring to the respective departments. This method will be explained in detail in Chapter XV.

PURCHASES AND EXPENSES DAY BOOK

A practical ruling is shown where the second method is adopted, i.e., the inclusion of expenses in the Purchases Day Book.

The analysis columns shown in the example will vary in number and description according to the requirements of the particular business.

The posting to the credit of the personal accounts in the Bought Ledger follow the usual principles and the totals of the

analysis columns will be posted to the debit of the relative accounts in the Nominal or Private Ledger. The Sundries Column will be found useful to record occasional expenditure which does not warrant a separate analysis column.

As previously stated, the particular system adopted will depend upon the nature and size of the business. The method of restricting the entries to purchases only will be quite suitable in a small business where the expenses are not large in number and are paid regularly. In a business where there is a large number of expenses payments, or where the expenses are not paid regularly, there may be a risk of accounts being mislaid and payment overlooked. In such cases the inclusion of the expenses in the Purchases Day Book is recommended.

In businesses of an operating nature, the Purchases Day Book becomes an Expenses Day Book and as such should be used to record the expenses on the lines of the last illustration. The columns would be headed with the various expenses of a recurring nature, and a Sundries Column is suggested for the purpose of recording those items which do not warrant a separate analysis column.

RETURNS OUTWARDS DAY BOOK

(Purchases Returns)

In the majority of businesses credits are claimed from time to time from suppliers for goods, cases, and packages returned, and for sundry other allowances. These credits are recorded usually in a Returns Outwards Day Book. Where the items are few in number, a separate page in the Purchases Day Book at the end of the month's purchases may be used, in which case the page should be headed "Credits" in red ink so that the entries cannot be confused with the Purchases.

The ruling of a Returns Outwards Day Book will follow that of the Purchases Day Book, and the columns will be headed accordingly. An illustration is, therefore, not shown.

The separate items will be posted to the debit of the personal accounts in the Purchases Ledger and the monthly totals column posted to the credit of Purchases Returns Account or direct to the credit of the Purchases Account in the Nominal or Private Ledger, thus completing the double entry.

If expenses are put through the Purchases Book and credits subsequently received, the monthly totals of the various analysis columns will be posted to the credit of the respective expenses accounts in the Nominal or Private Ledger.

SALES DAY BOOK

It has already been explained how cash sales are grouped together in a Cash Sales Book, Summary, or Till Rolls, and posted in total to the Cash Book. In the same manner the sales of goods on credit require to be recorded and conveniently grouped for subsequent posting to the ledgers.

The unreliable practice of charging amounts direct to customers' accounts in the Ledger from the original orders or other odd pieces of paper is strongly condemned. The Sales Day Book has been conceived as a book of first entry to record convenient details of the credit sales which should be promptly entered therein before posting the amounts to the ledger accounts.

There are many types of Sales Day Books in use, varying from loose sheets used in conjunction with mechanical accounting machines to a simple single-column cash ruling contained in a cheap exercise book.

An illustration is given of the Sales Day Book in its simplest form for use when the volume of transactions is small.

SALES DAY BOOK

Date.	Name.	Particulars.	L/F.	Details.	Total.
				£ s. d.	£ s. d.
19— Jan. 2	C. Oliver	240 Tms of Assorted @ 19/6 per doz. 120 G e n o a Cakes @ 16/- per doz.		19 10 0 8 0 0 27 10 0	
„ 10	M. Bradbury	Less 10 per cent. Trade Discount 12 cwt. Broken Mixed @ 50/- per cwt. Less 5 per cent. Trade Discount	24 16	2 15 0 30 0 0 1 10 0	24 15 0 28 10 0

N.L. 12 £53 5 0

One Sales Ledger has been assumed in the example. Readers are referred to Chapter V where a suitable Sales Day Book

ruling is shown for use in cases where more than one Sales Ledger is required.

The individual totals are posted to the debit of the customers' accounts in the Sales Ledger and the periodical sales totals posted to the credit of the Sales Account in the Nominal or Private Ledger, thus completing the double entry.

The type of Sales Day Book depends largely upon the system of invoicing goods to customers. Space does not permit reference to the various invoicing systems apart from observing that the "Copy Invoice" system may prove a great saving of time. Under this method a carbon copy is taken of each invoice and the copies adapted so as to form a Day Book. The time normally involved in writing up the particulars of invoices in the ordinary form of Day Book is therefore saved.

The invoices and the copies may be contained in a bound Invoice Book. The invoices with perforated edges are taken out and sent to the customers and the carbon copies left in the book to form the Sales Day Book.

The author finds that this simple system is successful in practice where the nature and size of the business permit, and an illustration of this form of Day Book is shown on page 25.

The invoice totals are extended daily on the carbon copy to the Totals column and posted to the debit of the individual customers' accounts in the Sales Ledger. The Totals column is added and posted in weekly or monthly totals to the credit of the Sales Account in the Nominal or Private Ledger.

Where the sales accounts are divided between more than one ledger, it is advisable to use separate invoice books for each ledger, if the sectional balancing system explained in Chapter V is to be carried out. Separate invoice books also enable the posting work to be divided between the clerks employed. The alternative is to have the necessary number of extension columns ruled to the right of the Totals columns shown in the example, but this cannot be conveniently arranged where there are more than two Sales Ledgers.

In some businesses the volume of the transactions is too heavy to allow the writing of the invoices by hand and the typewriter is used to make out the invoices and the carbon copies. If the copy invoices are adapted for use as the Sales Day Book, they should be numbered consecutively to avoid any being mislaid. At the end of the day the copy invoices are sorted and bound up together in suitable groups for posting to the debit of the personal accounts in the Sales Ledgers. In order to ascertain the total sales for posting to the credit of

COPY INVOICE BOOK
(adapted for use as a Sales Day Book).

These columns appear on carbon copy only.

Perforated Edge.	No. 1.	Jan. 2, 19—		Totals.	L/F.
	Barnum Supplies, Ltd.,			£ s. d.	
	Barnstaple.				
	24 Rich Assorted @ 26/- per doz.	£ s. d.			
	12 Thin Lunch @ 17/6 per doz.	2 12 0			
		17 6			
		3 9 6			
	Less 10 per cent. Trade Discount	6 11			
		3 2 7		3 2 7	50
	No. 2.	Jan. 2, 19—			
	J. Atkins,				
	Reading.				
	36 Genoa Cakes @ 18/- per doz.	£ s. d.			
	1 cwt. Broken Mixed @ 50/-	2 14 0			
		2 10 0			
		5 4 0			
	Less 5 per cent. Trade Discount	5 2			
		4 18 10		4 18 10	43
	No. 3.	Jan. 3, 19—			
	L. Stoneham,				
	Wokingham.				
	48 Jubilee Assorted @ 5/6 per doz.	£ s. d.			
		1 2 0		1 2 0	92
				c/f £9 3 5	

the Sales Account, summaries of the totals are prepared for each group and a total summary for the whole of the groups.

Where the volume of the transactions justifies, accounting machines may be profitably employed and readers interested are recommended to pay a visit to the leading accounting machine makers, who will gladly demonstrate and recommend suitable machines and systems.

RETURNS INWARDS DAY BOOK
(Sales Returns)

The Returns Inwards or Sales Returns Day Book is necessary for the purpose of recording sundry credits allowed to customers

in respect of goods, cases, and packages returned and to record other credit adjustments required to be made from time to time. These credits should never be recorded direct in the Sales Ledgers, but entered in the first place in the Returns Inwards Day Book, and thence posted to the Ledgers.

Being the contra to the Sales Day Book, the ruling and method of recording in the Returns Inwards Book will follow that used in connection with the Sales Day Book. Specimen rulings are, therefore, not shown. Carbon-copy Credit Notes may be used to form the Returns Inwards Book as in the case of the Sales Invoices.

The individual items are posted to the credit of the relative customers' accounts in the Sales Ledgers and the periodical totals posted to the debit of the Returns Inwards Account or direct to the debit of the Sales Account in the Private or Nominal Ledger.

BILL JOURNALS

The use of Bills of Exchange and the various terms connected with them are assumed to be known, and the following practical explanations of book-keeping records and Bill transactions have been written for the guidance of readers engaged in those trades in which the Bill of Exchange is used.

Where the number of Bill transactions is small, the entries may be separately journalised in the Journal Proper which is explained later in this chapter. When Bill transactions are frequent, it is necessary to consider special journals to record the primary entries prior to posting to the Ledger. The use of a special journal results in a considerable saving of time by posting one aspect of the double entry in total—the feature common to all the special journals used in modern book-keeping. Quite apart from this advantage, the Bill Journal is usually ruled to include certain statistical information, such as the names of persons in whose favour a bill is drawn, where the bill is payable, period of the bill, and the due date, etc.

BILLS PAYABLE

When a bill is accepted an entry should be made immediately by the acceptor in a Bills Payable Journal or Book, a specimen ruling of which is shown on page 28.

The individual items are posted to the debit of the personal accounts of the Drawers, and the total of the bills accepted for the period (month or quarter) is posted to the credit of the

Bills Payable Account in the Private or Nominal Ledger, thus completing the double entry. In effect, the creditors' accounts are treated for book-keeping purposes as if the amounts have been paid, and transfers are made of the amounts owing to the credit of the Bills Payable Account, representing the obligation of the business to meet the bills at maturity.

A bill is usually presented to the bank of the Acceptor for payment and, when paid, the transaction is shown as a payment in the Bank Pass Book of the Acceptor as in the case of a cheque being met. The payment will be recorded on the payments side of the Cash Book and posted to the debit side of the Bills Payable Account in the Private or Nominal Ledger.

The author has found in practice that it is very convenient to have a Bills Payable Diary when the number of bills payable is considerable. This book does not form part of the double-entry book-keeping, but is of a memorandum nature. Particulars of the bills accepted are entered in order of the date on which the bills become due, and serve the useful purpose of bringing to the notice of the proprietors of the business the amounts due for payment during any particular week or month, so that the necessary financial provision can be made to meet the bills.

BILLS RECEIVABLE

The method of recording entries of Bills Receivable is similar to that of Bills Payable, except, of course, that the postings to the Ledger are reversed.

When a Bill Receivable is acquired by the business, entries are made immediately in the Bills Receivable Journal or Book, an example of which is shown on page 28.

The individual entries are posted to the credit of the accounts of the customers from whom the bills were received, and the periodical totals of the Bills Receivable Book are posted to the debit of the Bills Receivable Account in the Private or Nominal Ledger, thus completing the double entry.

The effect of these entries is to transfer the original debit of the customer's account to the debit of the Bills Receivable Account. When the bill is paid into the bank for collection an entry will be made on the receipts side of the Cash Book and the amount posted to the credit of the Bills Receivable Account in order to cancel the original transfer made to that account when the bill was received. On the due date of the bill the bank will collect and the amount will be credited in the Pass Book.

BILLS PAYABLE

Date.	No. of Bill.	Drawer.	In whose favour drawn.	For whose account accepted.
19—				
Jan. 1	20	Day & Co.	Day & Co.	Day & Co.
„ 12	21	Elkin Bros.	G. Clark	Elkin Bros.
„ 27	22	M. Brown, Ltd.	D. Rose	M. Brown, Ltd.

BILLS RECEIVABLE

Date.	No. of Bill.	Acceptor.	Drawer.	From whom received.
19—				
Jan. 2	3	Max Bros.	T. Knight	T. Knight
„ 10	4	Reeves & Co. Ltd.	Selves	Reeves & Co. Ltd.
„ 20	5	S. Lainsbury	T. Vivian	M. Bradbury

The balance on Bills Receivable Account will therefore equal the total value of unmatured bills at any time.

In the unfortunate event of the bill not being met, the bill will be debited in the Bank Pass Book, and the original entry made on the receipts side of the Cash Book must be reversed by entering the amount on the payments side and debiting the sum to the account of the defaulting debtor. Any charges incurred will also be debited to the debtor's account from the Cash Book.

The phrase "discounting a bill" is probably already known to readers and a short explanation of the necessary book-keeping entries is given.

Bill discounting is usually carried on by the bankers of the business, who simply advance the face value of the bill, less a charge for interest which varies in rate according to the general money conditions prevailing at the time and the financial standing of the parties to the bill.

When the bank advances the value of the bill, the amount is

JOURNAL (OR BOOK)

Where payable.	Dates of Bills.	Period.	Due dates.	L/F.		Remarks.
London	Jan. 1	3 mos.	April 4	18	£ 250 0 0	
"	" 12	2 "	March 15	43	50 10 0	
"	" 27	4 "	May 30	20	25 0 0	
					<u>£325 10 0</u>	
					N.L.12	

JOURNAL (OR BOOK)

Where payable.	Date of Bill.	Period.	Due dates.	L/F.		Remarks.
Barclays, Moorgate	Dec. 31	2 mos.	March 3	40	£ 176 10 0	
Midland, Reading	Jan. 8	4 "	May 11	32	50 7 6	
Lloyds, Slough	" 17	3 "	April 20	10	53 10 0	Discounted with Bank do.
					<u>£280 7 6</u>	
					N.L.26	

credited to the banking account of the business and an entry is required on the receipts side of the Cash Book. This amount is posted to the credit of the Bills Receivable Account in the Private or Nominal Ledger just as if the bill were met at maturity in the ordinary way.

The interest or discount charged by the bank is entered as a debit in the Pass Book and requires to be entered on the payments side of the Cash Book. This amount is posted to the debit of Discounting Charges Account in the Private or Nominal Ledger as an expense of the business, and does not feature in the customer's or Bills Receivable Account.

JOURNAL PROPER

Explanations have now been given regarding the separate or special journals used for the purpose of grouping or marshalling transactions involving cash received and paid, purchases and purchases returns, sales and sales returns, bills receivable

and bills payable. It was explained that these special journals were introduced into modern book-keeping systems in order to group items of a like nature conveniently, so that posting to the ledgers might be facilitated.

Before these modern methods were evolved, all transactions were journalised separately in the Journal. The Journal, now usually known as the Journal Proper, is still used to record those transactions which cannot be classified in the special journals. These transactions include entries required to open and close a set of books, transfers from one account to another for the purpose of correcting errors or making adjustments at balancing time, and for any other items which cannot be passed through the other subsidiary books.

Quite often insufficient use is made of the Journal Proper, and there is a tendency to make direct transfers and adjustments as between ledger accounts. This practice is frequently the cause of annoying errors and is to be deprecated.

The passing of the entries through the Journal not only has the advantage of setting out in a convenient order the sums involved for posting to the Ledgers, but also permits fuller written narratives of the entries being given in the Journal than it is possible to show in the limited space provided in the Ledger.

Explanations of entries necessary to open and close a set of books and adjustments required at balancing time will be found in later chapters. At this stage some of the more general transfer entries will be explained so that the reader may grasp the principles involved.

Let us assume that goods to the value of £20 10s. 6d., ordered and dispatched to J. Brown of Exeter, have been charged to C. Brown of Honiton in error, and that the mistake was discovered and corrected on January 6th. The necessary entry to correct the mistake follows :

		<i>Dr.</i>			<i>Cr.</i>			
		L/F	£	s.	d.	£	s.	d.
19—								
Jan. 6	J. Brown (of Exeter) • Dr.	24	20	10	6			
	To C. Brown (of Honiton)	61				20	10	6
	(Being goods sent to J. Brown of Exeter, but incorrectly posted to the debit of C. Brown, Honiton, and now transferred.)							

The reader will observe that a simple double cash ruling only is required, the left-hand column for debits and the right-hand for credits. In this example J. Brown's Account is debited with the value of the goods supplied and C. Brown's Account credited in order to cancel the original debit posted to the account of the latter in error.

The entries in the Journal are folioed in the usual manner and the entries in the Ledger referenced with the Journal folio. As the Journal is used to record transactions of diverse natures, it will be appreciated that a short written explanation or narrative of the transaction is necessary.

Another example follows : Let it be assumed that amounts owing by certain customers have proved to be irrecoverable and it has been decided to transfer the amounts to Bad Debts Account in the Nominal or Private Ledger on December 31st, a special Bad Debts Journal not being kept. The necessary entries (assuming names and amounts) would be :

		<i>Dr.</i>			<i>Cr.</i>			
19—		L/F	£	s.	d.	£	s.	d.
Dec. 31	Bad Debts	Dr.	N L.34	13	6	0		
	To Sundries :							
	J. Ridd . . .		32			2	7	6
	B. Oliver . .		43			3	10	0
	H. Caswell .		14			7	8	6
	(Being irrecoverable amounts due from sundry customers and now transferred to Bad Debts Account.)							

The total of £13 6s. is debited to Bad Debts Account in the Nominal or Private Ledger and the individual amounts posted to the credit of the personal accounts of the defaulting debtors in the Sales Ledger, in order to cancel the original debits made when the goods were supplied.

Another Journal entry frequently met with in practice relates to the buying of machinery or vehicles on credit terms. Let us assume that a Motor Van was purchased on January 1st for £260 (including interest £10), through the H.P. Finance Co. Ltd., payable as to £60 down and the balance of £200 in 12 equal monthly instalments. The necessary Journal entry follows :

this account with a debit balance of £40 representing the loss on the sale. This loss would require transferring to Loss on Motor Van Account, through the medium of an entry in the Journal, as shown on the previous page.

These entries indicate that the loss of £40 is transferred to Loss on Motor Vans Account by debiting that account and crediting Motor Vans Account. This loss is transferred to the debit of the Profit and Loss Account at the end of the financial year. So far as the old van is concerned, the original debit of £60 has now been cleared by the posting to the credit of Motor Vans Account of the loss of £40 and the cash received of £20.

Space does not permit of further examples at this stage, but the explanations given should enable readers to understand the use and functions of the Journal Proper and assist them to apply the principles in practice.

Chapter IV

SALES AND PURCHASES LEDGERS

THE reader has so far been introduced to the usual subsidiary books or books of first entry used in modern book-keeping systems. The primary entries having been suitably classified in these books, the process of posting to the ledgers will now be considered.

In the olden days all the ledger accounts were contained in one ledger. This was probably quite satisfactory at the time, but as trade developed it became necessary to increase the number of ledgers. It was found convenient to enter the Sales Ledger Accounts in one ledger or group of ledgers, the Purchases Ledger Accounts in another ledger or group of ledgers, and the Impersonal Accounts in a separate Private or Nominal Ledger.

In the case of companies, the statutory provisions of Section 147 of the Companies Act, 1948, must be observed. This section states *inter alia* that every company shall cause to be kept proper books of account with respect to all sales and purchases of goods by the company and the assets and liabilities of the company. This section also states that this obligation will not be fulfilled if there are not kept such books as are necessary to give a true and fair view of the state of the company's affairs and to explain its transactions.

There is a wide variety of ledgers available to-day, with special types designed for the requirements of particular businesses. Generally speaking, they may be divided into three classes: (a) the ordinary bound type, (b) the loose-leaf type, and (c) the card type. The best form of ledger to use will largely depend upon the nature and volume of the transactions, the amount of information to be given, and the degree of control or check on the work of the book-keepers.

Whilst loose-leaf and card ledgers can be recommended for Sales and Purchases Ledgers, it is essential that their use should be accompanied by an efficient check on the issue of fresh ledger leaves or cards and that the keys of the ledgers or card

trays should be kept by a responsible official to avoid irregular withdrawal or insertion and to comply with Section 436 of the Companies Act, 1948.

The leaves or cards are usually arranged alphabetically and numerically. For instance, the customers whose names commence with A will be numbered A1, A2, A3, and so on, and the names listed on a separate index for each letter.

SALES LEDGERS

Subject to the observations made, the loose-leaf or card ledger is recommended for the purpose of recording customers' accounts. The bound type of ledger does not possess that advantage of elasticity which loose leaves or cards offer. Customers' accounts usually vary in size and identity which cannot be accurately estimated at the time the bound ledger is opened. The simplicity of inserting fresh leaves or cards as and when required, and taking out full or dead leaves, is a distinct and valuable advantage and preserves the continuity of the ledgers.

Whatever type or number of Sales Ledgers are in use, the same double-entry principles apply and the posting rules are identical, namely, that the invoice prices of all goods supplied or services rendered are debited and cash received and allowances made are credited to the customers' accounts. Bills Receivable from the Bills Receivable Book are also posted to the credit of the customers' accounts.

An example of a Sales Ledger Account follows :

<i>Dr.</i>				M. BRADBURY				<i>Cr.</i>			
19—			£	s.	d.	19—			£	s.	d.
Jan. 1	To Balance b/fd.	✓	19	0	6	Jan. 8	By Cash	20	18	11	0
" 10	" Goods	37	28	10	0	" 8	" Discount	"		9	6
" 28	" do.	59	54	10	0	" 12	" Empties re-				
							turned	63	1	0	0
						" 20	" Bill Receiv-				
							able	2	53	10	0
						" 31	" Balance c/d.	✓	28	10	0
			£102	0	6				£102	0	6
Feb. 1	To Balance b/d.	✓	28	10	0						

This example does not call for detailed explanation, the books of original entry from which the items are posted having already been explained. The cross-referencing of the folios is important, particularly where there are a number of

books involved, and the point is mentioned because this elementary rule is often not observed and time is wasted when checking the entries at audit time. Another feature is the ruling off of the ledger accounts and the bringing down of the balances. The slipshod method of leaving open entries or inserting pencil figures until the account is paid should be avoided; the accounts should be properly ruled off at the end of each month and the balance brought down as shown in the example. This work can be quite easily carried out when the monthly statements are being prepared.

It is not possible in this treatise to deal fully with the question of Internal Check as a means of preventing or discovering irregularities or errors on the part of those responsible for the keeping of the books. It is, however, pertinent to mention at this stage certain rules which should be carried out if the circumstances permit and the necessary staff is available.

The persons entering up the subsidiary books, including the Cash Books, should not be given the task of posting from those books to the Sales Ledgers. It is also inadvisable to leave the work of writing out and mailing the monthly statements of account in the hands of the clerk in charge of the ledger containing those accounts. If this cannot be avoided, a different clerk or responsible official should carefully check the statements and arrange for them to be mailed at once.

In small offices the carrying out of these rules may prove to be impossible, but the recommendations are worthy of mention and should be observed in as great a degree as circumstances permit.

COLUMNAR SALES LEDGERS

Where a single commodity or group of commodities is supplied the book-keeping work can be reduced and simplified by the use of a Columnar Sales Ledger. This type of ledger is extensively used in such trades as Dairy, Bakery and Confectionery, Gas, Electricity, and Water undertakings, etc. In these businesses a large number of customers are dealt with, each requiring a separate account of identical form.

A specimen ruling of a Columnar Ledger suitable for use in the business of a Baker and Confectioner is shown, and this ruling may be varied for use in the trades mentioned above or undertakings of a similar nature. The transactions are entered horizontally across the page instead of under one another, and the reader will appreciate that this type of ledger can accommodate a much larger number of accounts than could be shown in the same space in the ordinary form of ledger.

Referring to the illustration : Column 1 records the balance brought forward from the previous period (in the case illustrated the previous week). Column 2 is used to record the reference to the book of each customer and will be found useful in calling over from the customers' books to the ledger. Column 5 records the value of goods supplied during the week and, when added to the amount owing (if any) in column 1, gives the total amount due from each customer. Column 8 records the cash received as shown in the Cash Book, the folio of the Cash Book being shown in column 7. In most trades or undertakings credits are given for discount or allowances, and these are posted from the Discount Column in the Cash Book, or in the case of allowances from the Allowances Journal, to column 10 and the folio of the Cash Book or Allowances Journal inserted in column 9. The amounts in columns 8 and 10 are added and the total recorded in column 11. We now have the total due as shown in column 6 and the total cash received and credits allowed in column 11; by simple subtraction the balance owing is ascertained and inserted in column 12. If the size of the book permits columns 5 to 13 can be repeated across the page, column 13 forming the balance owing at the beginning of the new period.

When the page is completed and totalled a useful arithmetical check can be obtained, inasmuch as the totals of columns 1 and 5 must equal the total of column 6, whilst the totals of columns 8 and 10 must equal the total of column 11. By subtracting the total of column 6 from the total of column 11 the figures must agree with the total of column 12.

Another valuable advantage of this type of ledger is that the Sales Day Book may be entirely dispensed with as the total sales for the week or period can be ascertained by summarising the totals of column 5 on the pages referring to the week or period. The book-keeping work is thereby considerably reduced, whilst the facility of arithmetical check, as explained above, is a factor of considerable importance. As previously stated, however, this form of ledger can only be used in certain businesses and where an analysis of the classes of goods sold is not required.

The Columnar Ledger in a different form is used extensively in the Hotel trade. In this case the accounts are arranged vertically instead of horizontally, the details of the debits for goods supplied or services rendered being shown on the extreme left-hand side instead of across the page. The addition of each individual account is made vertically instead

BAKER AND CONFECTIONER'S

Round No.

Week ending

1	2	3	4	5	6
Balance owing.	Ref. No.	Name.	Address.	Week's Supply.	Total Due.
£ s. d.				£ s. d.	£ s. d.
5 6	42	Hunt	19, St. Peter's Hill	15 0	1 0 6
1 10 0	43	East	46, Darrell Road	18 0	18 0
2 0 0	44	Hill	2, Albert Road	7 6	1 17 6
	45	Hope	11, Highmoor Road		2 0 0

Further accounts follow,

£48 7 6			£62 8 4	£110 15 10
---------	--	--	---------	------------

HOTEL VISITORS

Folio.....

	Room No. 1.	Room No. 2.	Room No. 3.	Room No. 4.
<i>Debits.</i>	£ s. d.	£ s. d.	£ s. d.	£ s. d.
Balance brought forward .	2 10 0			3 7 6
Apartments	15 0	15 0	10 6	12 6
Breakfast	3 6		3 6	3 6
Lunch				4 0
Tea and Coffee	6			
Dinners	5 0		5 0	5 0
Suppers		3 0		
Wines	12 6			10 0
Spirits and Liqueurs		1 6		
Ale, Stout, etc.			6	
Minerals				
Cigars and Cigarettes	2 0			
Newspapers	6			
Postage				2
Laundry				2 0
Attendance				5 0
Baths	1 0			
Fires			1 0	
Sundries				
Total	£4 10 0	19 6	£1 0 6	£5 9 8
<i>Credits.</i>				
Cash received	4 9 0			
Allowances	1 0			
Ledger account				5 9 8
Balance carried forward		19 6	1 0 6	
Total	£4 10 0	19 6	£1 0 6	£5 9 8

COLUMNAR SALES LEDGER

7	8	9	10	11	12	13
Fol.	Cash Received	Fol.	Credits (for dis- counts and allow- ances).	Total Cash and Credits.	Balance owing.	
	£ s. d.		£ s. d.	£ s. d.	£ s. d.	
4	1 0 0	4	6	1 0 6		Whole set of columns (ex- cept "Bal- ance owing" column) can be repeated here if size of Ledger per- mits.
6	1 0 0	10	2 0	2 0	16 0	
7	10 0	6	9	1 0 9	16 9	
				10 0	1 10 0	

each occupying one line.

£72 3 1	£4 3 0	£76 6 1	£34 9 9
---------	--------	---------	---------

LEDGER

Monday..... 19....

Room No. 5.	Room No. 6.	Daily Total.	Folio.	
£ s. d.	£ s. d.	£ s. d.		
15 8		6 13 2	12	Brought forward
7 6	10 0	3 10 6	20	Apartments
3 6		14 0	28	Breakfast
		4 0	31	Lunch
		6	36	Tea and Coffee
		15 0	40	Dinners
	3 0	6 0	50	Suppers
		2 6	53	Wines
	2 6	2 6	60	Spirits and Liqueurs
		1 6	62	Ale, Stout, etc.
	6	1 0	64	Minerals
		2 0	69	Cigars and Cigarettes
		6	72	Newspapers
		2	78	Postage
		2 0	81	Laundry
		5 0	85	Attendance
1 0		2 0	88	Baths
		1 0	93	Fires
	1 0	1 0	101	Sundries
£1 7 8	17 0	£14 4 4		Total
1 7 0		5 16 0	58	Cash received
8		1 8	105	Allowances
	17 0	5 9 8	10	Ledger account
		2 17 0	14	Balance carried forward
£1 7 8	17 0	£14 4 4		

of horizontally. The credits are shown in a separate section below the debits.

For the guidance of those engaged in the Hotel trade a specimen ruling is shown. The upper part of the page recording the debits is divided from the lower, recording the credits, and the balance carried forward to the next day, by a thickly ruled line. The cash received is posted from the Cash Book and any allowances made are posted from the Allowances Journal.

A fresh page is used each day, the balances being carried forward at the close of business every night. The ruling will conveniently accommodate up to 24 rooms according to the width of the ledger. Where the rooms exceed this number it is advisable to use additional ledgers.

This type of ledger also possesses the advantage of dispensing with a Day Book, the totals for posting to the credit of the accounts in the Nominal Ledger being ascertained by summarising the totals shown in the Daily Total column.

PURCHASES LEDGERS

The loose-leaf type of ledger is suitable for use as a ledger containing the accounts of suppliers of goods or services. This recommendation is subject to the internal check mentioned in the case of the Sales Ledgers.

The values of goods supplied or services rendered to the business are posted from the Purchases Day Book to the credit of the personal accounts of the suppliers, whilst the cash paid and discounts allowed are posted from the Cash Book to the debit of the personal accounts. Bills Payable from the Bills Payable Book are also debited. Allowances given by the suppliers, e.g., for returns, are posted from the Purchases or Returns Outwards Book to the debit of the ledger accounts.

A simple example of a Purchases Ledger Account is given :

M. BROWN, LTD., HONITON

Dr.			Terms : 2½% monthly.			Cr.				
19—			£	s.	d.	19—		£	s.	d.
Jan. 2.	To Cash	10	47	10	0	Jan. 1. By Balance b/f.	✓	50	0	0
" 2.	" Discount	10	2	10	0	" 31. " Goods	40	110	19	7
" 13.	" Returns	20	3	7	6					
" 27.	" Bills Payable	3	25	0	0					
" 31.	" Balance c/d.	✓	82	12	1					
			£160	19	7			£160	19	7
						Feb. 1. By Balance b/d.	✓	82	12	1

The cross-referencing of the Purchases Ledger accounts with the subsidiary books is again emphasised. The ruling off and balancing of each account should be done monthly and the statement received from each supplier agreed with the balance before a cheque is drawn in payment.

The proper division of the book-keeping work between the clerks for the purpose of ensuring adequate internal check will again depend upon the circumstances and the number of the staff employed. It will be appreciated that the more the work is divided the greater is the check on the arithmetical accuracy and integrity of the clerks.

The recommended system is to arrange for each subsidiary book (including the Cash Payments Book) and the Purchases Ledger to be kept by separate clerks. The cheques should be drawn and agreed with the statements by a responsible official of the business and the cheques with invoices and statements attached submitted to the Secretary or Directors for signature.

The system of stock control is an important factor, and the link between the accounting and stores departments. It is recommended that the invoices should be examined and signed by the store-keeper when the goods have been received, and wherever possible these invoices should be attached to the statements submitted to the official responsible for the drawing of the cheques so that he may verify that the business is only paying for those goods which it has actually received. In order to ensure that the invoices have been checked in detail, it is a good plan to stamp each invoice with a rubber stamp showing such words as: "Prices checked by —"; "Calculations checked by —"; "Additions checked by —"; "Quality approved by —"; "Entered Purchases Book page —." The officials responsible for this work should initial in the spaces provided and the Purchases Book page should be filled in by the clerk who enters the invoices in the Purchases Book.

In large businesses particulars of the goods received are entered by the store-keeper in a Goods Received Book, which is checked by the accounting staff with the invoices received. One of the advantages of this system is that the invoices do not leave the accounting department.

It is, of course, impossible to attain the ideal check in small businesses where probably only one or two clerks are employed. In such cases the responsibility of the Accountant or Secretary is increased, and he should be constantly on the alert and subject the system to such periodical tests as experience proves necessary.

Chapter V

SELF-BALANCING LEDGER SYSTEM

SALES LEDGER

IN Chapter III, dealing with the subsidiary books, the advisability of carrying out a separate check on the arithmetical accuracy of the Sales and Purchases Ledgers was mentioned, especially where more than one ledger is kept. This check is made by means of what is known as the Self-balancing or Sectional-balancing System. Although of greater importance where several ledgers are in use, the system can nevertheless be applied with advantage where only one Sales Ledger is kept.

The Self-balancing System is quite simple in its application and can be carried out easily by the average book-keeper once the method is understood. Judging, however, from the examination papers submitted to the author for correction, it seems that students find difficulty in understanding the principles.

Briefly speaking, the self-balancing principle is simply the summarising in convenient totals of the details posted to the debit and credit of the personal accounts appearing in a particular ledger, and agreeing the balance of the Summary with the total balances of the accounts in that ledger. By this means the ledger is balanced or agreed by itself, apart from the other ledgers of the business.

As a simple example let us assume we have one Sales Ledger containing the accounts of ten customers, and that all the items posted are identical in each case with those shown in M. Bradbury's account illustrated in the previous chapter. In practice such a coincidence of figures would never occur, but the assumption simplifies the understanding of the self-balancing principle.

We shall now group in monthly totals the détails posted to the debit and credit of the ten accounts in a Summary known as the Sales Ledger "Control" or "Total" Account. This account would appear as follows :

Dr.

SALES LEDGER CONTROL ACCOUNT

Cr.

19—			£	s.	d.	19—			£	s.	d.
Jan. 1.	To Balance b/f.	✓	190	5	0	Jan. 31.	By Cash and				
							Discount	20	190	5	0
„ 31.	„ Goods	59	830	0	0	„ 31	„ Returns	63	10	0	0
						„ 31	„ Bills Re- ceivable	2	535	0	0
									735	5	0
						„ 31	„ Balance c/d.	✓	285	0	0
									£1,020	5	0
Feb. 1.	To Balance b/d.	✓	£285	0	0						

Before balancing this Control Account we must list the balances of the ledger accounts in the Sales Ledger. In this case we have assumed for the purpose of illustration that the ten ledger accounts are all the same, and therefore the total of the list of balances will be ten times the balance shown by M. Bradbury's account, namely £285.

The next stage is to balance the Control Account and compare the balance shown with the total of the balances extracted from the Sales Ledger. In the illustration the balance on the Control Account is £285 and agrees with the list of balances. The work of posting to, and balancing, the Sales Ledger is therefore *prima facie* correct under the Self-balancing System.

It now remains to be explained how the totals in the Sales Ledger Control Account are collected together for posting to this account.

The opening debit balance of £190 5s. 0d. is simply the total of the balances on the Sales Ledger as shown by the list of balances taken out on December 31st, which was proved to be correct under the system at the previous balancing. The other debits and credits are the monthly totals shown by the various subsidiary books. For instance, the goods sold debit of £830 is the total of the Sales Day Book for the month of January; the cash received and discount allowed, amounting to £190 5s. 0d., is the monthly total of the Sales Ledger Column in the Cash Received Book; the sales returns is the monthly total as shown by the Sales Returns Book; the bills receivable is the total of the Bills Receivable Book for the month.

The amount of any bad debts written off will be credited in monthly or other periodical totals to the credit of the Sales Control Account. In large businesses a special Bad Debts Journal is generally used, but in smaller concerns, or where the business is fortunate enough to sustain only a small number

of bad debts, the original entries may be made in the Journal Proper and the amounts either taken separately to the credit of the Control Account or conveniently summarised at balancing times.

The frequency with which the Sales Ledger is proved will depend upon the nature and size of the business. In banks, financial houses, and large businesses a daily balance is struck, whilst in other cases a monthly or quarterly balance may be sufficient. In deciding the period, readers are recommended not to leave their attempts to balance the ledgers until the end of the year, when the work of looking for errors, which may have occurred at any time during the year, will be much greater than in the case where a more frequent balance is struck.

The Control Account may be kept in the Private or Nominal Ledger. A better method, however, is to keep a separate Control Ledger (C.L.), especially where there is more than one Sales Ledger in use so that the pages of the Private or Nominal Ledger will not be used up by Control details. The Control Account should be prepared by the Accountant or Secretary when a useful and independent check is kept on the ledger clerk, who produces his list of balances to the Accountant or Secretary for agreement from time to time with the Control Account balance.

It is obvious from reading the foregoing explanations that the advantages of the Self-balancing principle become more apparent when there is more than one Sales Ledger in use. In businesses of any size the Sales Ledger Accounts are so numerous that it is impossible to keep all the accounts in one ledger; some division of the accounts must be made and separate ledgers used, so that the work of posting to the ledgers may be divided between the clerks employed.

The division of the Sales Ledgers may be made in several ways. Generally, the alphabetical division is found convenient. Assuming that the number of accounts justifies two Sales Ledgers, the accounts may be divided as between customers whose names are indexed under letters A to L, and those indexed from M to Z. Where more ledgers are necessary the accounts may be further divided alphabetically. In this question of subdividing, the usefulness of the loose-leaf Sales Ledger will be apparent, particularly where the number of ledgers is increased from time to time. The process is simply one of rearranging the account leaves in new binders and then reindexing.

Another form of classification is in territories or in travellers' zones. For example, the accounts of customers in Devonshire may be kept in one ledger; the customers in Somerset in another ledger, and so on throughout the counties, or group of counties, where the number of customers justifies the method. The Travellers' Zone Method is particularly convenient as it enables the executive to judge the efforts of individual travellers, and when commission is payable calculations of turnover, etc., can be made quite easily.

Space does not permit a description of other methods of dividing the Sales Ledger Accounts; the nature and size of businesses are so diverse that the choosing of a method suitable to a particular business is a task which should be left to the Accountant or Secretary responsible for the planning of the office routine.

The application of the Self-balancing System to a number of ledgers is simply a matter of analysing or dividing the various subsidiary books in use and preparing a separate Control Account for each ledger.

For the purpose of simple illustration, let us assume that there are two Sales Ledgers in use, one for the A-L customers and the other for M-Z customers. The subsidiary books must be ruled to permit an analysis of the entries as between these two ledgers. A suitable form of Sales Journal and Cash Received Book is shown on pages 46 and 47.

The amounts for goods supplied are divided as between ledgers A-L and M-Z by means of the analysis columns shown. The monthly A-L total is taken to the debit of the A-L Control Account and the monthly M-Z total to the debit of the M-Z Control Account.

The cash received is divided between the two ledgers by means of analysis columns in the Cash Received Book. The monthly A-L total is taken to the credit of the A-L Control Account and the monthly M-Z total to the credit of the M-Z Control Account.

The Sales Returns are divided between the two ledgers by a ruling similar to that of the Sales Day Book and posted to the credit of the relative Control Accounts.

The reference C.L. — at the foot of the analysis columns refers to the Control Ledger folio to which the totals have been posted, the entries in the Control Ledger being cross-referenced with the folio of the subsidiary book from which the entries have been posted.

When Bills Receivable are dealt with, the division between

SALES

Date.	Name.	Particulars.	L/F
19— Jan. 2	C. Oliver	240 Tins of Assorted @ 19/6 per doz. 120 Genoa Cakes @ 16/- per doz. Less 10% Trade Discount . . .	M-Z 24
„ 3	M. Bradbury	12 cwt. Broken Mixed @ 50/- per cwt. Less 5% Trade Discount . . .	A-L 16

Dr.

CASH

Date.	Particulars.	Fol.	Details.	Amounts Banked.
19— Jan. 1	To Balance b/f. .	✓	£ s. d.	£ s. d.
„ 2	„ Cash Sales .	12	54 7 6	260 8 6
„ 8	„ M. Bradbury .	A-L 10	18 11 0	
„ 8	„ T. Smith .	M-Z 31	2 12 2	
„ 9	„ Cash Sales .	19		75 10 8
„ 16	„ do. .	27	184 10 8	321 6 4
„ 16	„ J. Williams .	M-Z 28	40 6 0	
„ 16	„ E. Hicks .	A-L 43	19 11 0	244 7 8
				£901 13 2

the Sales Ledgers may be effected by additional rulings in the Bills Receivable Book, or where the number of bill transactions is not large the division may be made by simply making a monthly analysis.

Where a separate Bad Debts Journal is used, it may be ruled with analysis columns for the two ledgers and the monthly or quarterly totals taken to the credit of the relative Control Accounts. If the bad debts are few in number and

DAY BOOK

Details.	Totals.	A-L.	M-Z.
£ s. d.	£ s. d.	£ s. d.	£ s. d.
19 10 0			
8 0 0			
27 10 0			
2 15 0	24 15 0		24 15 0
30 0 0			
1 10 0	28 10 0	28 10 0	
	£53 5 0	£28 10 0	£24 15 0
	N.L.12	C.L.10	C.L.15

RECEIVED

Discount.	Sales Ledgers.		Cash Sales.	Sundries.
	A-L.	M-Z.		
£ s. d.	Cash and Discount. £ s. d.	Cash and Discount. £ s. d.	£ s. d.	£ s. d.
				260 8 6
			54 7 6	
9 6	19 0 6			
3 4		2 15 6		
			321 6 4	
			184 10 8	
2 3 0		42 9 0		
10 6	20 1 6			
£3 6 4	£39 2 0	£45 4 6	£560 4 6	£260 8 6
N.L.36	C.L.10	C.L.15	N.L.2	

the entries made through the Journal Proper, the division between the two ledgers is simply effected by means of an analysis, or each item posted to the credit of the relative Control Accounts as and when the entries are made in the Journal Proper.

Transfers from one Sales Ledger to another will also affect the Control Accounts. Here again, in large concerns a special Transfer Journal may be used, while in other cases the transfers

may be put through the Journal Proper. Whichever method is adopted, the rule to observe is that where the amount is debited to an account in a particular ledger, the figure must also appear on the debit side of the Control Account referring to that ledger. The same rule applies to the credit side, namely a credit to Sales Ledger account must appear on the credit side of the relative Control Account.

Where the number of Sales Ledgers in use is considerable, the entries in the subsidiary books cannot be divided by means of analysis columns. In such cases separate subsidiary books must be used for each of the Sales Ledgers, but the simple principles explained will still apply.

PURCHASES LEDGER

The advantages of the self-balancing principle outlined in connection with the Sales Ledger are equally attractive in dealing with the Purchases Ledger, especially where more than one ledger is in use.

As in the case of the Sales Ledger, the accuracy of the Purchases Ledger is proved by means of a Control Account in which is entered, in convenient totals, the details posted to the debit and credit of the personal accounts appearing in the Purchases Ledger.

The following is an example of a Purchases Ledger Control Account :

<i>Dr.</i>		<i>PURCHASES LEDGER CONTROL ACCOUNT</i>				<i>Cr.</i>	
19—			£	s.	d.	19—	
Jan. 31.	To Cash and Discount	10	286	12	0	Jan. 1.	By Balance b/f.
" 31.	" Bills Payable	3	250	0	0	" 31.	" Goods
" 31.	" Returns Outwards	20	33	15	0		
			570	7	0		
" 31.	" Balance c/d.	✓	189	19	0		
			£760	6	0		
						Feb. 1.	By Balance b/d.
						✓	£189 19 0

The debits and credits of this account are the monthly totals of the items which have been posted in detail to the Purchases Ledger, from the various subsidiary books.

On the Debit side the cash and discount, amounting to £286 12s. 0d., is the total of the Purchases Ledger Column in the

Cash Payments Book. The Bills payable, £250, are taken from the Bills Payable Journal. The Returns outwards, £33 15s. *od.*, is the total of the Returns Outwards Journal.

On the Credit side, the balance of £500 brought forward from the previous month is the total amount owing to the creditors on the Purchases Ledger as shown by the schedule of balances extracted from the Ledger as at December 31st. The goods credited, £260 6s. *od.*, is the total of the Purchases Journal for the month.

Having built up the account from the various subsidiary books, a balance is struck, in this instance amounting to £189 19s. *od.* A schedule of balances on the Purchases Ledger as at January 31st is prepared, and if the total balances of the schedule agrees with the balance shown on the Purchases Ledger Control Account, the posting and balancing of the Purchases Ledger for the month of January is *prima facie* correct.

For the purpose of this example it has been assumed that the Purchases Ledger is balanced and proved monthly. This period is frequently adopted, but in small businesses the balance may be struck quarterly or half-yearly. Unless the number of accounts and postings is small, it is not advisable to leave the proving of the ledger until the end of the year, as the field to be examined in case of errors is much wider than where the ledger is balanced at more frequent intervals.

Where more than one Purchases Ledger is used, the advantages offered by the Self-balancing method makes the system indispensable. As in the case of the Sales Ledger, the method simply involves an analysis of the subsidiary book figures as between the number of ledgers in use.

For the purpose of easy illustration, rulings are shown of a Cheque Payments Book and Purchases Book suitable where two Purchases Ledgers are used. The same methods apply where any number of ledgers are used, although horizontal space available in a convenient-size subsidiary book will restrict the number of rulings to three or four ledgers. Where more than this number of ledgers is in use, separate subsidiary books will be required for each ledger or group of ledgers.

The rulings shown assume that the two Purchases Ledgers are divided as to accounts indexed under letters A–K and L–Z. The alphabetical method of division is usual in connection with the Purchases Ledgers, although other methods, e.g., departmental, territorial, etc., may be found more convenient in certain cases.

CHEQUE

Date.	Particulars.	V	L/F.	Cheque.	Discount.
19—				£ s. d.	£ s. d.
Jan. 3	By M. Brown . .	1.	A-K10	47 10 0	2 10 0
„ 4	„ Wages . .	2.	N.L. 18	28 4 0	
„ 4	„ Petty Cash . .	3.	P.C. 22	3 10 0	
„ 6	„ J. Oslo & Co. . .	4.	L-Z 14	118 15 0	6 5 0
„ 7	„ O. Richards . .	5.	L-Z 31	35 2 0	18 0
				£233 1 0	£9 13 0

N.L.10

PURCHASES

Date.	Inv. No.	Name.	L/F.
19—			
Jan. 2	1	M. Brown, Ltd. . . .	
„ 4	2	„ „ „ . . .	
„ 16	3	„ „ „ . . .	A-K 10
„ 3	4	J. Oslo & Co. . . .	
„ 15	5	„ „ „ . . .	
„ 31	6	„ „ „ . . .	
„ 31	7	„ „ „ . . .	L-Z 14
„ 10	8	O. Richards	
„ 20	9	„ „	L-Z 31

The cash paid and discounts allowed are divided between the two ledgers by means of analysis columns, and the monthly totals of these columns are posted to the debit of the respective Control Accounts.

Where Bills Payable are given they may be divided between the two ledgers by means of analysis rulings in the Bills Payable Book and posted to the debit of the Control Account. Where

PAYMENTS

Bought Ledger.		Private or Nominal Ledger.	Petty Cash.
A-K.	L-Z.		
Cash and Discount.	Cash and Discount.		
£ s. d. 50 0 0	£ s. d.	£ s. d.	£ s. d.
		28 4 0	
	125 0 0		3 10 0
	36 0 0		
£50 0 0	£161 0 0	£28 4 0	£3 10 0

C.L.22

C.L.25

DAY BOOK

Details.	Total.	A-K.	L-Z.
£ s. d.	£ s. d.	£ s. d.	£ s. d.
35 4 5	110 19 7	110 19 7	
41 7 8			
34 7 6			
11 8 7	127 4 4		127 4 4
54 3 2			
28 8 6			
33 4 1			
	22 2 1		22 2 1
18 4 8			
3 17 5			
	£260 6 0	£110 19 7	£149 6 5

N.L. 20

C.L. 22

C.L. 25

the number of bills accepted is small the division may be made by making an analysis at the end of each month.

The Purchases Returns or Returns Outwards entries are also divided between the ledgers by analysis columns in the subsidiary book and taken in monthly totals to the debit of the Control Accounts. The ruling follows that of the Purchases Book illustrated, where the purchases are also divided by means

of analysis columns and the totals taken to the credit of the respective Control Accounts.

Transfers from one Purchases Ledger to another will require to be entered in the Control Accounts. In large businesses a separate Transfer Journal will be necessary, as explained in the case of the Sales Ledgers. In smaller concerns the transfers may be put through the Journal Proper. Whichever method is adopted, the principle to observe is that where the transfer is a debit in, say, ledger A-K, the A-K Control Account must be debited. Conversely the credit in ledger L-Z must appear on the credit side of L-Z Control Account.

The same principle applies where a transfer is made between a Purchases and a Sales Ledger Account. For example, a transfer involving a debit to an account in the A-K Purchases Ledger and a credit to an account in the A-L Sales Ledger to record a contra account transaction will require to be entered on the debit side of the A-K Purchases Ledger Control Account and on the credit side of the A-L Sales Ledger Control Account. The transfer will be made through the Journal Proper or through the Transfer Journal where there is one in use.

Chapter VI

THE NOMINAL OR PRIVATE LEDGER. THE TRIAL BALANCE

IN Chapters IV and V the recording of book-keeping transactions in the personal accounts of customers in the Sales Ledger and the personal accounts of creditors in the Purchases Ledger was explained. The posting of the entries from the Cash Books and other subsidiary books to the Nominal or Private Ledger was referred to in the chapters dealing with those subsidiary books.

This chapter will be devoted to an explanation of the Nominal or Private Ledger and the Trial Balance method of check on the book-keeping.

In some cases it may be necessary for the accountant, secretary, or directors to keep an additional Private Ledger to record details which should not be within the knowledge of the book-keeping staff, such as capital particulars, investments, and certain items of profit and loss. For the purposes of this book, however, one ledger will be assumed and described as the Nominal Ledger.

The function of the Nominal Ledger is to record accounts other than the personal accounts of customers (debtors) and suppliers of goods and services (creditors). The accounts to be found in the Nominal Ledger will thus include those dealing with expenses and gains, assets, capital, debentures, loans, etc. The Sales and Purchases Ledger Control Accounts may also be kept in the Nominal Ledger, but these accounts are more conveniently recorded in a separate Control Ledger as suggested in Chapter V.

At the end of the accounting period, the balances of the accounts in the Nominal Ledger are extracted. These balances are listed on a statement known as the Trial Balance and when agreed, the arithmetical accuracy of the work is proved. Then the final Accounts, i.e., Trading or Manufacturing Account, the Profit and Loss Account, and the Balance Sheet, are prepared on the lines described in Chapter VIII.

The information given in the Nominal Ledger is an indica-

tion as to the trading and financial position of the business, especially if the Profit and Loss Account is shown in detail, and for this reason the ledger is usually kept by a responsible official, such as the Accountant or Secretary, and as a deterrent to the prying mind a lock is frequently fitted.

The ruling recommended is a double-cash one, i.e., two debit columns on the left-hand page and two credit columns on the right-hand page, as shown by the illustration which follows.

The planning of the various account headings will largely depend upon the nature and degree of information required. Adequate subdivision of the usual headings shown in the final accounts is recommended. The practice of grouping items is permissible in the final accounts within limits, but the Ac-

		<i>RENT</i>			
<i>Dr.</i>					
		Fol.	£	s.	d.
19—					
Jan. 1	To Cash—Sch. A tax for year 19—	10			90 0 0
Mar. 31	„ Cash—Office Rent for quarter to date		100	0	0
	Less Sch. A tax	21	90	0	0
June 30	„ Cash—Office Rent for quarter to date	33			100 0 0
Sept. 30	„ do.	42			100 0 0
Dec. 31	„ do.	61			100 0 0
					<u>£400 0 0</u>

		<i>INSURANCE</i>			
<i>Dr.</i>					
		Fol.	£	s.	d.
19—					
Jan. 1	To unexpired amounts b/f.: Comprehensive policy.		25	0	0
	Special Fire policy	✓	6	0	0
June 30	„ Cash—A.I. Comprehensive policy—premium for year to June 30, 19—	33			50 0 0
Sept. 30	„ Cash—X.Y. Insurance Co.—Special Fire policy—premium for year to September 30, 19—	42			8 0 0
					<u>£89 0 0</u>
19—					
Jan. 1	To unexpired amounts b/f.: Comprehensive policy		25	0	0
	Special Fire policy	✓	6	0	0
					31 0 0

countant or Secretary should arrange for his Nominal Ledger to give the greatest possible amount of information as to how the items in the final accounts are made up. The use of a Sundries Account should be avoided as far as possible and an endeavour should be made to bring all items under definite headings.

It is found helpful in practice to arrange the accounts in the Nominal Ledger in the order in which they appear in the final accounts, commencing with the capital, liabilities, and assets shown in the Balance Sheet and following on with the debits and credits of the Trading or Manufacturing and Profit and Loss Accounts.

The posting of the entries from the cash and subsidiary books

ACCOUNT

			<i>Cr.</i>					
19—		Fol.	£	s.	d.	£	s.	d.
Dec. 31	By Profit and Loss A/c. .	150				400	0	0
			£400 0 0					

ACCOUNT

			<i>Cr.</i>					
19—		Fol.	£	s.	d.	£	s.	d.
Dec. 31	By unexpired amounts c/d.: Comprehensive policy		25	0	0			
	Special Fire policy .	✓	6	0	0			
„ 31	„ Profit and Loss Account	150				31	0	0
			£89 0 0					

ACCOUNT

Cr.

19—		Fol.	£	s.	d.	£	s.	d.
Mar 31	By Sundries as per Sales Day Book . . .	12	341	6	4			
	„ Sundries as per Cash Sales Book . . .	6	183	10	6			
						524	16	10
June 30	„ Sundries as per Sales Day Book . . .	31	684	3	6			
	„ Sundries as per Cash Sales Book . . .	18	250	7	8			
						934	11	2
Sept. 30	„ Sundries as per Sales Day Book . . .	53	685	3	1			
	„ Sundries as per Cash Sales Book . . .	31	210	15	6			
						895	18	7
Dec. 31	„ Sundries as per Sales Day Book . . .	75	546	1	8			
	„ Sundries as per Cash Sales Book . . .	42	407	3	2			
						953	4	10
						£3,308	11	5

limit of space. In practice monthly totals are usually shown.)

Bills Receivable.

Bills Payable.

Other Special Journals kept.

Journal Proper.

The postings from these subsidiary books to the Nominal Ledger have already been explained in the chapters dealing with those books and need not be repeated here.

There is a great deal of variation in practice as to the length of narrative or description shown against the items in the Nominal Ledger. The principle to observe is that the narrative should be sufficiently descriptive to enable the entries to be understood so that an annual analysis and summary of any account may be made, if necessary, without frequent reference to the subsidiary books. On the other hand, the available space in the Nominal Ledger is limited and should be conserved. The entries in certain Nominal Ledger accounts, such as Purchases and Sales, which simply record the periodical (usually monthly) totals from the subsidiary books, and many of the expenses accounts which also record similar totals, do not call for detailed narratives. In such cases the words "To (or By) Sundries as per Book" and the folio indicating the source of the amounts is all that is necessary. On the

other hand, accounts recording such items as Rent, Rates, Income Tax, Insurance, Interest, etc., will require sufficient narrative to indicate at least the period to which the amounts paid or received refer. In order to illustrate this question of narrative, specimen Rent, Insurance, and Sales Accounts are shown on pages 54-57.

THE TRIAL BALANCE

When explaining the principles of double-entry in Chapter I, it was stated that every entry is posted twice—to the debit of one account and to the credit of another, and that if the work has been carried out correctly the total debits must equal the total credits. This method of proving the accuracy of book-keeping entries is the prime function of the double-entry method and is the reason for its universal adoption.

As already stated, the proof is carried out by preparing a statement of debit and credit balances known as the Trial Balance. In its original form this statement showed the total debits and total credits on each account in the ledgers. This type of Trial Balance, however, was extremely cumbersome, and under the modern method the balance on each account is scheduled instead of the totals of the debit and credit sides. The result is the same and considerable time is saved.

The Trial Balance on page 59 is based on a set of books in the office of the author at the time of writing, and a careful study of this practical example will enable readers to appreciate the principles involved.

The items down to and including the Profit and Loss Account balance were extracted from the Nominal Ledger. The Sales and Purchases Control balances were taken from the separate Control Ledger which is kept by this Company on the lines recommended in the chapter on Self-balancing Ledgers. The balance of cash at bank was taken from the Cash Book and the balance of the petty cash from the Petty Cash Book. The fact that the last two items are taken from the cash books emphasises the point that the cash books are in effect ledger accounts in themselves, but contained in special books for the sake of convenience.

It is inadvisable actually to rule off the accounts in the Nominal Ledger at the time of taking out the Trial Balance; the accounts should be totalled in pencil for the time being. When the Trial Balance has been agreed and the final accounts prepared and approved, the Nominal Ledger accounts may be ruled off and balanced as explained in a later chapter.

Fol.		Dr.			Cr.		
		£	s.	d.	£	s.	d.
1.	Share Capital				7,600	0	0
2.	Mortgage on Premises . .				1,000	0	0
3.	Goodwill	1,500	0	0			
5.	Freehold Premises . . .	2,000	0	0			
6.	Furniture and Fittings . .	371	4	1			
8.	Motor Vans	212	11	3			
11.	Stock—Raw Materials and partly finished goods	549	17	10			
	" —Finished Goods . .	2,895	4	10			
18.	Sales				11,050	0	3
22.	Rent from Sub-let				30	0	0
24.	Purchases of Raw Materials .	1,980	12	10			
	" of Finished Goods . .	6,090	2	2			
30.	Salaries—Travellers' . . .	620	10	6			
	" —Office Staff	797	16	6			
33.	Manufacturing Wages . . .	502	7	6			
45.	Rates	46	14	8			
47.	Insurance	54	14	2			
50.	Repairs	45	11	1			
53.	Heat and Light	60	17	5			
67.	Advertising	16	5	0			
70.	Printing and Stationery . .	68	14	10			
82.	Postage and Telephone . .	50	0	3			
87.	Carriage on Raw Materials .	44	10	7			
	" on Finished Goods . .	15	10	0			
96.	Motor Expenses	110	14	7			
108.	Sundry Trade Expenses . .	44	1	3			
119.	Discounts	194	8	11	145	15	9
130.	Audit Fees	42	0	0			
134.	Bad Debts	35	16	7			
136.	Income Tax				12	10	0
138.	Mortgage Interest	37	10	0			
191.	General Reserve				150	0	0
168.	Profit and Loss Account . .				40	3	4
12.	Sales Ledger Control . . .	1,938	15	7	27	8	5
26.	Purchases Ledger Control . .	10	9	0	653	11	5
74.	Cash at Bank	368	5	7			
38.	Petty Cash in Hand	4	2	2			
		£20,709 9 2			£20,709 9 2		

In practice the Trial Balance seldom agrees at the first attempt, except, perhaps, in the case of a very small set of books. Errors occur and a search must be made until they are discovered. The practice of dealing with a difference on the Trial Balance by means of an entry in a Suspense Account is dangerous and contrary to accepted principles.

Quite often a difference of, say, £1-odd is made up of a number of errors in different accounts, and it is therefore unwise to assume because the Trial Balance disagrees by a certain figure that it is simply necessary to look for one error of that figure.

There are certain classes of errors which can occur in a set of books and yet the Trial Balance agrees. These errors include the posting of an item to the correct side but to the wrong ledger account ; compensating errors, for example, the under-casting of the debit side of one account and the overcasting of the debit side of another account ; the total omission of an item (debit and credit aspects) from the books. For all practical purposes, however, the agreement of the Trial Balance is sufficient proof of the accuracy of the book-keeping.

It is difficult in the limited space available to give the reader a comprehensive series of hints as to where to look for errors should the Trial Balance fail to agree, especially as nearly every set of books differs in some detail. A great deal also depends upon the amount of the error ; for example, a difference of £10 exactly is frequently traced to an error in the cast of a subsidiary book or in the Nominal Ledger itself.

Considerable saving of time in looking for errors is, of course, avoided where the Sales and Purchases Ledgers have been separately balanced on the Self-balancing System, as the field of examination is limited to the postings to, and the castings of, the Nominal Ledger. Sometimes the error is traced to a cast in the Cash Book or Petty Cash Book, but if the Bank Reconciliation of the Cash Book and the counting and agreeing of the Petty Cash have been properly carried out such an error should have been discovered at the time.

Assuming the Self-balancing System has been adopted and the Purchases and Sales Ledgers have been agreed, but the Trial Balance disagrees, it is advisable first to recheck the casts of the Trial Balance and the accounts in the Nominal Ledger and the balances taken to the Trial Balance. If this test fails to find the error, the postings to the Nominal Ledger should be rechecked in the order in which the postings were made. If still unsuccessful, the cross-casts in the Cash and Petty Cash Books and cross-casts of any other subsidiary book where the total of the analysis columns are posted to the Nominal Ledger should be rechecked, together with the casts of any analysis columns where the items have been separately posted.

The cardinal point to bear in mind is that book-keeping and accountancy is an exact science and any set of books kept on

double-entry principles can be made to agree if sufficient care and patience is exercised. Many book-keepers have made hard remarks about the man who invented the system, but the feeling of satisfaction experienced when the Trial Balance agrees is well worth the effort made.

Chapter VII

ACCRUALS, ADJUSTING ENTRIES AND DEPRECIATION ; STOCK-TAKING

WHEN the Trial Balance has been agreed, consideration must be given to those items which have not yet been passed through the books, although referring to the accounting period covered by the Trial Balance. These items are called "accruals" or "adjustments" and refer to depreciation, outstanding income or unexpired expenditure as well as to outstanding expenses, all of which must necessarily be brought into account so that the final trading and financial statements may reflect the aggregate result of all transactions relative to the period under review.

EXPENSES DUE AND ACCRUED

When provision is to be made for an expense, the amount to be reserved is entered on the debit side of the relative expense account immediately below the last posting entry. At the same time an entry of equal amount is made a few lines below on the credit side forming the first credit entry for the subsequent period. Readers will follow that the double-entry has thus been properly carried out. The few lines provided between the entries are required for the purpose of making the subsequent transfer to the Trading or Manufacturing and Profit and Loss Accounts and ruling off.

Examples of accounts which generally require adjustment for expenses due and accrued are Rent, Rates, Heat and Light, Interest Payable, etc. Where the date on which the expenses are due coincides with the date up to which the accounts of the business are being prepared, the actual amounts due will usually be known and provision made accordingly. In other cases and where expenses have accrued, it is necessary to make a calculation on a time basis or an estimate based on past experience. For example, in the case of accounts being made up to March 31st, provision for such expenses as Electric Light and Gas will be the amounts due for the Lady Day

quarter, if unpaid on March 31st, plus an estimate to cover the six days to that date.

The principle can be seen in the illustration of the Heat and Light Account on page 68, where the amount due and accrued at the beginning of the year was £10 15s. 7d. to cover the charges paid on April 20th amounting to £10 os. 7d., plus an estimate of 15s. for the other six days to March 31st.

UNEXPIRED EXPENDITURE

In the case of unexpired expenditure the adjustment required is similar to that necessary in the case of expenses due and accrued, but on the reverse sides. That is, the unexpired amount to be carried forward is entered on the credit side of the relative account immediately below the last entry and an entry of equal amount is made a few lines below on the debit side ; this debit entry will form the first item for the following period. Thus, the double entry is completed and the account is ready for balancing and transfer to the debit of the Profit and Loss Account.

The reader will follow this explanation by reference to the Motor Expenses Account on page 70. Here Road Tax amounting to £13 10s. was paid on January 1st in respect of the whole year to December 31st. On March 31st nine months of the tax was unexpired and nine-twelfths of £13 10s., namely £10 2s. 6d., is therefore carried forward.

INCOME DUE AND ACCRUED

The adjustment necessary to bring into account income due and accrued is similar to the entry in the case of unexpired expenditure, i.e., the amount is entered on the credit side of the account and brought down as the first debit entry of the new period. The example of the Rent from Sub-let Account on page 72 provides for three months rent receivable and due on March 31st amounting to £10.

DEPRECIATION

The provision for depreciation is necessary in all cases where the assets employed in earning profits deteriorate in value through use and other causes.

The usual methods of providing for depreciation are as follows :

1. Straight Line or Equal Instalment method.
2. Diminishing Balance method.
3. Annuity method.
4. Sinking Fund method.
5. Insurance Policy method.
6. Valuation method.

The aim of all these methods is to charge an annual amount against profits, which will reduce the value of the asset to a figure which approximates its value to the business as a going concern at the end of each year and to spread the amounts so charged equitably over the life of the asset.

Straight Line Method. Under this method the difference between the cost of the asset and its residual value is written off by equal annual amounts over the estimated life of the Asset. For example, in the case of a machine costing £500 and residual or scrap value estimated at £50 at the end of ten years, the annual charge for depreciation would be £45.

The Straight Line method ignores the question of interest due on the capital outlay and also the fact that the cost of repairs increases as the machine becomes older, resulting in the annual charge for depreciation plus repairs increasing in later years. This method, however, is becoming increasingly popular as it is simple and ensures that the machine is definitely written down to scrap value by the end of its estimated life, which is not always done under some methods of depreciation. The method is usually applied to write down the cost of leases of short duration and to Plant and Machinery where circumstances require.

Diminishing Balance Method. In this case the annual depreciation is calculated on the written-down value each year. The method is widely applied to assets of all kinds and works satisfactorily in practice if the rate of depreciation selected is adequate. For instance, assuming the case of the machine costing £500 mentioned in the previous paragraph: under the Diminishing Balance method the written-down value at the end of ten years, after allowing for depreciation at 10 per cent. per annum, would be £174 and with the residual value at £50 there would be a loss on sale amounting to £124 to be written off. The appropriate rate to adopt in such a case should approximate 20 per cent. per annum.

Annuity Method. Under this method the amount written off each year is calculated to reduce the asset to scrap value at

the end of its useful life, plus interest on the capital sunk in the Asset. The annual charge is constant and is ascertained by reference to tables.

The amount of interest is calculated annually, debited to the Asset and credited to Profit and Loss Account. Each instalment of interest credited to Profit and Loss Account decreases as the annual depreciation instalment is written off the Asset. As the charge to Profit and Loss Account for depreciation is constant in amount, the effect of the process is that Profit and Loss Account gradually bears an increasing charge as time goes on. Theoretically this is the most scientific method and is recommended in the case of long leases. The method is not suitable for such assets as Plant and Machinery and Vehicles, since the calculations will require revision when additions or replacements are made from time to time.

Sinking Fund Method. The principle of taking interest into consideration is also applied in this method. A stipulated sum is set aside each year and invested in gilt-edged securities and the interest received is similarly reinvested. These annual sums, together with compound interest on the investments, are calculated to produce sufficient cash to meet the cost of replacing the asset at the end of its estimated life when the investments are realised. The asset is not depreciated annually but is left in the books at cost, and at the end of its estimated life the accumulated reserve is transferred to the credit of the Asset Account, reducing it to scrap value.

Insurance Policy Method. This is another form of the Sinking Fund Method ; instead of investing the annual sums in securities the amounts are paid to an Insurance Company in the form of premiums on a policy which will produce the required sum to replace the asset at the end of its estimated life. Provided there is no likelihood of the policy being surrendered during its currency, the method has the advantage of providing a definite sum, whereas securities may depreciate and fail to produce the amount anticipated.

Valuation Method. Under this method an actual valuation of the asset is made and the shrinkage in value between the accounting dates is written off as depreciation. The method is suitably applied to assets such as loose tools and equipment, horses, cattle, patents, copyrights, etc., but is impracticable in the case of fixed plant and machinery, buildings and similar assets of a permanent or semi-permanent nature. Should the valuation of an identical asset disclose an increase, it is unwise

to take credit for such increase, but to carry the asset forward at the valuation figure of the previous year.

SUITABILITY OF THE METHODS

In considering the most suitable method of depreciation to adopt, business men should remember that in all cases of provision for future expenditure there are two aspects to bear in mind. Firstly, there is the deduction from profits of the estimated depreciation, and secondly, the important question of making provision for the cash required to replace the Asset when necessary. In the author's experience the latter point is often forgotten, particularly in a growing business where there is a danger of locking up funds in stock, book debts, etc., to such an extent that the replacing of assets means recourse to borrowing or acquiring assets by means of hire purchase.

The method selected in deducting depreciation from profits will depend upon the type of asset to be depreciated and the nature and requirements of the particular business. Except in the case of long leases or other assets of considerable value and long life, interest may be pardonably ignored and a choice made between methods (1) and (2). The ideal to observe is that the book figure of the asset at the end of each financial year should approximate its productive value, and at the end of its useful life the book figure should represent as closely as possible the residual worth. It is not, of course, always possible to achieve this ideal owing to factors such as inventive improvements which could not be envisaged at the time, but an intelligent and conservative survey of values at the end of the financial year, accompanied by adjustment of the rates of depreciation where circumstances dictate, will assist in keeping book figures within a reasonable margin of productive value.

The question of making provision for the necessary funds wherewith to meet the cost of replacement requires an equally intelligent review from time to time, and where there may be some difficulty, the method of investing funds outside the business in gilt-edged securities or taking out a suitable insurance policy should be considered. The rate of interest earned from funds so invested may be less than the rate which could be earned within the business, but this disadvantage may be more than covered by the saving of interest on borrowings which are necessary when the coffers of the company are empty.

The necessary book-keeping adjustment for depreciation simply involves the transfer of an amount, calculated to cover

the reduction in value, from the Asset Account to the debit of the Profit and Loss or Manufacturing Account. The amount transferred is entered on the credit side of the Asset Account as a transfer to the debit of Profit and Loss or Manufacturing Account, thus reducing the book value shown on the debit side of the Asset Account.

In special cases and where depreciation is to be provided in respect of many assets, the transfers are made to the debit of a Depreciation Account which is subsequently closed by a transfer to the Profit and Loss or Manufacturing Account.

In theory the entries recording the adjustments mentioned should be passed through the Journal Proper in the first place and posted from there to the accounts in the Nominal Ledger. But in practice unless special circumstances dictate, the transfers are usually made in the Nominal Ledger accounts without passing the entries through the Journal.

The attention of readers is called to the examples of Furniture and Fittings and Motor Vans Accounts shown on pages 72 and 73, where separate columns are ruled to show the original cost and book values of the assets. This method is recommended as it enables the total depreciation written off up to each accounting date to be ascertained in accordance with the requirements of the Eighth Schedule to the Companies Act, 1948, which states that a Company's Balance Sheet must show the aggregate amount provided or written off for depreciation since the date of the acquisition or valuation of the asset. It was realised, however, that in the case of an asset acquired many years ago, there may be difficulty in arriving at the aggregate amount written off since the date of its acquisition. The Act therefore provides that if the figures relating to the period prior to July 1st, 1948, cannot be obtained without unreasonable expense and delay, the net amount at which the asset stood in the books of the company at July 1st, 1948, may be taken as the opening figure from which subsequent amounts written off are to be deducted and aggregated.

MACHINERY AND PLANT REGISTER

Where the machinery and plant in use is extensive, it is advisable to keep a Machinery and Plant Register. This book does not form part of the double-entry book-keeping and its purpose is to classify the machinery and plant into suitable groups showing cost prices, additions, depreciation written off, and the resulting written-down values at the end of each financial year ; columns may also be ruled to record repairs

68 BOOK-KEEPING & ACCOUNTANCY FOR PRIVATE COMPANIES

<i>Expenses Accrued</i>			<i>Accrued Income and Payments in Advance</i>		
	£	s. d.		£	s. d.
Carriage Inwards	4	13 4	Rent from Sub-let	10	0 0
Rates	8	10 4	Motor Road Tax	10	2 6
Heat and Light	9	8 10	Insurance	24	14 4
Mortgage Interest	12	10 0			
Telephone Calls	3	8 0			
Motor Van Repairs	24	5 3			
	<u>£62 15 9</u>			<u>£44 16 10</u>	

The general reserve to be increased by £100.

Current Income Tax to be provided £150.

Depreciation to be provided :

Furniture and Fittings	5%
Motor Vans	20%

HEAT

Dr.

		Fol.	£	s. d.	£	s. d.
19—						
April 20	To Cash—Electricity for quarter to Lady Day	21	7	8 6		
" 20	" Cash—Gas for quarter to Lady Day	21	2	12 1	10	0 7
June 10	" Cash—Western & Co. —Coal	40			12	10 0
July 25	" Cash—Electricity for quarter to Midsummer	52	5	3 9		
" 25	" Cash—Gas for quarter to Midsummer	52	2	8 3	7	12 0
Oct. 2	" Cash—Electricity for quarter to Michaelmas	75	5	17 6		
" 2	" Cash—Gas to Michaelmas	75	1	11 6	7	9 0
Dec. 3	" Cash—Gas Co.—Coke	86			16	9 5
19—						
Jan. 16	" Cash—Electricity for quarter to Christmas	93	12	3 0		
" 16	" Cash—Gas to Christmas	93	5	9 0	17	12 0
March 31	" Amounts due and accrued to date c/d.: Electricity	✓	6	2 0	71	13 0
	Gas		3	6 10	9	8 10
					<u>£81 1 10</u>	

and renewals. A separate account is used for each classification of machinery or plant, and notes are made of the description, where erected, date purchased, estimated life, estimated residual value, overhauls, breakdowns, etc.

The reader will understand that this information, which is really a history of each group of machinery and plant, serves a useful purpose when reviewing factory costs, and when calculations are required to ascertain the loss on replacement for accountancy and Income Tax purposes.

In order that the provision of the Eighth Schedule to the Companies Act, 1948, mentioned above, may be observed, the keeping of a register for plant and machinery and other fixed assets which are subject to depreciation is recommended as a supplement to the accounts in the Nominal Ledger.

AND LIGHT

				<i>Cr.</i>	
		Fol.	£ s. d.	£ s. d.	
19— April 1	By Amounts due and accrued b/f.	✓		10 15 7	
19— March 31	„ Profit and Loss A/c.	N.L. 110		70 6 3	
				£81 1 10	
19— April 1	By Amounts due and accrued b/d.	✓		9 8 10	

MORTGAGE

Dr. Mortgage—£500.

19—			Fol.	£	s.	d.	£	s.	d.
July	1	To Cash—Miss E. Ward							
		—Interest for 6							
		months to June 30		25	0	0			
		Less tax @ 5s. in £		6	5	0			
19—			49				18	15	0
Jan.	2	„ Cash—Miss E. Ward							
		—Interest for 6							
		months to December 31		25	0	0			
		Less tax @ 5s. in £		6	5	0			
			91				18	15	0
March	31	„ Income Tax transferred	N.L. 70				12	10	0
							50	0	0
„	31	„ Interest accrued to date c/d.	✓				12	10	0
							£62	10	0

MOTOR

19—			Fol.	£	s.	d.	£	s.	d.
April	1	To Amount paid in advance b/f.	✓				10	2	6
„	1	„ Cash—X.Y. Insurance Co., comprehensive policy to March 31 next	18				19	5	6
„	10	„ Cash—A. J. B., Ltd. Petrol and Oil Maintenance	20	14	1	6			
			„	6	1	0	20	2	6
July	11	„ Cash—A. J. B., Ltd. Petrol and Oil Maintenance	51	16	3	4			
			„	9	7	1	25	10	5
Oct.	10	„ Cash—A. J. B., Ltd. Petrol and Oil Maintenance	76	17	8	0			
			„	2	2	0	19	10	0
19—									
Jan.	1	„ Cash—Road Tax to December 31 next	91				13	10	0
„	10	„ Cash—A. J. B., Ltd. Petrol and Oil Maintenance	92	18	6	2			
			„	4	10	0	22	16	2
March	31	„ Amount due to A. J. B., Ltd. c/d.: Petrol and Oil Maintenance	✓	19	10	3	130	17	1
				4	15	0	24	5	3
April	1	„ Amount paid in advance b/d.	✓				£155	2	4
							10	2	6

INTEREST

Interest @ 5% p.a. payable June 30 and December 31.

Cr.

19— April 1	By Amount accrued b/f.	Fol. ✓	£ s. d.	£ s. d. 12 10 0
19— March 31	„ Profit and Loss A/c.	N.L. 110		50 0 0
19— April 1	By Amount accrued b/d.	✓		£62 10 0 12 10 0

EXPENSES

Cr.

		Fol.	£	s.	d.	£	s.	d.
19— April 1	By Amounts due b/f. .	✓				20	2	6
19— March 31	„ Road Tax paid in advance c/d. .	✓				10	2	6
„ 31	„ Profit and Loss A/c.	N.L. 110				124	17	4
						£155 2 4		
April 1	By Amount due b/d. .	✓				24	5	3

RENT FROM

Terms : £40 p.a.

Dr.

Tenant : J. Brown.

19— April 1	To Amount due b/f. .	Fol. ✓	£ s. d.	£ 10 0 0
19— March 31	„ Profit and Loss A/c. .	N.L. 110		40 0 0
				£50 0 0
19— April 1	To Amount due b/d. .	✓		10 0 0

FURNITURE

			Fol.	Cost.			Book Value.		
				£	s.	d.	£	s.	d.
19—									
April	1	To Balances b/f.	✓	351	6	1	301	4	1
"	10	" Cash—Additional Showcases	20	68	0	0	68	0	0
"	10	" Cash—Fixing charges	20	2	0	0	2	0	0
				£421	6	1	£371	4	1
19—									
April	1	To Balances b/d.. . . .	✓	£421	6	1	352	12	10

MOTOR

		Fol.	Cost. £ s. d.			Book Value. £ s. d.		
19— April 1	To Balances b/f.:							
	Van No. 1 . .	✓	176	0	4	90	2	6
	„ „ 2 . .		191	6	3	122	8	9
			£367	6	7	£212	11	3
19— April 1	To Balances b/d.							
	Van No. 1 . .	✓	176	0	4	72	2	0
	„ „ 2 . .		191	6	3	97	19	0
			367	6	7	170	1	0

SUB-LET

exclusive), payable quarterly commencing January 1, 19—

Cr.

19—		Fol.	£	s.	d.	£	s.	d.
April 8	By Cash—Rent to March 31	19				10	0	0
July 11	„ Cash—Rent to June 30	51				10	0	0
Oct. 10	„ Cash—Rent to September 30	76				10	0	0
19—								
Jan. 12	„ Cash—Rent to December 31	92				10	0	0
						40	0	0
March 31	„ Amount due to date c/d.	✓				10	0	0
						£50	0	0

AND FITTINGS

Depreciation 5% p.a.

19—		Fol.	Cost.	Book Value.
March 31	By Profit and Loss A/c.—Depreciation @ 5% p.a.	N.L. 110	£ s. d.	£ s. d.
„ 31	„ Balances c/d.	✓	421 6 1	18 11 3 352 12 10
			£421 6 1	£371 4 1

VANS

Depreciation 20% p.a.

19—		Fol.	Cost.	Book Value.
March 31	By Profit and Loss A/c.—Depreciation @ 20% p.a.	N.L. 110	£ s. d.	£ s. d.
„ 31	„ Balances c/d.	✓	367 6 7	18 0 6 24 9 9 170 1 0
			£367 6 7	£212 11 3

AN EXAMPLE

Referring to the Trial Balance shown in the previous chapter, some of the adjustments made in that case are shown on page 68. These details are recorded on a schedule of adjustments for use in constructing the Final Accounts explained in the next chapter.

Space does not permit each of these items to be dealt with in detail, so the writer has selected for illustration the adjustments in respect of Heat and Light, Mortgage Interest, Motor Expenses, Rent from Sub-let, and Depreciation.

Readers will observe that the accounts illustrated, except those relating to Furniture and Fittings and Motor Vans, are sub-totalled before the outstanding items are entered. This method has the advantage of making a permanent record as to how each item in the Trial Balance is made up. The adjustments follow and are usually entered after the final accounts have been considered and approved.

Schedules of the necessary adjustments are prepared at the end of the financial year, and particular attention should be paid to this work so as to ensure that all necessary provisions have been noted relating to the period under review. It is a good plan to make a note in red ink on the Trial Balance against the items subject to adjustment, thereby facilitating the accurate preparation of the final accounts.

The adjustments which have not been illustrated are made on similar lines to those shown by the examples given, and a careful study of these examples should enable readers to apply the principles to the accounts with which they are concerned in practice.

Where the Purchases Day Book is ruled to include expenses as illustrated in Chapter III, the expenses due but not paid will have already been entered and further adjustment will not be necessary. Expenses accrued, as distinct from those due, will, however, require adjustment on the lines indicated, since the expenses are not entered in the Purchases Day Book until the amounts actually become due.

STOCK-TAKING

The importance of correct stock-taking is not always appreciated, and a great deal of laxity appears to exist in practice, particularly in the smaller type of business. It should be remembered that no matter how carefully the book-keeping has been carried out, the trading results as revealed by the

Final Accounts will be inaccurate and valueless if the stocks of materials and finished goods have been taken out incorrectly.

It is generally appreciated that a considerable saving of time is effected, and inconvenience reduced to a minimum, if the end of the financial year is arranged to coincide with the time when the stocks are lowest in volume.

Most business men are acquainted with stock-taking and for this reason the author does not propose to go into familiar detail, but to offer a few suggestions and to summarise some of the precautions which he has found of general application in practice.

Stock-taking comprises two separate tasks : (a) recording the description and quantities, and (b) the pricing out, extensions, and additions of the items. In trades dealing with articles such as Jewellery, Motor-cars, Pianos, etc., stock books are kept in which the number and a brief description of each item is recorded, showing the date of purchase, reference to the Purchases Journal or Cash Book, date when each article is sold and the reference to the Sales Journal or Cash Sales Book, and provision for particulars of any revision in the prices of unsold articles. When a stock book is kept on these lines, the actual stock-taking comprises the calling over of the articles in stock with the book and the consideration of the revision of prices where necessary.

In other businesses, the nature of the goods may not permit a continuous stock record to be kept, the details taken of the stock being recorded on schedules. In such cases, it is a good plan, when possible, to divide the stock into convenient groups and to prepare schedules for each group in advance showing a description of the leading lines. By this method the stock-taker is not delayed by his assistant having to write out the description of each item when the quantities are being given to him, and if it is possible to leave the pricing of the stock until after the quantities have been taken, further time may be saved.

The following notes indicate some of the precautions desirable in stock-taking :

(a) Stock should be taken immediately after the close of business on the last day of the accounting period ; this usually means in the morning of the first day of the new period.

(b) Wherever possible ordinary business should be temporarily suspended during stock-taking. Orders received should be held for execution after stock has been counted. Alternatively, goods taken out before stock is counted must be carefully noted and added to the counted stocks later.

(c) It should be seen that all goods sold and invoiced on the last day have actually been dispatched before stock is taken.

(d) Similarly it should be seen that all purchases invoiced during the last few days of the period are delivered, and that no goods are taken into stock which have not been invoiced by the suppliers.

(e) The price at which goods are brought into stock should, wherever possible, be the cost price or the net current market price, whichever is the lower, due allowance being made for old or obsolete stock. In certain instances, particularly in the Antique trade when an article may have been bought at a time of inflated prices and the present market price is difficult to estimate, the stock value may be roughly determined by taking the price which the business is prepared to accept for a ready sale and deducting from this price a percentage representing a reasonable average rate of gross profit.

(f) In the case of goods which have been partly or wholly manufactured by the company, the price per unit is normally taken at cost, i.e., materials, manufacturing labour, and a reasonable proportion of factory overheads. In some cases this should be reduced. (i) where the total cost exceeds the sale price, or (ii) where partly manufactured goods and components could be bought in their present state for less than cost.

(g) The actual work of taking stock should be the responsibility of the head of each department ; the stock sheets, prices, extensions, and additions being independently checked. All work should be signed by those responsible, the total value in each department being countersigned by the head of the department.

(h) The stock sheets as a whole should be examined by the Managing Director and certified as correct by him for the purpose of the accounts and their audit.

Chapter VIII

MANUFACTURING, TRADING, AND PROFIT AND LOSS ACCOUNTS. BALANCE SHEET

THE Trial Balance having been agreed and a schedule of the adjusting entries prepared, the interesting work of constructing the Manufacturing, Trading, and Profit and Loss Accounts, and Balance Sheet, known as the Final Accounts, will now be considered.

In the author's experience, this work is frequently left to the auditors of the company, although, strictly speaking, it is not part of their duties. Section 162 of the Companies Act, 1948, states that the auditors shall make a report to the members of the company on the accounts *examined* by them and on every Balance Sheet laid before the company in general meeting during their tenure of office. This section also extends the auditors' duties to a report on every Profit and Loss Account laid before the company in general meeting during their tenure of office. The Act does not make the auditors responsible for the preparation of the Final Accounts. This responsibility, including the preparation of the Profit and Loss Account, rests with the Directors of the company under Section 148. It is therefore suggested that where there is no objection to the private information revealed by the Final Accounts being known, the preparation of these documents in draft form may be left to a responsible member of the accounting staff, or that the work be undertaken by the secretary or a director. One of the particular objects of this book is to afford a practical guide to business men in the interesting detail of preparing intelligible accounts of their own particular company for presentation to the auditors.

The primary purpose of the Manufacturing, Trading, and Profit and Loss Accounts is to ascertain the result of the manufacturing or trading activities of the business during the period covered by the accounts, and to show in a clear and concise form the constituent debit and credit items taken into consideration in arriving at that result.

The function of the Balance Sheet is to show the financial position of the business in the form of an orderly statement of assets and liabilities, including the Capital and the balance of the Profit and Loss Account.

The wide variety of businesses, each with its own particular features and wishes of the proprietors, makes it impossible to put forward any dogmatic rules as to the precise form of presentation which the final accounts of all businesses should follow. The cardinal principle to observe, however, is consistency of method, so that comparisons of the accounts of one year with another can be made. Without this consistency comparisons are useless.

The final accounts explained and illustrated in this chapter have been constructed from the Trial Balance and adjustments shown in Chapters VI and VII, and whilst the form of presentation may require to be varied according to the nature and requirements of individual businesses, the method will form a general indication of the usual and accepted lines.

If sufficient information is shown, it is suggested that the Final Accounts be prepared from the Trial Balance and schedule of adjustments, and the items ticked as they are dealt with so as to avoid duplication or omission. It may, of course, be necessary to refer to the Nominal Ledger for further details, especially where transfers have been made after the Trial Balance has been completed.

MANUFACTURING ACCOUNT

Where the activities of a business include manufacturing, it is necessary and desirable to ascertain the prime cost of the goods manufactured during the accounting period, and this is done by means of a Manufacturing Account. The term "prime cost" here refers to the aggregate cost of material used, carriage on the material, and the wages of persons engaged in manufacturing the goods. These items, together with the values of the opening stocks of raw materials and partly manufactured goods, are taken from the Trial Balance.

The closing stock does not appear in the Trial Balance ; it is brought into the final accounts by a Journal entry debiting the Stock Account in the Nominal Ledger and crediting the Manufacturing Account with the value of the raw materials and partly manufactured goods. In the case of finished goods the credit is made to the Trading Account.

Readers will see from the example on page 86 that the balance of the Manufacturing Account represents the manufacturing cost of the finished stock and the amount is brought down to the debit of the Trading Account.

Further elaboration of the principle of ascertaining the cost of manufacture may be carried out, if necessary, by including in the Manufacturing Account other items of factory expense, such as the cost of fuel and power, factory maintenance charges, including rent and rates, insurance, repairs and renewals, etc. To obtain these details it is necessary to keep appropriate accounts in the Nominal Ledger, or to obtain the information by an analysis of the relative accounts.

If the goods produced can be valued at trade buying prices and the total amount credited to the Manufacturing Account, the credit balance on this account will represent the manufacturing profit earned by the factory and is taken to the credit of Profit and Loss Account. In the event of a manufacturing loss, the Manufacturing Account will show a debit balance to be taken to the debit of Profit and Loss Account. The advantage of this method is that the result of the factory production is known, but the difficulty, as experienced in the business referred to in the example, is in determining the trade buying prices of the wide range of lines produced.

TRADING ACCOUNT

When the business carried on includes the buying of goods for resale, it is necessary to prepare a Trading Account for the purpose of ascertaining the gross profit earned on the total sales. The term "gross profit" is very difficult to define, as opinions differ regarding the items which should be taken into consideration in determining gross profit. Without going into details which may lead the reader into controversial and theoretical realms, the term "gross profit" for the purposes of this chapter may be taken as the excess of the sales over the purchasing and manufacturing cost of the goods sold, and after taking into consideration items directly affecting the prime cost of purchasing and manufacturing those goods.

Apart from the cost of the goods manufactured, as already explained, the items taken to the debit of the Trading Account illustrated are the opening stock of finished goods, goods bought for resale, and carriage thereon. The credit side records the total sales after deducting returns, and the closing stock of finished goods.

It should be emphasised that the items charged in this specimen Trading Account are not the only items chargeable in all cases. As previously stated, items directly affecting the prime cost of purchasing the goods should be brought into the Trading Account. For example, where goods are bought in bulk, repacked, and sold in small units, it is suggested that the wages of employees engaged on this work should be included in the Trading Account. Again, the cost of storing goods which improve with age, such as wines and spirits, is an item directly affecting the prime cost of the goods, and this expense is chargeable in the Trading Account. The question is a very interesting one and can only be determined after a study of the nature and circumstances of the particular business.

The credit balance of the Trading Account, representing the gross profit earned, is brought down to the credit of the Profit and Loss Account. A debit balance on the Trading Account represents a gross loss and would be brought down to the debit of the Profit and Loss Account.

When the nature of the business is solely manufacturing, a Trading Account is not required, the gross profit being the credit balance on Manufacturing Account, which is taken to the credit of the Profit and Loss Account; conversely, if the business is solely merchanting, the gross profit is the credit balance on Trading Account, and a Manufacturing Account is not required. In businesses of an "operating" nature, such as cinemas or haulage contracting, the preparation of a Profit and Loss Account only is normally necessary to ascertain the results for the accounting period.

PROFIT AND LOSS ACCOUNT

The next step is the preparation of the Profit and Loss Account for the purpose of ascertaining the net profit for the accounting period. Section 149 of the Companies Act, 1948, provides that every Profit and Loss Account of a company shall give a true and fair view of the profit or loss of the company for the financial year and the Eighth Schedule to the Act sets out general directions as to the contents of the Profit and Loss Account. These directions are dealt with in Chapter XI.

Apart from the figure of gross profit brought down from the Trading Account, the credit side of the Profit and Loss Account contains sundry items of income such as discounts received, rent of sub-lettings, transfer fees, etc.

On the debit side of the account the expenses incurred in earning the profit, other than those dealt with in the Manufacturing and Trading Accounts, will be listed. The order of listing the items largely depends upon the nature of the business, and no hard-and-fast rules can be made. In practice, however, the expenses usually fall into three or four general groups and readers are advised to follow this order if possible. The groups are as follows :

(a) *Selling Expenses*. These include salaries, commission, and expenses of the sales staff ; rent, rates, insurance, and maintenance charges of the warehouse ; advertising and other expenses incurred in selling the goods.

(b) *Distribution Expenses*. Included under this heading are delivery expenses and carriage outwards ; packing and other expenses in connection with distribution.

(c) *Administration Expenses*. These expenses include salaries of the office staff and executive, directors' remuneration, rent, rates, insurance and expenses of the offices, supervisory and management expenses.

(d) *Financial Expenses*. The usual items in this group are discounts allowed, bad debts written off, legal, accountancy, and other professional charges.

Readers will, no doubt, envisage expenses in connection with their own businesses which may not be capable of grouping under any of these headings, especially items of an extraordinary or non-recurring nature. These may be shown last on the debit side of the Profit and Loss Account according to their order of importance.

Depreciation is an important debit item to Profit and Loss Account, and here again there is some diversity of practice. Where loss through general usage of machinery is heavy and capable of ascertainment, a convenient method of grouping can be formulated, and depreciation of machinery used solely in the manufacture of goods may be charged to Manufacturing Account.

The adjustments and reserve shown on page 68, and brought into the example under consideration in this chapter, fall into two classes : (a) Expenses Accrued and (b) Accrued Income and Payments in Advance. In addition, provision for depreciation is to be made at the rates mentioned, the appropriation to General Reserve and provision for Income Tax.

As regards Expenses Accrued, the specimen Nominal Ledger Accounts and explanations given in Chapter VII show that the adjustment takes the form of a further debit or addition

to the expense account, and an equal amount brought down as a credit balance forming the first item on the credit side of the account for the next accounting period. These credit balances, as listed on the schedule, are included on the liabilities side of the Balance Sheet under the heading Current Liabilities and Provisions ; thus the debit for the adjustment is made to the Profit and Loss Account and the credit included in the Balance Sheet, the double entry being completed as far as the final accounts are concerned. The double entry in the Nominal Ledger is carried out when balancing the account as already explained in Chapter VII.

The method is reversed in dealing with Accrued Income and Payments in Advance, as in this case the account to be adjusted is credited with the amount of the provision and the figure brought in as a debit balance in the Balance Sheet under the sub-heading of Debtors and Payments in Advance. The double entry is also made in the Nominal Ledger when balancing the ledger accounts.

Depreciation is debited in the Profit and Loss Account and the amount credited to the Asset Account affected and shown as a deduction from the asset in the Balance Sheet, together with the aggregate depreciation written off in previous years.

The adjustments shown in the inset columns of the Trading and Profit and Loss Account illustrated on page 86 appear on the draft accounts, but these details are omitted when preparing fair copies.

APPROPRIATION ACCOUNT

This account is, in effect, a second or subsidiary section of the Profit and Loss Account, and its function is to show the balance of profit or loss brought forward from the previous accounting period, the net profit or loss for the current period brought down from the Profit and Loss Account, provision for taxation, the distributions by way of dividends and appropriations made to reserves, etc.

The balance of the Appropriation Account is carried to the Balance Sheet as shown in the example.

BALANCE SHEET

Section 149 of the Companies Act, 1948, provides that every Balance Sheet of a company shall give a true and fair view of the state of the affairs of the company at the end of its financial

year and shall comply with the requirements of the Eighth Schedule to that Act. These requirements are dealt with in Chapter XI.

Turning to the example under consideration, the remaining items of the Trial Balance are taken to the Balance Sheet on page 88 together with the adjustments.

The first entry on the liabilities side of the Balance Sheet of a limited company is a statement of the Nominal or Authorised Share Capital in accordance with the Eighth Schedule to the Companies Act, 1948. The amount is not extended to form part of the total of that side of the Balance Sheet, but is left inset, serving as a memorandum note of the amount to capital which the company has power to issue under its Memorandum and Articles of Association.

The next entry is the amount and description of the shares issued and paid-up, also in accordance with the Eighth Schedule and is taken from the Trial Balance. In the example 7,600 Ordinary Shares only have been issued, leaving 400 Ordinary and the whole of the Preference Shares to be allotted when further capital is required.

The particulars of the capital subscribed by the shareholders being recorded, the General Reserve is now brought in, followed by the credit balance of the Profit and Loss Account as shown by the appropriation section of that Account.

Loans secured by a Mortgage or Debentures form the next item. As accrued interest is also secured under the charge, any interest outstanding at the end of the year should be added to the principal money as shown in the example.

Unsecured indebtedness of the Company follows under the heading of Liabilities and Provisions. The credit balances on the Sales and Purchases Ledger Control Accounts are taken from the Trial Balance, and the remaining items are the total of the Expenses Accrued Schedule, after deducting the mortgage interest which has been shown separately, the provision for current taxation and the proposed dividend for the year on the Ordinary Shares. The detail figures are omitted from the final Accounts, the item of Creditors and Accrued Expenses being shown in the one amount of £731 5s. 7d.

In the event of a debit balance to Profit and Loss Account, the amount of the balance will be deducted from the total of the Capital and Revenue Reserves group.

The presentation of the assets in a Balance Sheet of a commercial company is usually in order of unrealisability. In the case of Banks, Insurance Companies and Financial Houses,

the sequence is reversed. The most unrealisable or intangible asset in the accounts which are now being considered is Goodwill, and, at the other extreme, Cash in Hand.

The Eighth Schedule to the Companies Act, 1948, provides, *inter alia*, that fixed assets shall be distinguished from current assets and that the method used to arrive at the amount of the fixed assets under each heading shall be stated in the Balance Sheet. For instance, the specimen Balance Sheet states that Goodwill and Freehold Premises have been valued at cost; Furniture and Fittings and Motor Vans have also been valued at cost less depreciation provided to date.

The stock-in-trade is divided between raw materials, including partly manufactured goods, and finished goods. Readers will remember the explanation already given that the closing stocks do not feature in the Trial Balance, the double entry being effected on the Final Accounts by a credit to Manufacturing or Trading Account and a debit to the Stock Account, the latter appearing in the Balance Sheet as an asset.

The debit balances on the Sales and Purchases Ledger Control Accounts are brought in, together with the total of the adjustments for accrued income and payments in advance as shown by the schedule, and included under the sub-heading Debtors and Payments in Advance. The detail figures are omitted from the final accounts and the item shown in the one figure of £1,994 1s. 5d.

B. & B. LTD.

MANUFACTURING ACCOUNT FOR THE

19— (Previous year) £		£	s.	d.
	To Stock of Raw Materials and Partly Manufactured Goods, April 1, 19—	549	17	10
672	„ Purchases of Raw Materials	1,980	12	10
1,853	„ Carriage on „ „	44	10	7
41	„ Manufacturing Wages	502	7	6
497				
£3,063		£3,077	8	9

Cash at Bank and in hand, as listed in the Trial Balance, form the last assets.

If the work of preparing the Final Accounts has been carried out correctly on double-entry principles, the sides of the Balance Sheet should agree.

The accounts are now ready in draft form for examination by the auditors of the company, who, on being satisfied with the statements, will intimate that they are prepared to sign the report on the accounts. Before doing so, however, the auditors will request that the accounts be submitted to the directors of the company for their approval and signatures.

The ruling off and balancing of the accounts in the Nominal Ledger may now be finished, and when this has been done it is a good plan to check the balances in the Nominal Ledger with the figures in the Balance Sheet and schedule of adjustments, or alternatively to prepare a Trial Balance of the final balances as brought down. By this means any error or omission in bringing down the balances will be discovered. Otherwise such errors will upset the next Trial Balance taken out.

The Final Accounts are frequently copied into the Nominal Ledger, the transfers from the Nominal Ledger to the Final Accounts being cross-referenced by folio numbers. This procedure enables the trading result of any particular year to be referred to easily, but may not be favoured where the book-keeping staff have access to the Nominal Ledger.

YEAR ENDED MARCH 31st, 19—

19—
(Previous
year)

£

550

2,513

£3,063

By Stock of Raw Materials and Partly Manufactured
Goods, March 31, 19—
„ Balance carried to Trading A/c, being Prime Cost
of goods manufactured

£ s. d.

593 18 1

2,483 10 8

£3,077 8 9

B. & B. LTD.

TRADING ACCOUNT FOR THE

19—
(Previous
year)

£		£	s.	d.	
3,184	To Stock of Finished Goods, April 1, 19—	2,895	4	10	
2,513	„ Manufacturing A/c—Prime Cost of goods manu- factured	2,483	10	8	
5,658	„ Purchases, less Returns	6,090	2	2	
27	„ Carriage Inwards	15	10	0	
		o/s	4	13	4
2,373	„ Gross Profit carried to Profit and Loss A/c	20	3	4	
£13,755		2,671	14	3	
		£14,160	15	3	

PROFIT AND LOSS ACCOUNT FOR THE

		£	s.	d.
51	To Rates	46	14	8
	o/s	8	10	4
58	„ Repairs to Buildings	45	11	1
67	„ Heat and Light	60	17	5
	o/s	9	8	10
29	„ Insurance	54	14	2
	Less c/f.	24	11	4
598	„ Travellers' Salaries and Commis- sion	620	10	6
18	„ Advertising	16	5	0
121	„ Motor Delivery Expenses	110	14	7
	o/s	24	5	3
	Less c/f.	134	19	10
764	„ Office Salaries	10	2	6
119	„ Printing, Stationery, Postage and Telephone	68	14	10
	o/s	50	0	3
52	„ Sundry Trade Expenses	3	8	0
185	„ Discount allowed	44	1	3
50	„ Mortgage Interest	194	8	11
	o/s	37	10	0
		12	10	0
42	„ Audit and Professional Fees	42	0	0
18	„ Bad Debts	35	16	7
16	„ Depreciation : Furniture and Fixtures @ 5%.	18	11	3
53	Motor Van @ 20%.	42	10	3
311	„ Net Profit carried forward	61	1	6
£2,552		547	7	2
		£2,857	10	0

YEAR ENDED MARCH 31st, 19—

19—
(Previous
year)

£
10,860
2,895

	£	s.	d.
By Sales, less Returns	11,050	0	3
„ Stock of Finished Goods, March 31, 19—	3,110	15	0

£13,755

£14,160 15 3

YEAR ENDED MARCH 31st, 19—

2,373
139
40

By Gross Profit brought from Trading A/c
„ Discounts received
„ Rent from Sub-let

	£	s.	d.
	2,671	14	3
	145	15	9
	30	0	0
	10	0	0
o/s	40	0	0

£2,552

£2,857 10 0

APPROPRIATION

19—
(Previous
year)

£		£	s.	d.
118	To Provision for Income Tax	137	10	0
25	„ Transfer to General Reserve Account	100	0	0
190	„ Proposed Dividend, less tax, on Ordinary Shares for the year	285	0	0
40	„ Balance carried to Balance Sheet	65	0	6
<u>£373</u>		<u>£587</u>	<u>10</u>	<u>6</u>

B. & B. LTD.

BALANCE SHEET

	Share Capital :	£	s.	d.	£	s.	d.
	Authorised :—						
2,000	2,000 6% Cumulative Preference Shares of £1 each	2,000	0	0			
8,000	8,000 Ordinary Shares of £1 each	8,000	0	0			
<u>£10,000</u>		<u>£10,000</u>	<u>0</u>	<u>0</u>			
	Issued —						
7,600	7,600 Ordinary Shares of £1 each, fully paid				7,600	0	0
	Revenue Reserves :						
	General Reserve at 31st March, 19—	150	0	0			
	Add Transfer for year to date	100	0	0			
150		250	0	0			
40	Profit and Loss Account :						
	Balance unappropriated	65	0	6	315	0	6
<u>7,790</u>					<u>7,915</u>	<u>0</u>	<u>6</u>
	Mortgage at 5% :						
1,013	£1,000 secured on Freehold Premises, per contra, plus interest accrued				1,012	10	0
	Current Liabilities and Provisions :						
693	Creditors and accrued expenses	731	5	7			
130	Current Taxation	150	0	0			
190	Members for proposed dividend (less tax) on Ordinary Shares for year to date	285	0	0	1,166	5	7
<u>2,026</u>					<u>£10,093</u>	<u>16</u>	<u>1</u>
<u>£10,016</u>	H. Harwood } A. Green } Directors						

Report of the Auditors to the Members of B. & B. Limited.

We have obtained all the information and explanations which to the best of our proper books of account have been kept by the Company so far as appears from our annexed Profit and Loss Account which are in agreement with the books of account. given us the said accounts give the information required by the Companies Act, of the state of the Company's affairs as at 31st March, 19—, and the Profit and Loss

Stevenage House,
40-44, Holborn Viaduct,
London, E.C.1.

10th July, 19—

ACCOUNT

19—
(Previous
year)

£

62

311

	£	s.	d.
By Balance forward from last year	40	3	4
„ Net Profit for year brought forward	547	7	2

£373

£587 10 6

31ST MARCH, 19—

	£	s.	d.	£	s.	d.
1,500	Goodwill, at cost			1,500	0	0
2,000	Freehold Premises, at cost			2,000	0	0
	Furniture and Fittings, at cost to					
	31st March, 19—	351	6	1		
	Additions at cost during year to date	70	0	0		
		421	6	1		
	Deduct : Provision for deprecia-					
	tion, including £18 11s. 3d. for					
	year to date	68	13	3		
351				352	12	10
	Motor Vans, at cost to 31st March,					
	19—	367	6	7		
	Deduct : Provision for deprecia-					
	tion, including £42 10s. 3d. for					
	year to date	197	5	7		
367				170	1	0
4,218				4,022	13	10
	Current Assets :					
	Stock-in-trade, as certified by the					
	Managing Director :					
550	Raw materials and partly manu-					
2,895	factured goods	593	18	1		
	Finished goods	3,110	15	0		
		3,704	13	1		
3,445	Debtors and payments in advance .	1,994	1	5		
1,874	Cash at Bank	368	5	7		
472	Cash in hand	4	2	2		
7				6,071	2	3
5,793				£10,093	16	1
£10,016						

knowledge and belief were necessary for the purposes of our audit. In our opinion examination of those books. We have examined the above Balance Sheet and In our opinion and to the best of our information and according to the explanations 1948, in the manner so required and the Balance Sheet gives a true and fair view Account gives a true and fair view of the profit for the year ended on that date.

(Signed) Accurate & Co.
Chartered Accountants.
Auditors.

Chapter IX

INCORPORATION OF A PRIVATE LIMITED COMPANY

THE rapid growth in the number of companies incorporated during recent years, particularly in the number of Private Limited Companies, is ample testimony to the advantages to be derived from incorporation.

Apart from the obvious advantage of limitation of liability, the raising of capital and loans for the purpose of the business can usually be arranged without difficulty under approved conditions, and extensions and amalgamations of interests may be carried out without unduly disturbing the businesses involved. That valuable incentive to efficiency—"A stake in the business"—can be given to employees, and the ownership of the concern can be shared by an unlimited number of members, except in the case of a Private Limited Company, where the number of shareholders must be restricted to fifty persons exclusive of past and present employees. A further important advantage is that the death of a member does not necessarily involve the closing or disposing of the business, which so frequently happens in the case of a sole trader or partnership. The sale of the holding of a deceased member can usually be arranged, or the shares divided according to the testamentary wishes of the deceased, without interfering with the conduct of the business.

Where a sole trader or partners are liable to Sur-tax the question of incorporation possesses a further advantage. In the case of individuals, this tax is payable on the whole of the profits over the Sur-tax limit before any sums are placed to reserves. A company, however, is not liable to pay Sur-tax unless it can be proved that the company has withheld from distribution to its shareholders an unreasonable amount of its profits. It therefore follows that reasonable sums placed to reserve by a Private Limited Company do not suffer Sur-tax, as in the case of a sole trader or partners.

In this chapter we shall consider the steps to be taken by a

sole trader or partners who wish to convert their business into a Private Limited Company. The procedure simply involves the sale of the undertaking to the newly-formed company in return for shares which are allotted to the proprietors.

Where the vendor of the business taken over is a sole trader, the matter is comparatively simple, since he will be allotted shares to the agreed net value of the assets (after deduction of any liabilities taken over), including any value placed on Goodwill. Where outside capital is also being introduced some differentiation may be necessary, for example by the creation of Preference Shares or the variation of voting rights so as to safeguard the control by the old proprietor, or partners, who may be governing directors of the new company.

Further considerations arise where the vendor is a partnership, the members of which do not, under their agreement, share profits and losses equally, although their capitals may be the same. For example, assume the case of two partners, A and B, with equal capitals and sharing as to one-third and two-thirds respectively. While the allotment to the partners of an equal number of, say, £1 Ordinary Shares would satisfy their requirements as regards capital, B would suffer a loss of one-sixth of his annual income. There are several possible methods of overcoming such a difficulty: probably the simplest is for A to pay B privately a sum of money to buy the increased share in the profits; alternatively, £1 Preference Shares may be allotted to A and B for the amounts of their capitals, the dividend on which would replace the usual interest on partnership capital, and Ordinary or Deferred Shares (taking the residue of the profits) allotted for cash as to one-third to A and two-thirds to B, so that the old partnership profit-sharing basis would, in effect, be preserved.

STEPS IN THE CONVERSION

The first step in the conversion of a business into a Private Limited Liability Company is to decide what assets are to be taken over. Since the State demands stamp duty of £2 per cent. on the value of the property passing under the conveyance, a conservative valuation is necessary. The Nominal Capital also attracts duty at the rate of 10s. per cent. and should be fixed at an amount sufficient to cover the valuation of the assets to be purchased for shares, plus whatever shares are to be issued for cash, and a reasonable margin of capital for future requirements.

The stamp duty on the contract for sale attaches in respect

of all assets not capable of manual delivery, including Plant and Machinery, Fixtures and Fittings, Debtors, and the like. It is customary therefore to exclude from the transfer such items as Debtors and Creditors, the vendor undertaking to be responsible for the collection of outstanding debts and the payment of creditors as at the date from which the company takes over the business.

Among the assets to be transferred will be the Goodwill attaching to the old business. This is an important matter in many cases where the vendor has built up a valuable connection and reputation for service among his customers. For the purpose of preserving continuity of goodwill, companies frequently take the same name as that under which the vendor traded, with the addition of the word "Limited." Where the proprietors of the old business are the sole shareholders in the company, the financial value placed on Goodwill transferred is not so important and is often omitted. In cases where outside capital and new shareholders are being introduced, a proper value should be placed on the Goodwill of the business, otherwise the new shareholders will acquire a share in an asset for which they have not paid. The amount of the valuation is usually arrived at by multiplying the average profits of the old business by an agreed figure representing so many years' purchase.

Having agreed the basis of the transfer, the assets to be included, and their value, these facts are then embodied in a contract for sale made between the vendors and the nominees (usually the future directors) on behalf of the new company.

PROFITS AND LOSSES PRIOR TO INCORPORATION

A company cannot carry on business or acquire profits until it is incorporated, and in the case of a public company a special Certificate to Commence Business is necessary. It is not usually possible or convenient, however, to prepare the accounts of the old business up to the exact date of incorporation. It is therefore usual for the Sale Agreement to provide for the assets to be taken over as from the date of the last Balance Sheet of the vending concern, the business thus becoming the property of the company as from that date. Profits made between the date of the last Balance Sheet and the incorporation of the company thus belong to the company and are capital profits. These profits cannot be paid to the shareholders as dividends, but must be retained in the Balance

Sheet in the form of a capital reserve or used to write down fixed assets such as Goodwill.

The Sale Agreement may provide that the profits prior to incorporation shall belong to the vendor, in which case the amount of the profits when ascertained will be credited to the account of the vendor pending payment to him.

A "rule of thumb" method of ascertaining the amount of profits made between the date of the last Balance Sheet and the incorporation of the company is to divide the profit revealed by the first accounts of the company on a simple time basis, the proportion based on the number of days from the date of the last Balance Sheet to the date of incorporation being regarded as profits prior to incorporation.

But since the sales and therefore the profits in the two periods may have varied considerably, the following procedure is usually adopted :

- (1) Ascertain Net Sales before and after incorporation.
- (2) Apportion the Gross Profit in the ratios of Net Sales.
- (3) Deduct from the Gross Profit prior to incorporation a due proportion of the fixed charges such as rent, office salaries, etc., calculated on a time basis but excluding any expenses such as Directors' Fees and Debenture Interest, which apply solely to the company.
- (4) The difference between the apportioned charges and the Gross Profit prior to incorporation represents the Net Profit to be carried to Capital Reserve.

(5) The remainder of the Net Profit for the first year (or other accounting period) represents the profit available for dividends to the shareholders of the company.

Should the period prior to incorporation unfortunately show a loss, such loss can be deducted from future profits, or charged to Goodwill as representing an additional cost of acquiring the vendor's business. On the other hand, if the Sale Agreement provides that losses prior to incorporation shall be borne by the vendor, any such loss when ascertained will be debited to the account of the vendor pending payment by him.

MEMORANDUM AND ARTICLES OF ASSOCIATION

It is not the intention or province of the author to discuss in detail the purely legal matters connected with the formation of limited companies ; this subject is fully covered in other specialised books of the publishers. It is necessary, however,

for the sake of completeness, to mention certain legal documents which must be prepared.

Memorandum of Association. This may be broadly described as the Charter of the Company. It sets out the company's powers and the objects for which it is formed, and consists of five main parts :

(1) The name of the company (previously approved by the Registrar of Companies) with " Limited " as the last word.

(2) The domicile of the registered office (i.e., the country in which it will be situated).

(3) The objects for which the company is being formed.

(4) A statement that the liability of members is limited.

(5) The amount of the share capital with which the company is to be registered and its division into shares.

It is important that the powers and objects should be clearly and widely stated, since after registration these can be altered only after confirmation by the Court in accordance with Section 5 of the Companies Act, 1948.

The Memorandum must be signed by two persons, called " Subscribers," who are sufficient to form a Private Company as opposed to seven in the case of a Public Company, each subscriber taking at least one share.

Articles of Association. Every Company must possess and register with the Registrar of Companies Articles of Association. The First Schedule (Part I) to the Companies Act, 1948, contains a model set of Articles known as Table A which may be adopted by a Public Company. With the addition of the special clauses contained in Part II of the First Schedule, this model set of Articles may be adopted by a Private Company. It is usual, however, for companies to frame their own Articles and wholly or partly exclude the contents of Table A. In this connection the reader will find that the draft set of Articles prepared by the publishers can usually be adapted for use, and the expense of specially prepared Articles considerably reduced.

The special clauses which must be included in the Articles of a Private Company provide for the following (Section 28, Companies Act, 1948) :

(1) Restriction in some form of the right of members to transfer shares.

(2) Limitation of the number of members to fifty, not including present employee-members or past employees who became members during their employment with the Company.

(3) Prohibition of the issue of shares or debentures to the outside public.

Whereas the Memorandum of Association is the document defining the powers of the company *vis-à-vis* the outside world, the Articles are the bye-laws and regulations governing the internal affairs and conduct of the company. Unlike the Memorandum of Association, which can only be varied within certain limits, the Articles can be altered by the members of the company by the passing of a Special Resolution (i.e., a resolution passed by a three-fourths majority of the members at a meeting of which twenty-one days' notice specifying the proposed Special Resolution has been given).

In addition to the clauses already mentioned, the Articles contain regulations dealing with such matters as the powers, appointment, and remuneration of directors ; calling of meetings and notices thereof ; regulations regarding the use of the company's seal ; use of proxies ; payment of interest and dividends, and the power to reduce and vary the capital, subject to the consent of the Court.

DOCUMENTS TO BE FILED WITH REGISTRAR

In order that the authorities may be sure the affairs of a Limited Company are being conducted with a proper regard to the provisions of the Companies Act, and that information regarding the activities of the company shall be available for the general public, every company is required to furnish a number of Returns to the Registrar of Companies. These Returns are collected into a file for each company, which is open to inspection by any member of the public on payment of the prescribed fee of 1s. at the Registrar's offices in Bush House, London.

The following list indicates briefly the usual Returns which must be made. The actual forms are in many instances laid down by the Act, and may be obtained ready for completion from the publishers of this book and other company stationers.

In the case of a Private Company the following documents must be filed prior to Incorporation :

(1) Printed copy of the Memorandum and Articles of Association signed by the subscribers ; stamp, as deeds, 10s. each. The Memorandum also attracts an *ad valorem* duty according to the scale shown in the twelfth schedule to the Companies Act, 1948, ranging from a minimum of £2 to a maximum of £50. A registration fee of 5s. is payable on the Articles.

(2) A Statement of the Nominal Capital and its division into shares ; stamp duty at the rate of 10s. per cent.

(3) A Statutory Declaration by a solicitor acting in the formation of the company, or by a director or secretary named in the Articles, that all the legal requirements have been complied with ; fee 5s.

(4) Particulars of Contract of Sale if an existing business is being taken over ; fee 5s.

(5) Notice of Situation of the Registered Office ; fee 5s.

(6) Return of Directors and Secretaries ; fee 5s. This Return may be filed within fourteen days after the date of incorporation, if inconvenient to file prior to incorporation.

In addition to the above documents a Public Company must also file :

(7) Consent of Directors to Act ; fee 5s.

(8) Written undertaking by each director to acquire and pay for qualification shares where they are not signatories to the Memorandum ; fee 5s., together with a 6d. agreement stamp in respect of each signature if the nominal value of the shares exceeds £25. The contract to take the shares may be dispensed with where the director has signed the Memorandum for sufficient shares to qualify.

(9) Prospectus, or Statement in Lieu of a Prospectus.

[No Statement need be filed in respect of a Private Company unless underwriting commission is being paid, in which case a Statement in the prescribed form must be filed (Section 53 (1)).]

If the documents set out above are found to be in order, the Registrar will issue a Certificate of Incorporation, and in the case of a Private Company this entitles it to commence business as from the date of the certificate. In the case of a Public Company, a special Certificate to Commence Business must be obtained, and this will be issued only after a further declaration has been filed, stating that the minimum number of shares necessary to provide for the requirements of the company (defined by the fourth schedule of the Act) when a public issue is made has been received, and that the directors have paid the due proportion on their shares.

Return of Allotments. Within one month of allotting shares, whether on the first or later issues, a Return, bearing a 5s. fee stamp, must be made, giving particulars of the shares allotted, distinguishing between those allotted for cash and those allotted for a consideration other than cash. The Return also

states the names, addresses, and descriptions of the shareholders, with the number of shares held by each.

Mortgages and Charges. Particulars of all charges on the property of a company, including debentures, must be sent to the Registrar for registration within twenty-one days of the creation of the charge, otherwise the charge will be void against creditors in the event of liquidation of the company. Apart from the *ad valorem* duty of 5s. per cent. which is payable on the charge, the fees payable to the Registrar on registration of the charge are 10s. when the charge does not exceed £200 and £1 when it exceeds £200. When charges, including debentures, are repaid, a Memorandum of Satisfaction (fee 5s.) may be filed, but this is not obligatory.

The Annual Return. One of the most important documents required to be filed by a company is the Annual Return, which must be completed within forty-two days of the annual general meeting held in each year. This document gives a summary of share capital and shares, showing in detail the number of shares issued for cash and otherwise, discount allowed on shares, calls made, calls in arrears, shares forfeited, and share warrants issued; the total indebtedness of the company on debentures, etc.; and in the case of a Public Company a copy of the last Balance Sheet including every document required by law to be annexed thereto, together with a copy of the report of the auditors.

A Private Company must include in its Annual Return a certificate to the effect that no public invitation has been made to subscribe for its shares or debentures since the last Return, and where the number of shareholders exceeds fifty, that the excess consists of employees or ex-employees.

The Return must also include particulars of Directors and Secretaries, and a list of all persons who hold shares in the company, or have held them since the date of the last Return, with, in the latter case, the dates on which they ceased to be members.

The Return must also state where the register of members is kept if it is not kept at the registered office of the company.

Unless the Private Limited Company is an "exempt private company" within the meaning of Section 129 of the Companies Act, 1948, a copy of the last Balance Sheet and annexed documents must be filed with the Annual Return. The main conditions which qualify a company as an "exempt private company" are (a) that no body corporate is a holder of any of its shares or debentures and no person other than the holder

has any interest in the shares and debentures, (b) that the number of persons holding debentures of the company is not more than fifty, and (c) that no body corporate is a director of the company and no arrangement is in existence whereby the policy of the company can be determined by persons other than the directors, members and debenture holders or the trustees for the debenture holders.

The majority of private companies already fulfil these conditions and will therefore continue to be exempt from filing accounts with the Annual Return.

The provisions of Section 130 of the Companies Act, 1948, relating to the Statutory Meeting and Report, do not apply to a Private Limited Company, and as this book is primarily intended for use in connection with this class of company, it is not considered necessary to deal with the provisions of the section.

This chapter is by no means a detailed exposition of the process of converting an existing business into a limited liability concern, but the main steps have been covered in sufficient detail for the reader to obtain a broad outline of the procedure. The preparation of the legal documents is, of course, placed in the hands of a solicitor, and the registration is usually carried out by Company Registration Agents, who have the necessary facilities and experience to perform the work in an economical and expeditious manner.

Chapter X

CONVERSION OF A BUSINESS INTO A PRIVATE LIMITED COMPANY

BOOK-KEEPING ENTRIES

THE necessary legal steps to be taken on the conversion of a business into a Private Limited Company having been indicated in the previous chapter, consideration will now be given to the book-keeping entries required, together with some practical suggestions as to suitable books.

As mentioned in Chapter IX, it is necessary for a Balance Sheet to be prepared as at the date from which the business is to be acquired by the company, and for a decision to be made as to what assets are to be taken over and the values of such assets, including Goodwill. These details are embodied in a contract for sale from which the particulars are taken for closing the books of the vendors' business and opening the books of the new company.

An illustration is given of an actual case dealt with in practice, with variations in certain details to amplify general principles.

Example. J. Alvan and S. Roberts, trading in partnership and sharing profits as to two-thirds and one-third, decided to convert their business into a Private Limited Company with an authorised capital of £7,000, divided into 5,800 6 per cent. Cumulative Preference Shares of £1 each and 1,200 Ordinary Shares of £1 each, the partners receiving shares at par value in exchange for their interests in the assets to be taken over by the company.

The last Balance Sheet of the partnership, dated March 31st, 19—, is given, and the contract for sale dated May 10th, 19—, provided for assets to be taken over as from the date of this Balance Sheet at the following values :

	£
Goodwill	1,200
Plant and Machinery	2,000
Fixtures and Fittings	500
Stock-in-Trade	1,500
Cash ex balance at Bank . . .	500
	£5,700

BALANCE SHEET AS AT MARCH 31, 19—

Liabilities						Assets					
	£	s.	d.	£	s.	d.		£	s.	d.	
Creditors				784	11	0	Plant and Machinery at cost, less depreciation		2,080	15 0	
Capital Accounts							Fixtures and Fittings at cost, less depreciation		579	10 0	
J. Alvan	2,660	10	8				Stock-in-Trade, as valued by Partners	1,502	9	6	
S. Roberts	2,315	8	6				Debtors		969	10 6	
	--	--	--	4,975	19	2	Cash at Bank		628	5 2	
				£5,760	10	2			£5,760	10 2	

In order to provide additional working capital the company on the same date issued to sundry persons 4 per cent. Debentures at par totalling £1,000, the cash being received on May 18th.

The book-keeping procedure involves the closing of the books of the partnership through the medium of Journal entries from which the items are posted to the relative accounts in the ledgers. The Journal entries, Nominal Ledger accounts, and the Cash Book entries are shown together with the Purchases and Sales Ledger Control Accounts, but the separate personal accounts of the debtors and creditors are omitted owing to limit of space. It has been assumed that the debts were collected by May 31st, with the exception of £24 10s. 6d., which proved to be irrecoverable, and that the liabilities were paid by the same date less allowances given amounting to £18 11s. 0d.

It is necessary to open a "Realisation" Account and to transfer to the debit of that account the book values of each of the assets which are being assigned to the company.

JOURNAL ENTRIES

(In Partnership Books)

			<i>Dr.</i>			<i>Cr.</i>		
19—			£	s.	d.	£	s.	d.
Mar. 31	Realisation Account . . . <i>Dr.</i>	6	4,662	14	6			
	To Plant and Machinery	3				2,080	15	0
	„ Fixtures and Fittings	4				579	10	0
	„ Stock-in-trade	5				1,502	9	6
	„ Cash at Bank	40				500	0	0
	(Being transfer of assets taken over by A. & R., Ltd.)							
May 10	Preference Shares in A. & R., Ltd. <i>Dr.</i>	7	4,500	0	0			
	Ordinary Shares in A. & R., Ltd. „	8	1,200	0	0			
	To Realisation Account					5,700	0	0
	(Being shares in A. & R., Ltd., taken as purchase consideration of the assets transferred to A. & R., Ltd.)							
May 10	J. Alvan's Capital Account <i>Dr.</i>	1	800	0	0			
	S. Roberts's Capital Account „	2	400	0	0			
	To Ordinary Shares in A. & R., Ltd.					1,200	0	0
	(Being Ordinary Shares in A. & R., Ltd., divided between Partners according to their profit-sharing ratios of two-thirds and one-third.)							
May 10	J. Alvan's Capital Account <i>Dr.</i>	1	2,250	0	0			
	S. Roberts's Capital Account „	2	2,250	0	0			
	To Preference Shares in A. & R., Ltd.					4,500	0	0
	(Being Preference Shares in A. & R., Ltd., divided between Partners in equal shares.)							
May 31	Realisation Account . . . <i>Dr.</i>	2	24	10	6			
	To Debtors	10				24	10	6
	(Being sundry debts written off as irrecoverable.)							
May 31	Creditors <i>Dr.</i>	9	18	11	0			
	To Realisation Account	6				18	11	0
	(Being allowances given by Creditors.)							
May 31	Realisation Account . . . <i>Dr.</i>	6	1,031	6	0			
	To J. Alvan's Capital Account	1				687	10	8
	„ R. Roberts's Capital Account	2				343	15	4
	(Being profit realised on assets taken over by A. & R., Ltd., and transferred to Partners' Capital Accounts.)							

NOMINAL LEDGER

(In Partnership)

1.	<i>Dr.</i>				J. ALVAN
19—					
May 10	To Ordinary Shares in A. & R., Ltd.	J/32	£	s.	d.
" 10	" Preference Shares in A. & R., Ltd.	"	800	0	0
" 31	" Cash	40	2,250	0	0
			298	1	4
			£3,348 1 4		

2.	<i>Dr.</i>				S. ROBERTS
19—					
May 10	To Ordinary Shares in A. & R., Ltd. .	J/32	£	s.	d.
" 10	" Preference Shares in A. & R., Ltd.	"	400	0	0
" 31	" Cash	40	2,250	0	0
			9	3	10
			£2,659 3 10		

3.	<i>Dr.</i>				PLANT AND
19—					
Mar. 31	To Balance b/f.	✓	£	s.	d.
			2,080	15	0

4.	<i>Dr.</i>				FIXTURES
19—					
Mar. 31	To Balance b/f.	✓	£	s.	d.
			579	10	0

5.	<i>Dr.</i>				STOCK-IN-
19—					
Mar. 31	To Trading A/c	✓	£	s.	d.
			1,502	9	6

6.	<i>Dr.</i>				REALISATION
19—					
Mar. 31	To Sundry Assets transferred . . .	J/32	£	s.	d.
May 31	" Bad Debts	"	4,662	14	6
" 31	" Profit on Realisation transferred to Partners' Capital A/cs :		24	10	6
	J. Alvan, two-thirds	"	687	10	8
	S. Roberts, one-third	"	343	15	4
			£5,718 11 0		

ACCOUNTS

Books)

CAPITAL ACCOUNT

Cr.

19—			£	s.	d.
Mar. 31	By Balance b/f.	✓	2,880	10	8
May 31	„ Profit on transfer of business	J/32	687	10	8
			£3,348	1	4

CAPITAL ACCOUNT

Cr.

19—			£	s.	d.
Mar. 31	By Balance b/f.	✓	2,315	8	6
May 31	„ Profit on transfer of business	J/32	343	15	4
			£2,659	3	10

MACHINERY

Cr.

19—			£	s.	d.
Mar. 31	By Realisation A/c	J/32	2,080	15	0

AND FITTINGS

Cr.

19—			£	s.	d.
Mar. 31	By Realisation A/c	J/32	579	10	0

TRADE

Cr.

19—			£	s.	d.
Mar. 31	By Realisation A/c	J/32	1,502	9	6

ACCOUNT

Cr.

19—			£	s.	d.
May 10	By Preference Shares in A. & R., Ltd.	J/32	4,500	0	0
„ 10	„ Ordinary Shares in A. & R., Ltd.	„	1,200	0	0
„ 31	„ Allowance by Sundry Creditors	„	18	11	0
			£5,718	11	0

7.

*Dr.**PREFERENCE SHARES*

19— May 10	To Realisation A/c	J/32	£	s.	d.
			4,500	0	0
			£4,500 0 0		

8.

*Dr.**ORDINARY SHARES*

19— May 10	To Realisation A/c	J/32	£	s.	d.
			1,200	0	0
			£1,200 0 0		

9.

*Dr.**PURCHASES LEDGEI*

19— May 31	To Cash	40	£	s.	d.
	„ Allowances	J/32	766	0	0
			18	11	0
			£784 11 0		

10.

*Dr.**SALES LEDGEI*

19— Mar. 31	To Balance b/f.	✓	£	s.	d.
			969	10	6
			£969 10 6		

40.

*Dr.**CASH*

19— Mar. 31	To Balance b/f.	✓	£	s.	d.
May 31	„ Book Debts collected	40	628	5	2
			945	0	0
			£1,573 5 2		

The Realisation Account is credited with the purchase consideration and a reciprocal debit made in the Cash Book if the consideration is being paid in cash, or, as in this case, the debit is made to Shares Accounts if shares are being

IN A. & R., LTD.

Cr.

19—				£	s.	d.
May 10	By Partners' Capital A/cs :					
	J. Alvan	J/32		2,250	0	0
	S. Roberts	"		2,250	0	0
				£4,500	0	0

IN A. & R., LTD.

Cr.

19—				£	s.	d.
May 1	By Partners' Capital A/cs :					
	J. Alvan	J/32		800	0	0
	S. Roberts	"		400	0	0
				£1,200	0	0

CONTROL (CREDITORS)

Cr.

19—				£	s.	d.
Mar. 31	By Balance b/f.	✓		784	11	0
				£784	11	0

CONTROL (DEBTORS)

Cr.

19—				£	s.	d.
May 31	By Cash	40		945	0	0
" 31	" Bad Debts	J/32		24	10	6
				£969	10	6

BOOK

Cr.

19—				£	s.	d.
May 1	By A. & R., Ltd.	J/32		500	0	0
" 31	" Creditors	40		766	0	0
" 31	" Partners' Capital A/cs :					
	J. Alvan	1		298	1	4
	S. Roberts	2		9	3	10
				£1,573	5	2

taken in satisfaction. The Shares Accounts are then closed by a transfer to the debit of the Partners' Capital Accounts according to the value of shares they have agreed to take.

The book debts collected by the partners are entered on the

receipts side of the Cash Book as and when the amounts are received, and posted to the credit of the personal accounts in the Sales Ledger, the total collected being credited to the Sales Ledger Control Account as shown in the example. The amounts paid to Creditors are entered on the payments side of the Cash Book when cheques are drawn and debited to the personal accounts of the creditors in the Purchases Ledger, the total being debited to the Purchases Ledger Control Account.

Through the medium of Journal entries the total of the bad debts, amounting to £24 10s. 6d., is debited to Realisation Account and the individual amounts credited to the personal accounts in the Sales Ledger. The total is taken to the credit of the Sales Ledger Control Account, which now balances.

The allowances given by creditors are also passed through the Journal, the personal accounts in the Purchases Ledger being debited and the Realisation Account credited with the total of £18 11s. 0d. The total is debited to the Purchases Ledger Control Account, which can now be closed.

The credit balance on Realisation Account, amounting to £1,037 5s. 6d., represents the realised surplus on the transfer of the business to the company, and the account is closed by a transfer to the Capital Accounts of the partners according to their profit-sharing ratios of two-thirds and one-third. If the Realisation Account shows a debit balance the amount represents a loss on realisation and is debited to the partners in the same ratios. Readers will appreciate that the Realisation Account is, in effect, a Profit and Loss Account, and the final balance thereon is a profit or loss of the proprietor or partners of the business which is being acquired.

The final stage is the transfer of the remaining cash in hand or at the bank to the partners. If the book-keeping work has been correctly carried out the cash balance should equal the total standing to the credit of the partners' Capital Accounts and the books are closed by drawing cheques and posting the amounts from the payments side of the Cash Book to the debit of the partners' Capital Accounts.

Book Debts and Liabilities. In the previous chapter it was pointed out that it is usual for the vendor to collect the outstanding amounts due from customers and to accept responsibility for the payment of the creditors at the date the business is acquired by the company in order to save the stamp duty of £2 per cent. payable on the book debts and liabilities, and the example already given assumes that these items are excluded. Under certain circumstances, however, it may be necessary or

desirable that the company shall acquire the book debts and assume responsibility for the creditors, subject to an undertaking by the vendor to indemnify the company against any liabilities which have not been taken into consideration.

In order that the assignment of the book debts may be valid, it will be necessary to notify each debtor in writing that the debt is being taken over by the company, and this is usually done in the form of a suitably worded combined circular letter addressed to the customers by the vendors and the new company. It is also advisable to inform the creditors that their claims will be paid by the company.

Assuming that the company is acquiring the book debts for £945, and is to be responsible for the £766 due to sundry creditors of the vendors, the closing Journal entries already shown will require modification and will appear as follows :

		Dr.			Cr.		
		£ s. d.			£ s. d.		
19—							
Mar. 31	Realisation Account Dr.	6	5,607	14 6			
	To Plant and Machinery	3			2,080	15 0	
	„ Fixtures and Fittings	4			579	10 0	
	„ Stock-in-Trade	5			1,502	9 6	
	„ Debtors	10			945	0 0	
	„ Cash at Bank	40			500	0 0	
	(Being transfer of Assets taken over by A. & R., Ltd.)						
19—							
Mar. 31	Creditors Dr.	9	766	0 0			
	To Realisation Account	6			766	0 0	
	(Being Creditors taken over by A. & R., Ltd.)						

The debit of £5,607 14s. 6d. to Realisation Account now includes the book debts totalling £945, the latter figure being credited in individual amounts to the accounts of the debtors in the Sales Ledger and the total taken to the credit of the Sales Ledger Control, which can now be closed.

The creditors' accounts in the Purchases Ledger are closed by debiting the accounts with the balances taken over by the company and the Realisation Account credited with the total of £766. The latter figure is debited to the Purchases Ledger Control Account, which is then closed.

Revised ledger accounts are not shown owing to limit of space, but the modification simply means that the purchase

price which the company is paying for the business is increased by £179 (the difference between the book debts and liabilities taken over), and assuming that this is being paid by the company to the partnership in cash or an equivalent amount in shares at par, the profit realised on the transfer of the business will be the same as shown in the previous example.

OPENING THE BOOKS OF THE NEW COMPANY

The company having been incorporated, the assets acquired and the liabilities (if any) assumed by the company in accordance with the contract of sale are brought into the company's books by means of Journal entries. The values placed on the assets for book-keeping purposes usually follow those stated in the contract, although they may be amended if necessary.

Referring to the example given, the amounts of the various assets taken over are posted from the Journal to the debit of the respective accounts, including the entry of £500 to the receipts side of the Cash Book, and the total credited to the Purchase of Business Account in the Nominal Ledger.

From the next Journal entry a debit is made to the Purchase of Business Account and a credit to the account of the vendors of the purchase price of £5,700. This closes the Purchase of Business Account which has served the purpose of a permanent record of the amount paid for the business.

On May 10th the Preference and Ordinary Shares are allotted to the vendors, and the Journal entry comprises a debit to the Vendors Account (thereby closing this account) and a credit to the Preference and Ordinary Share Capital Accounts.

These three simple Journal entries and postings to the accounts complete the recording of the acquisition of the business. The remaining Journal entry deals with the issue of the £1,000 4 per cent. Debentures and the amount is posted to the debit of the Debenture Holders Account and to the credit of Debentures Account. The former account is closed by a credit entry from the receipts side of the Cash Book when the money is received from the debenture holders on May 18th.

The payment of £185 covering the formation or preliminary expenses is recorded on the payments side of the Cash Book and debited to Preliminary Expenses Account. At the end of the first accounting period this account is usually closed by a transfer to Profit and Loss Account. If the formation expenses are heavy and the directors so desire, they may be charged to the Profit and Loss Accounts by instalments during the first

two or three years. In such a case the balance of the preliminary expenses carried forward each year is shown on the assets side of the Balance Sheet, but as the item is of no realisable value the whole should be written off to Profit and Loss Account as soon as possible.

The relative Nominal Ledger Accounts are shown together with an Opening Trial Balance which is taken out to prove the correctness of the book-keeping entries.

The example selected is a simple one; in practice many other problems arise requiring special entries, but these should present no difficulty to readers who have grasped the principles explained in this chapter.

A. & R., LTD.

JOURNAL ENTRIES

(In Company's Books)

1.		Dr.			Cr.			
			£	s.	d.	£	s.	d.
19—								
May 10	Sundry Assets : <i>Dr</i>							
	Goodwill	1	1,200	0	0			
	Plant and Machinery	4	2,000	0	0			
	Fixtures and Fittings	8	500	0	0			
	Stock-in-Trade	12	1,500	0	0			
	Cash	1	500	0	0			
	To Purchase of Business Account	15				5,700	0	0
	(Being Sundry Assets acquired by company under contract of sale dated May 10, 19—)							
May 10	Purchase of Business Account <i>Dr</i>	15	5,700	0	0			
	To Vendors	17				5,700	0	0
	(Being agreed purchase price of business acquired by company as per contract of sale dated May 10, 19—)							
May 10	Vendors <i>Dr</i>	17	5,700	0	0			
	To 6% Cum. Preference Shares	18				4,500	0	0
	„ Ordinary Shares	20				1,200	0	0
	(Being allotment to the vendors of 4,500 6% Cum. Preference Shares of £1 each, at par, and 1,200 Ordinary Shares of £1 each at par, both fully paid as per contract of sale dated May 10, 19—)							
May 18	Sundry Debenture Holders <i>Dr</i>	22	1,000	0	0			
	To 4% Debentures	24				1,000	0	0
	(Being 4% Debentures issued this day.)							

NOMINAL LEDGER ACCOUNTS

(In Company's Books)

1.

<i>Dr.</i>		GOODWILL				<i>Cr.</i>	
19— May 10	To Purchase of Business A/c .	J/1	£ 1,200				£

4.

<i>Dr.</i>		PLANT AND MACHINERY				<i>Cr.</i>	
19— May 10	To Purchase of Business A/c .	J/1	£ 2,000				£

8.

<i>Dr.</i>		FIXTURES AND FITTINGS				<i>Cr.</i>	
19— May 10	To Purchase of Business A/c .	J/1	£ 500				£

12.

<i>Dr.</i>		STOCK-IN-TRADE				<i>Cr.</i>	
19— May 10	To Purchase of Business A/c .	J/1	£ 1,500				£

15.

<i>Dr.</i>		PURCHASE OF BUSINESS ACCOUNT				<i>Cr.</i>	
19— May 10	To Vendors .	J/1	£ 5,700	19— May 10	By Sundry Assets	J/1	£ 5,700

17.

<i>Dr.</i>		VENDORS' ACCOUNT				<i>Cr.</i>	
19— May 10	To Preference Share Capital .	J/1	£ 4,500	19— May 10	By Purchase of Business .	J/1	£ 5,700
	„ Ordinary Share Capital .	„	1,200				
			5,700				5,700

18.

Dr. 6% PREFERENCE SHARE CAPITAL Cr.

			£	19— May 10	By Vendors .	J/1	£ 4,500
--	--	--	---	---------------	--------------	-----	------------

20.

Dr. ORDINARY SHARE CAPITAL Cr.

			£	19— May 10	By Vendors .	J/1	£ 1,200
--	--	--	---	---------------	--------------	-----	------------

22.

Dr. SUNDRY DEBENTURE HOLDERS Cr.

19— May 18	To 4% Debentures	J/1	£ 1,000	19— May 18	By Cash .	1	£ 1,000
---------------	------------------	-----	------------	---------------	-----------	---	------------

24.

Dr. 4% DEBENTURES Cr.

			£	19— May 18	By Sundry Deben- ture Holders .	J/1	£ 1,000
--	--	--	---	---------------	------------------------------------	-----	------------

26.

Dr. PRELIMINARY EXPENSES Cr.

19— May 10	To Cash .	1	£ 185				£
---------------	-----------	---	----------	--	--	--	---

1.

Dr. CASH BOOK Cr.

19— May 10	To Purchase of Business A/c.	J/1	£ 500	19— May 10	By Preliminary Expenses .	26	£ 185
" 18	" Sundry Deben- ture Holders.	22	1,000	" 18	" Balance c/d.	✓	1,315
			<u>1,500</u>				<u>1,500</u>
May 19	To Balance b/d.	✓	1,315				

A. & R., LTD.

OPENING TRIAL BALANCE—MAY 18th, 19—

	Folio	Dr.	Cr.
Goodwill	1	£ 1,200	£ .
Plant and Machinery	4	2,000	
Fixtures and Fittings	8	500	
Stock-in-Trade	12	1,500	
6% Preference Share Capital	18		4,500
Ordinary Share Capital	20		1,200
4% Debentures	24		1,000
Preliminary Expenses	26	185	
Cash at Bank	1	1,315	
		£6,700	£6,700

Book Debts and Liabilities Taken Over. If the company is taking over the book debts and liabilities of the vendors, amounting to £945 and £766 respectively, and paying the difference of £179 in cash to the vendors as mentioned on page 106, the opening entries will be as follows :

19—		Dr.	Cr.
May 10	Sundry Assets : <i>Dr.</i>		
	Goodwill	1 1,200 0 0	£ s. d.
	Plant and Machinery	4 2,000 0 0	
	Fixtures and Fittings	8 500 0 0	
	Stock-in-Trade	12 1,500 0 0	
	Debtors	27 945 0 0	
	Cash	1 500 0 0	
	To Purchase of Business Account	15	6,645 0 0
	(Being sundry assets acquired by the company under contract of sale dated May 10th, 19—)		
May 10	Purchase of Business a/c <i>Dr.</i>	15 766 0 0	
	To Creditors	30	766 0 0
	(Being liabilities assumed by the company under contract of sale dated May 10th, 19—)		
May 10	Purchase of Business a/c <i>Dr.</i>	15 5,879 0 0	
	To Vendors	17	5,879 0 0
	(Being agreed purchase price of business acquired by company as per contract of sale dated May 10th, 19—)		

The values of the assets, as stated in the contract of sale, are debited, as before, to the respective Nominal Ledger Accounts, and the opening cash posted to the receipts side of the Cash Book. The total of the book debts assigned to the company is debited to a Sales Ledger Control Account and the individual amounts posted to the debit of the customers' accounts in the new Sales Ledger. The total value of the assets, amounting to £6,645, is credited to the Purchase of Business Account.

The total claims of the sundry creditors assumed by the company are credited to a Purchases Ledger Control Account, and the amount due to each creditor posted to the credit of the individual accounts in the new Purchases Ledger. The total of £766 is debited to the Purchase of Business Account, thus reducing the credit balance on that account to £5,879, the net purchase consideration. The purchase price given in the previous example was £5,700, and assuming that the extra amount of £179 (the difference between the book debts and liabilities taken over) is paid to the vendors by the company in cash, the Purchase of Business Account is closed by a posting of £179 from the payments side of the Cash Book to the debit of Purchase of Business Account.

The opening Trial Balance will then be as follows :

A. & R., LTD.

OPENING TRIAL BALANCE—MAY 18th, 19—

	Folio	Dr.	Cr.
		£	£
Goodwill	1	1,200	
Plant and Machinery	4	2,000	
Fixtures and Fittings	8	500	
Stock-in-Trade	12	1,500	
6% Preference Share Capital	18		4,500
Ordinary Share Capital	20		1,200
4% Debentures	24		1,000
Preliminary Expenses	26	185	
Debtors	27	945	
Creditors	30		766
Cash at Bank	1	1,136	
		<u>£7,466</u>	<u>£7,466</u>

INITIAL TRADING TRANSACTIONS

In the previous chapter it was pointed out that it is not usually possible or convenient to prepare the accounts of the vendor's business up to the exact date of the incorporation of the company. In the example which is being considered the last Balance Sheet of the partnership was prepared on March 31st, and the company incorporated on April 30th. Under the terms of the contract of sale, dated May 10th, the company acquired the assets, including the benefit of the trading as from March 31st. As the records of the company could not be commenced until it was in existence, the question arose as to a suitable and practical method of recording the transactions as from March 31st until May 10th, when the contract of sale was sealed and the assets transferred.

In the case in question, the decision to convert the business into a Private Limited Company was made prior to March 31st, and the plan was adopted of opening a separate banking account on April 1st, into which all receipts referring to sales subsequent to March 31st were paid and on which all cheques for transactions entered into after that date were drawn. Moneys received after March 31st, referring to sales effected prior to that date, were paid into the partnership bank account, as the book debts were not assigned to the company. Similarly, the liabilities of the partnership were paid by cheques drawn on the partnership bank account.

A completely new set of books was commenced on April 1st, and continued when the company was formed. The separate banking account opened on April 1st was closed when the account of the new company was opened on May 10th, and the balance transferred thereto.

When the book debts and liabilities are being taken over by the new company, the procedure is further simplified by the fact that the whole of the receipts may be paid into the separate bank account opened on the day from which the company takes over, and all payments made therefrom.

Frequently, the decision to convert the business into a Private Limited Company is not made until after the date of the final Balance Sheet, and it is not desirable or convenient to prepare a later Statement of Affairs. In such cases the transactions which have been carried out on behalf of the company since the date of the last Balance Sheet and passed through the books of the vendors must be reversed by means of Journal entries, credit being given to the company for cash

collected and a debit made for amounts paid on its behalf. The difference between the amounts collected and amounts paid is then settled by a cash payment between the partnership and the company.

In the company's books reciprocal entries are made bringing in the transactions carried out on its behalf by the vendors whose account is debited with amounts collected, and credited with amounts paid on behalf of the company.

It will be apparent to readers that the simplicity or complexity of the book-keeping entries necessary on the conversion of a business into a Private Limited Company will largely depend on the terms under which the business is being assigned. Complicated propositions do not usually appeal to persons who contemplate taking an interest in a Private Limited Company, and the incorporation of a company on plain straightforward terms is most desirable and can usually be achieved.

SUITABLE BOOKS

The Author has heard business men put forward the suggestion that the conversion of their business into a Private Limited Company would necessitate such a complete upheaval of their book-keeping methods that the process would not be worth while. The degree of change will, of course, depend very largely on the method under which the present book-keeping of the business is conducted, and if the simple requirements of the Companies Act, 1948, as regards the keeping of books are not already met, it suggests that a drastic change of system is necessary in any event.

Assuming that the book-keeping system already in use is arranged on correct double-entry principles, practically no alteration is necessary. The Nominal Ledger will contain an account for the Share Capital and an account for Debentures, if the latter are being issued, instead of the customary Capital Account of the Sole Trader or Partners. If and when dividends and interest are paid, Nominal Ledger accounts will be opened to record the payment of these items. Readers will, no doubt, agree that these simple variations do not justify the book-keeping system being regarded as a deterrent to company incorporation.

If convenient and desirable, the present subsidiary books in use may be continued on the formation of the company, provided they have proved satisfactory in practice. The Sales and Purchases Ledgers may also be continued if the book debts and liabilities are being taken over by the company, although

new loose-leaf ledgers may be preferable if the ledgers of the Vendors are of the old-fashioned bound type. A new Nominal Ledger is recommended and also a Control Ledger where the Self-balancing System is being applied to more than two ledgers.

Throughout the previous chapters it has been explained that the type of books required varies according to the nature of the business and the volume of transactions, and specimen rulings have been shown for various classes of trades from which readers may adapt rulings suitable for their own particular requirements.

Generally speaking, the type and number of books required will largely depend upon whether credit is given to customers, or the sales are made for cash only. It is therefore proposed to divide the selection of books between those required for (a) a cash trade and (b) a business in which credit is allowed customers.

The following is a summary of the books which will normally be found necessary, and the chapter in which they are dealt with in this treatise is indicated for reference purposes.

CASH TRADE

1. Till Roll records or Cash Sale duplicates and summaries (Chapter II).

2. Cash Book—to record cash received and banked on the debit side and cheque payments on the credit side (Chapter II).

If the number of entries is considerable, it is advisable to record the cash received in a Cash Received Book and the cheque payments in a separate Cheque Payments Book, as suggested in Chapter II.

3. Petty Cash Book (Chapter II).

4. Purchases and Returns Outward Day Book (to include the recording of expenses when possible and advisable—Chapter III).

The Returns Outwards (Purchases Returns) are shown as deductions in the Purchases Day Book, as explained in Chapter III. If, however, the items are numerous, a separate Returns Outwards Book is recommended—Chapter III.

5. Purchases Ledger (Chapter IV).

The loose-leaf form of ledger kept on the self-balancing principle is recommended—see Chapter V.

Under certain circumstances, as mentioned in Chapter III, Purchases and Purchases Return Day Books and Ledgers may be dispensed with, in which case it will be necessary to pay strict attention to the filing of the invoices and receipted statements to comply with Sections 147 and 331 of the Companies Act, 1948.

6. Journal Proper (Chapter III).

Bills Payable, and also Bills Receivable in the case of a Credit Trade, may be entered in the Journal Proper, but when the bill transactions are numerous, separate Bills Payable and Bills Receivable Journals are necessary (Chapter III).

7. Nominal or Private Ledger (Chapter VI).

The Purchases Ledger Control Account (and also the Sales Ledger Control Account in a Credit Trade) may be kept in the Nominal Ledger in the case of small businesses. Where, however, more than one ledger is kept, a separate Control Ledger on the lines indicated in Chapter V will be found more convenient.

CREDIT TRADE

In addition to the foregoing books, a credit trade calls for proper credit sales records, and the following books will be found necessary :

8. Sales Day Book (bound or loose-leaf type whichever is the more suitable, as discussed in Chapter III).

9. Returns Inwards (Sales Returns) Day Book (bound or loose-leaf type, as explained in Chapter III).

10. Sales Ledger (Chapter IV).

The loose-leaf form of ledger kept on self-balancing principles, as suggested in Chapter V, is recommended.

MEMORANDUM BOOKS

Apart from the double-entry book-keeping records, most businesses find it necessary to record memorandum data varying in detail according to the nature and size of the business.

Salaries and Wages should be properly recorded in a Salaries and Wages Book showing the necessary detail and agreed in total with the amount of the salaries and wages cheque drawn each pay-day.

The proper recording of stock is also a matter of considerable importance in some trades as explained in Chapter VII, and suitable Stock Books are required.

Again, the Machinery and Plant Register or Ledger suggested in Chapter VII is essential in businesses where machinery is used extensively.

The " Statutory " books which every company is required to keep are dealt with in the following chapter.

Chapter XI

A COMPANY'S ACCOUNTS—STATUTORY PROVISIONS

As the granting of the right to carry on trade with " Limited Liability " is regarded as a privilege, certain duties and responsibilities are placed by Statute on limited companies. One branch of these duties relates to the keeping of books of account. The ordinary sole trader, or partnership, keeps such records as may be required for private information only ; companies are compelled by law to keep certain books, both financial and statistical, and even in the case of private companies part at least of the information contained therein is available to the public.

Such books may be divided into two classes : first, the Cash Book, Purchases and Sales Books, and Ledgers, commonly known as " Financial Books " ; second, the various records which must be kept of members, directors, copies of the Annual Returns and the like, commonly known as " The Statutory Books."

THE FINANCIAL BOOKS

The principal regulations regarding the financial records which a company is required to keep are contained in Sections 147 to 152 of the Companies Act, 1948, and the Eighth Schedule to that Act, and these provisions are summarised in this chapter.

The everyday records which must be maintained are set out in Section 147, where it is directed that a company shall cause to be kept proper books of account with respect to :

(a) All sums of money received and expended by the company, and the matters in respect of which the receipt and expenditure takes place.

(b) All sales and purchases of goods by the company.

(c) The assets and liabilities of the company.

It will be seen that these requirements are fully satisfied by keeping Cash Books, Purchases and Sales Day Books, Bought and Sales Ledgers, and a Private or Nominal Ledger, on the lines set out in the preceding chapters of this book.

Section 147 also states that the books of account must give a true and fair view of the state of the company's affairs and explain its transactions.

It is further laid down that the books must be kept at the registered office of the company, or at such other place as the directors see fit, and must at all times be open to inspection by the directors.

If any director fails to take reasonable steps to secure compliance by the company with this section, or causes any default by the company, then, if in the opinion of the Court the offence was committed wilfully, he is liable to imprisonment for six months or a fine not exceeding £200 unless he can prove that he had reasonable grounds to believe and did believe that a competent and reliable person was charged with the duty of seeing that those requirements were complied with and was in a position to discharge that duty.

Moreover, if the company is unsuccessful and is wound up, a further penalty is provided by Section 331 of the Act. Here it is stated that failure to keep "proper books of account" in the two years before winding up (the definition of proper books of account corresponding, broadly, with that in Section 147) renders a manager or other officer, as well as the directors, liable to imprisonment, unless he can prove that he acted honestly or that the circumstances excused the breach. This period of two years is reduced to the period between the incorporation of the company and the commencement of the winding up if this period is shorter than two years.

THE ANNUAL ACCOUNTS

In addition to the regulations just considered regarding the day to day book-keeping records, the Act also contains directions in respect of the annual accounts to be prepared. By Section 148, the directors of companies trading for profit must lay before the shareholders at a general meeting a Profit and Loss Account once at least in each calendar year. The first account must be presented not later than eighteen months after the incorporation of the company, and in all cases the Profit and Loss Account must be laid before the shareholders in general meeting within nine months of the end of the period to which the accounts relate (twelve months if the company has foreign interests). If these time-limits cannot be complied with, the Board of Trade has power to extend them if it thinks fit.

In the case of a company not trading for profit, the same provisions apply, but the name Income and Expenditure Account is substituted for Profit and Loss Account ; this applies to such bodies as Learned and Professional Societies, and similar organisations registered as Limited Companies.

In addition to the Profit and Loss Account or Income and Expenditure Account the directors must also lay before the company in general meeting a Balance Sheet as on the terminal date of the account, with a report from the directors. This report (Section 157) is to give the directors' opinion as to the state of the company's affairs, the dividend which the directors recommend, and the amount which they propose to carry to reserve within the meaning of the Eighth Schedule to the Act. The penalty for non-observance of the provisions of Sections 148 and 157 is six months' imprisonment or a fine of £200, for wilful default.

The Act gives general instructions as to the contents of the Balance Sheet and Profit and Loss Accounts. The overriding provision of Section 149 states that the Balance Sheet shall give a true and fair view of the state of the affairs of the company as at the end of its financial year and that the Profit and Loss Account shall give a true and fair view of the profit or loss of the company for the financial year. This general provision is followed by a direction that the Balance Sheet and Profit and Loss Account shall comply with the requirements of the Eighth Schedule to the Act. Special directions are given in Part II of the Eighth Schedule where the Company is a holding or subsidiary company, whilst Part III deals with exceptions for special classes of companies.

The general provisions applicable to the usual type of company are clearly set out in Part I of the Eighth Schedule. These provisions are additional to those contained in Sections 196 and 197 of the Companies Act, 1948, regarding the disclosure in the accounts of particulars of directors' salaries, pensions, etc., and particulars of loans to officers, etc., respectively.

A clear understanding of Part I of the Eighth Schedule by all those engaged in company administration is necessary, and the provisions of Part I are therefore reproduced in full as an appendix to this edition.

SUBSIDIARY COMPANIES

The problems regarding subsidiary companies may not be of major importance in connection with the type of company

generally considered here. A Private Limited Company may, however, purchase a competing business and run it in its original name, or it may arrange to carry on an allied business by means of a company, specially formed for the purpose, under a name other than that of the parent company. In either case, the provisions of the Companies Act, 1948 (Sections 150 to 153), and the directions given in Part II of the Eighth Schedule regarding subsidiary companies must be observed, and these regulations are summarised below.

Where a company holds shares in another, is the other company a subsidiary? The Act gives three broad tests (Section 154).

(1) Does one company control the composition of the board of directors of the other company?

(2) Do the shares held by one company amount to more than one-half in nominal value of the equity share capital of the other company?

(3) Is one company a subsidiary of any company which is that other's subsidiary?

If the answer to any one of these questions is "yes," then the second company is a subsidiary company within the meaning of the Act.

The expression "equity share capital" refers to the issued capital of a company after deducting capital which is not entitled to participate in a distribution of dividends or capital beyond a specified amount. Usually the equity is the total of the issued Ordinary share capital of a company.

Where this relationship of holding and subsidiary company exists, the provisions of Part II of the Eighth Schedule of the Companies Act, 1948, must be observed. Section 150 of the Act introduces the obligation to lay group accounts before the holding company, whilst Section 151 gives general guidance as to the form of the group accounts. Section 152 repeats the over-riding rule that the accounts shall give a "true and fair view" of the state of affairs and the profit and loss of the company, including the subsidiaries as a whole, and states that the group accounts shall comply with the requirements of the Eighth Schedule or give the same or equivalent information.

The contents of Part I of the Eighth Schedule have been given in full as an appendix. Certain modifications of and additions to these requirements as regards holding companies are given in Part II of the Eighth Schedule, summarised as follows:

(1) The aggregate amount of assets consisting of shares in or amounts owing *from* the subsidiaries shall be shown separately

in the Balance Sheet from all the other assets, and the aggregate amount of indebtedness to the company's subsidiaries shall be so set out separately from its other liabilities.

(2) There shall be shown by way of note on the Balance Sheet or in a statement or report annexed, details of the amount of shares in and debentures of the company, held by its subsidiaries or their nominees, with certain exceptions

(3) Where group accounts are not submitted, a statement shall be annexed to the Balance Sheet showing :

(a) the reason why subsidiaries are not dealt with in group accounts ;

(b) the aggregate amount of the subsidiaries' profits after deducting the subsidiaries' losses (or *vice versa*) for the current and previous financial years ;

(c) any qualifications contained in the report of the auditors of the subsidiaries on their accounts for their respective financial years.

The presentation of the accounts of holding and subsidiary companies is not within the intended scope of this book. Readers who wish to study the matter further are referred to books which have been specially written on the matter.

SIGNING AND CIRCULATING THE ACCOUNTS

The Balance Sheet which is to be laid before the company must be signed on behalf of the board by two of the directors of the company, or, if there is only one, then by that one. The Profit and Loss Account, duly approved by the Board of Directors, must be annexed to the Balance Sheet and the Auditors' Report attached.

The law naturally wishes to safeguard the shareholders as far as possible, and careful provisions are therefore made by Section 158 of the Companies Act, 1948, regarding the rights to receive copies of the annual accounts.

Briefly, Section 158 provides that a copy of every Balance Sheet, including every document required by law to be annexed thereto (i.e. the Profit and Loss Account, the Directors' Report, and the statements required by Part II of the Eighth Schedule), which is to be laid before a company in general meeting, together with the Auditors' Report, must, not less than twenty-one days before the meeting, be sent to every member of the company, every holder of debentures in the company, and all other persons entitled to receive notices of general meetings.

Penalties for the non-observance of these various provisions are set out in the Act.

EXAMPLE OF AN ANNUAL REPORT AND ACCOUNTS

The following is an example of the report of directors and the usual form of abbreviated accounts circulated and submitted to shareholders at the Annual General Meeting.

The attention of readers is drawn to the treatment of taxation in the Balance Sheet. The item is divided between (a) current taxation grouped under the heading "Current Liabilities and Provisions" and (b) future Income Tax grouped under the heading "Revenue Reserves." Current taxation amounting to £7,500 refers to Profits Tax payable on the profits shown by the Accounts, plus Income Tax based on the profits of the preceding year. This amount is a known liability and payable on January 1st, the day after the date of the Balance Sheet, and represents a current liability or provision. The item of £6,500 refers to Income Tax normally based on the profits shown by the accounts, but payable on January 1st twelve months after the date of the Balance Sheet. The item may therefore be described as a Reserve and grouped under the heading "Revenue Reserves."

X. Y. Z., LIMITED
DIRECTORS' REPORT

The Directors have pleasure in submitting to the Shareholders audited Accounts of the Company and their report for the year ended December 31st, 19—.

The Directors are glad to record that sales and profits showed increases during the past year, the results of which are reflected in the Accounts.

	£
The net profit for the year ended December 31st, 19—, after charging Debenture Interest, Directors' Fees and providing for Depreciation, was	17,000
<i>To which is added:</i>	
The balance brought forward from the previous year	11,000
<i>Making a total of</i>	28,000
After providing for	
Profits Tax	£3,000
Income Tax (balance of current liability)	500
Income Tax (reserve for future liability).	6,500
Transfer to General Reserve	2,000
	12,000
<i>There remains a balance of</i>	16,000
The Directors recommend the payment of a dividend of 4%, free of tax, on the Ordinary Shares requiring	6,000
<i>Leaving a balance to be carried forward of</i>	£10,000

The Directors retiring in rotation are Messrs. C. Kent and B. Sussex, who, being eligible, offer themselves for re-election.

The Auditors, Messrs. Accurate & Co., having expressed their willingness to continue in office, a motion will be proposed at the meeting fixing their remuneration.

(Signed) A. BERKS, Chairman.

B. SURREY, Managing Director.

February 10th, 19—.

X. Y. Z., LTD.

PROFIT AND LOSS ACCOUNT

19— (Previous year)		
£		£
4,000	To Debenture Interest	4,000
2,000	„ Directors' Fees	2,000
9,000	„ Provision for Depreciation	8,100
13,000	„ Balance, Net Profit for the year, carried down	17,000
<u>£28,000</u>		<u>£31,100</u>
2,000	To Profits Tax (estimated liability based on profits for the year)	3,000
6,000	„ Income Tax, balance of current liability (£500) and reserve for future liability based on profits for the year (£8,500)	7,000
1,500	„ Transfer to General Reserve	2,000
4,500	„ Proposed Dividend of 4%, free of tax, on Ordinary Shares for the year	6,000
11,000	„ Balance carried forward to next year	10,000
<u>£25,000</u>		<u>£28,000</u>

X. Y. Z., LTD.

BALANCE SHEET

19— (Previous year)		£	£
£			
£150,000	<i>Share Capital :</i>		
	Authorised :—		
	150,000 Ordinary Shares of £1 each	£150,000	
150,000	Issued :—		£150,000
	150,000 Ordinary Shares of £1 each, fully paid		
	<i>Revenue Reserves :</i>		
	General Reserve at December 31st, 19—	26,000	
	Add Transfer for year to date	2,000	
26,000		28,000	
5,500	Reserve for future Income Tax based on profits for year to date	6,500	
11,000	Profit and Loss Account, Balance unappropriated	10,000	
			<u>44,500</u>
<u>£192,500</u>			<u>194,500</u>
	<i>Long-term Liabilities :</i>		
£80,000	Fixed Mortgage Debentures at 5% (Secured on Freehold Land and Buildings, per contra)		80,000
41,100	<i>Current Liabilities and Provisions :</i>		
6,000	Creditors and accrued expenses	35,400	
4,000	Current Taxation	7,500	
	Members for proposed dividend of 4% (free of tax) on Ordinary Shares for year to date	6,000	
<u>£51,100</u>			<u>48,900</u>
<u>£323,600</u>			<u>£323,400</u>

REPORT OF THE AUDITORS TO THE

We have obtained all the information and explanations which to the best of our proper books of account have been kept by the Company so far as appears from our annexed Profit and Loss Account which are in agreement with the books of account, given us the said accounts give the information required by the Companies Act, 1948, state of the Company's affairs as at December 31st, 19—, and the Profit and Loss

Stevenage House,

London, E.C.1.

February 3rd, 19—.

FOR THE YEAR ENDED DECEMBER 31st, 19—

19— (Previous year)		£
£		
27,500	By Profit on trading after charging all expenses and	
500	providing for contingencies	30,500
	„ Income from Investments	600
<u>£28,000</u>		<u>£31,100</u>
13,000	By Net Profit for year brought down	17,000
12,000	„ Balance brought forward from last year	11,000
<u>£25,000</u>		<u>£28,000</u>

31st DECEMBER, 19—

19— (Previous year)		£	£
£			
20,000	<i>Fixed Assets :</i>		
14,000	Goodwill, at cost		20,000
120,000	Patents and Trade Marks, at cost		14,000
	Freehold Land and Buildings, at cost		120,000
	Plant and Machinery, at cost	100,000	
	Deduct : Provision for depreciation, in- cluding £8,100 for year to date	27,100	
81,000			72,900
<u>£235,000</u>			<u>226,900</u>
	<i>Current Assets :</i>		
30,500	Stocks of Materials and Stores, as certified by the Managing Director	32,400	
17,800	Debtors and Bills Receivable	18,100	
20,000	Investments in Government Securities (market value at date £21,000)	20,000	
20,300	Cash at Bank and in Hand	26,000	
<u>£88,600</u>			96,500
<u>£323,600</u>			<u>£323,400</u>

(Signed) A. BERKS } Directors.
B. SURREY }

MEMBERS OF MESSRS. X.Y.Z., LTD.

knowledge and belief were necessary for the purposes of our audit. In our opinion examination of those books. We have examined the above Balance Sheet and In our opinion and to the best of our information and according to the explanations in the manner so required and the Balance Sheet gives a true and fair view of the Account gives a true and fair view of the profit for the year ended on that date.

(Signed) ACCURATE & Co.,
Chartered Accountants.
Auditors.

THE STATUTORY BOOKS

The Statutory Books and other similar records which a company is required, or finds it convenient to keep, may be obtained, suitably ruled, from the publishers and other company stationers. As the publishers' catalogues will show the rulings in use, it is not considered necessary to reproduce specimens in this book, but in the following paragraphs brief notes are given on the nature and purpose of these records.

Register of Members. The purpose of this Register is to show the names and addresses of the members, stating the shares held by each and the dates of commencing and ceasing to be a member in each case. If there are more than fifty members of the company an index of the members' names must be kept. This can only arise in the case of a Private Limited Company if the excess of fifty members comprises present or past employees who acquired the shares during their employment with the Company. (Section 28, Companies Act, 1948.) The Register shall be kept at the Registered Office or at another office of the Company or at the office of some other person who makes up the Register. If the Register of Members is not kept at the Registered Office of the Company, a notice must be sent to the Registrar of Companies of the place where its Register of Members is kept and any change in that place. The Register may be inspected by members free, or by some other person on payment of the prescribed fee of not more than one shilling.

Register of Directors' Shareholdings. This Register was introduced by Section 195 of the Companies Act, 1948, which requires details to be shown of the shares and debentures of the company and its subsidiaries or holding company which are held by or in trust for each director. This Register must be kept at the Registered Office of the Company and is open for inspection by the Board of Trade at any time and by any member or debenture holder during a period of fourteen days before and three days after the date of the annual general meeting.

Register of Directors and Secretaries. This book must be kept at the Registered Office of the Company. It records the names, addresses, and nationality of all directors of the company. In the case of a Public Company the Register must show the age of any director over 70 years of age who retains his office by virtue of the provisions of Section 185 of

the Companies Act, 1948. The Register must also contain the name and address of the Secretary of the Company. A return showing these particulars must be made to the Registrar of Companies within fourteen days of the appointment of the first directors and secretary, and any changes therein must also be notified to the Registrar within fourteen days.

Register of Mortgages and Charges. This Register is also kept at the Registered Office of the Company and must show details of all charges (including debentures) on the property and assets of the company, whether such charges are fixed or floating, with a short description of the property charged, the amount of the charge, and the names of the persons entitled to the securities unless in the form of securities to bearer. Members and creditors of the company are entitled to inspect this Register free, and any other person is entitled to the same privilege on payment of the prescribed fee not exceeding one shilling. Registration of all mortgages and charges (including debentures) must be effected with the Registrar of Companies within twenty-one days after the creation of the charge, as stated in Chapter IX.

A company must keep at its Registered Office a copy of every instrument creating any charge requiring registration with the Registrar, and the copy must be open for inspection at the Registered Office by any creditor or member without charge.

The Annual Return. As explained in Chapter IX an Annual Return of members must be made to the Registrar of Companies at least once in every calendar year.

The aforementioned Statutory Books may be obtained, bound in one volume, with suitably ruled pages for recording applications for, and allotment of, shares, and a register of share transfers. This combined form of register is very handy for use by a small company, but is obviously impracticable where there are a large number of members whose names, addresses, and shareholdings must be recorded.

Minute Book. A company is required to keep Minute Books in which to record the proceedings of all general meetings, and also to record the meetings of directors and managers (Section 145). When signed by the Chairman of the meeting, or by the Chairman of the succeeding meeting, the minutes are evidence of the proceedings. The Minute Book containing the proceedings of any Annual General Meeting shall be kept at the Registered Office of the Company and shall be open to inspection by any member without charge.

The subject of loose-leaf or card records is referred to in Section 436 of the Companies Act, 1948, which states that where any register, index, or minute book or book of account is not kept in bound book form, adequate precautions shall be taken for safeguarding against falsification and facilitating its discovery. It is considered that the terms of this section will be fulfilled if there is an efficient system of locking the binder in such a way that leaves may not be inserted or withdrawn without the knowledge of more than one official of the company, coupled with an infallible means of identifying the leaves by numbers and the signature of the chairman on each leaf. In small companies where it is not possible to obtain such a degree of control over the binder the ordinary bound form of minute book should be used.

Chapter XII

THE CAPITAL OF A COMPANY

THE capital which a sole trader or a partnership employs in a business is a flexible amount, the proprietors being free to increase or decrease it as they wish. A Limited Company, on the other hand, must be registered with a stated capital on which duty is paid, and although the whole of this amount need not be issued, it may be *exceeded* in total only by compliance with the formalities set out in the Companies Act, while even more stringent regulations apply to the return of capital to the proprietors or shareholders once the capital has been paid up.

Share capital represents the interest of the proprietors in the capital of the business. Debentures, which are sometimes referred to as capital, are in fact long-term indebtedness. They are issued to persons who lend money to the concern as creditors and not as proprietors. The holders of debentures are entitled to a fixed rate of interest on the sums they have contributed whether the company makes profits or not, and are given, in the majority of cases, the right to step in and seize the assets, or certain property as defined by the deed, should default be made in the payment of interest or the repayment of principal when due.

FORMS OF SHARE CAPITAL

Whatever priority particular classes of shares may enjoy, no dividends can be paid on any of them unless the company has profits available for the purpose. As between themselves, however, it is customary to vary the rights of different classes of shares, by giving to some of them preferential rights as regards dividend, and in some cases as regards repayment of capital on winding-up. These priorities which attach to fixed dividend shares are important, and it is usually found that the greater the priority and security of dividend the lower the fixed rate of dividend.

In the following summary of the different types of share capital, the classification commences with the share carrying

the greatest priority. Shares which have no priority and are dependent for their return on the residue of profits after the shares carrying preferential or fixed dividends have been satisfied are usually referred to nowadays as "Equity Shares."

Cumulative Preference Shares. The holders of these shares are given the right to a dividend at a fixed rate before the "junior shareholders" (i.e., those having less priority) receive any dividend, and, moreover, if in any year the profits are insufficient to pay the fixed dividend, the arrears are carried forward until such times as sufficient profits are made to enable preference dividends, including the arrears, to be paid. No dividends on the junior classes of shares may be paid until these arrears have been met.

Preference Shares. These shares give the holders the right to a fixed rate of dividend before the junior classes of shareholders are paid a dividend. The rights are not cumulative, so that if profits are insufficient to pay a dividend, the holders have no claim on future profits for the arrears.

In addition to their fixed dividend right, Preference Shares are sometimes given a portion of the residue of profits; they are then known as "Participating Preference Shares."

Redeemable Preference Shares. Section 58 of the Companies Act, 1948, authorises the issue of Redeemable Preference shares, subject to certain conditions. These conditions include a provision to the effect that the shares must be redeemed out of profits normally available for dividend, or out of the proceeds of an issue of new shares made for the purposes of the redemption.

Any class of Preference Shares may enjoy the right to priority of repayment of capital on a winding-up, although in the absence of provisions to this effect the right does not automatically attach. It is important that the rights should be clearly defined in the Articles of Association, as to whether, for instance, the Preference shareholders have the right to share in a surplus which remains on a winding-up, after all shareholders have been paid in full.

Ordinary Shares. The bulk of the share capital of most companies is in the form of Ordinary Shares. These give the right to dividends from the remainder of the profits, subject to provision for reserves, etc., after the Preference Shares have received their fixed dividend. They may be further subdivided into Preferred and Deferred Ordinary Shares, the former being entitled to a priority rate of dividend in preference to the latter.

Deferred Shares. Where these exist the dividend rates on all senior classes of shares are fixed, and after these have been paid the residue goes to the deferred shareholders. In a prosperous company the Deferred Shares may thus obtain a high rate of return and are frequently of correspondingly high value.

Management or Founders' Shares. This class of share is sometimes issued where a business formerly carried on by a sole trader or a partnership is acquired by a company. These shares correspond normally to Deferred Shares with a right to the residue of profits after the other shareholders have received their dividends.

Stock. Shares which are fully paid up may, by resolution of the company, be changed into Stock. This may then be divided into any amount, whereas shares cannot be subdivided. There is no intrinsic difference between shares and stock.

Share Warrants. A company, if its Articles allow (Section 83), may also issue "Share Warrants" under its seal, which entitle the holder to the shares specified; in this event the shares must be fully paid. Such an issue is not allowed in the case of a Private Company. The warrants are transferable by delivery and dividends are provided for by means of coupons attached.

Reserve Capital. A company may by Special Resolution declare that part of its uncalled capital shall not be called up except in the event, and for the purpose, of a winding-up. Reserve capital cannot be changed back into share capital without leave of the Court, and it cannot be charged by the directors or otherwise dealt with.

DEBENTURES

As already stated, a debenture holder is not a proprietor but a creditor of the company. The usual form of debenture is known as a Mortgage Debenture, conferring a charge on part or the whole of the assets of the company and ranking in priority to the claims of ordinary creditors. The rights of the debenture holders are defined in the debenture or in the Trust Deed, setting out the conditions under which the issue is made and usually appointing Trustees to watch the interests of the debenture holders in the property which forms the subject of the charge.

A debenture may not carry a charge of any kind and it is then nothing more than an acknowledgment of indebtedness by

the company. Such debentures are termed Simple, or Naked, Debentures, and are seldom met with in practice.

The most common form of debenture is one which gives what is known as a "Floating Charge" over the whole or part of the assets of the company. The term "floating" means that the charge covers such assets as may vary in value and identity from day to day, e.g., book debts, work in progress, stock, cash, etc., including uncalled capital. The company is free to deal with its assets in the ordinary course of trade, so long as the terms of the debentures are observed. These terms provide that the charge crystallises when the interest is in arrear, or when the principal monies are due but not paid, or when the property of the company is in jeopardy. In any of these events the debenture holders have the right to appoint a Receiver to realise the assets charged and repay the principal and interest due.

An important point to observe in the case of debentures carrying a floating charge is that under Section 322 of the Companies Act, 1948, such a charge created within twelve months of the commencement of the winding up of the company is void except to the extent of the cash actually paid to the company in consideration of the charge with interest at the rate of 5 per cent. per annum, unless it can be proved that the company was solvent immediately after the charge was created.

Debentures may give a specific or "fixed" charge over specified assets belonging to the company, usually freehold land and buildings, the deeds of which are deposited with the Trustees for the debenture holders.

All debentures creating or secured by any charge must be registered with the Registrar of Companies within twenty-one days of creation as mentioned in the preceding chapter.

When it is anticipated that an issue of debentures will be required, it should be seen that the directors' borrowing powers, which may be limited and defined in the Articles of Association, are sufficient to cover the amount; otherwise it may be necessary to revise the Articles.

A practical point which should be borne in mind by business men, especially those interested in Private Limited Companies, is that the creating of Mortgage Debentures may have the effect of restricting the credit of the company. The registration of debentures becomes public knowledge and suppliers are often wary of allowing credit to a company which is burdened with a large debenture indebtedness. In such cases creditors frequently insist upon guarantees being given by the

directors, thus nullifying the advantage of limited liability to a great extent. However, the judicious creation of debentures accompanied by the good reputation of those responsible for the company is, generally speaking, no bar to the enjoyment of reasonable credit.

GENERAL STRUCTURE OF CAPITAL

It may be said in general terms that it is to the interest of the Ordinary Shareholder that as much as possible of the capital requirements of the company shall be satisfied either by debentures or by preference shares taking fixed interest rates, provided the rates of interest or dividend are low. The residue of the profits remaining for the Ordinary Shareholder will then, obviously, be larger. The debenture holders, however, will be mainly concerned with their security, and in the absence of assets specifically charged to them, their security increases with the amount of share capital which has been issued. The Preference Shareholders, again, will usually feel more secure with a large ordinary share capital behind them, so that the final structure of the capital of the company will largely depend on a careful balancing of these requirements as to security.

The amount of nominal or authorised capital of a company is stated in the Memorandum, and the total amount cannot be exceeded without passing the requisite Ordinary or Special Resolution and filing with the Registrar of Companies the required form of Notice of Increase of Capital (fee 5s.) and a Statement of Increase of Capital (stamp duty at the rate of 10s. per cent.). If a Special Resolution is required by the Articles of the Company, such resolution must be printed and also filed with the Registrar (fee 5s.).

The actual division of the capital into ordinary and preference shares (or other classes) may be set out in the Memorandum, but is more usually defined in the Articles of Association, since, in the latter case, the arrangements are more easily modified when necessary.

In the event of circumstances arising under which it is necessary to reduce the capital, either by repaying capital which has been subscribed and which is found to be in excess of the needs of the company, or by writing off capital which has been lost, reference should be made to Sections 66 to 71 of the Companies Act, 1948, where the full provisions are set out.

Chapter XIII

DIVIDENDS—CAPITAL AND REVENUE—RESERVES

A distinctive feature of company organisation is the provision for at least an annual division of profits among shareholders. The income paid to shareholders in the form of dividends presents one of the most difficult problems of company accounting, namely, what profits are available for dividends. The law has always been opposed to any payment which amounted to the return of capital to shareholders by way of dividend, and a clear distinction between revenue receipts and capital is therefore necessary.

The fund normally available for the declaration of dividends is the final credit balance of Profit and Loss Appropriation Account, being the Net Profit for the year plus the balance of profits brought forward from the previous year and not divided or carried to reserve. Occasionally, however, profits of a capital nature, arising, for instance, on the sale of land or other fixed asset, may be included. Again, profits available for dividend may be swollen by reason of the fact that insufficient provision has been made for the depreciation of fixed assets.

A number of cases have been before the courts for consideration in this connection, and on account of the decisions the following rules are put forward as broadly summarising the position :

(1) Fixed Assets may be sunk and lost but yet the current surplus may be divided. In other words, depreciation need not be provided before arriving at a profit on such assets as asphalt deposits, land and property, and the like.

(2) Floating Capital must be kept up. Any losses in assets such as stock-in-trade or debtors must be charged against revenue.

(3) Profits of a capital nature, for example the sale of an asset at a price exceeding its cost, may be used for dividend purposes if the profits are actually realised (a mere writing up in book value is insufficient) and if they remain on an all-round revaluation of assets, and such division is not prohibited by the company's Articles.

The following example and Journal entries necessary to record dividends in the books of a company will indicate the book-keeping procedure.

On May 1st, 19—, W. & W., Ltd., declares and pays a dividend of 8 per cent. on £10,000 Preference Shares and 10 per cent. on £20,000 Ordinary Shares.

		<i>Dr.</i>	<i>Cr.</i>
19—		£	£
May 1	Profit and Loss Appropriation A/c <i>Dr.</i>	400	
	To Preference Dividend		400
	(Being a dividend of 8 per cent., less tax, on the Preference Shares for year ended as per resolution dated, 19 —.)		
„	Profit and Loss Appropriation A/c <i>Dr.</i>	1,000	
	To Ordinary Dividend		1,000
	(Being a dividend of 10 per cent., less tax, on the Ordinary Shares for year ended as per resolution dated, 19—.)		
„	Preference Dividend <i>Dr.</i>	400	
	Ordinary Dividend „	1,000	
	To Cash		1,400
	(Being payment of above dividends, less tax at 10s. in the £.)		

Note.—In practice the last entry would be shown in the Cash Book.

If a dividend is declared “free of tax” (i.e., tax is not deducted by the company on payment), the dividend at the rate actually declared is shown as a debit to Appropriation Account.

BONUS SHARES

It is sometimes found advisable to declare a dividend payable in the form of a distribution of the company's shares and not in cash. In this case the dividends which would otherwise be paid to the shareholders are in effect retained by the company and used to pay for fresh shares issued to members. The Bonus Shares are issued to the existing shareholders in proportion to their holdings, for example one share for each ten held. In such a case it is necessary to provide for the fractions of shares to which shareholders might be entitled but which of course cannot be issued ; these may be sold to a

shareholder by arrangement and the proceeds of the fractions distributed among those entitled to the fractions.

When large Reserves have accumulated an amount is often appropriated from the Reserve for the purposes of the share bonus as well as the existing balance of undistributed profits in the Profit and Loss Appropriation Account.

An example follows of the payment of a dividend in the form of bonus shares together with the necessary Journal entries.

On May 1st, 19—, A. C. B., Ltd., declares a bonus of 50 per cent. payable in fully paid Ordinary Shares on the existing £50,000 Ordinary Shares, such bonus to be provided as to £12,000 from Appropriation Account, and the remainder from General Reserve. The entries in the financial books for this transaction are :

		Dr.	Cr.
19— May 1	Profit and Loss Appropriation A/c Dr.	£ 12,000	£
	General Reserve A/c „	13,000	
	To Bonus Dividend A/c		25,000
	(Being dividend of 50 per cent. on Ordinary Shares for year ended payable in fully paid shares, as per resolution dated May 1st, 19—.)		
„	Bonus Dividend A/c Dr.	25,000	
	To Ordinary Share Capital A/c.		25,000
	(Issue of Bonus Shares in payment of dividend for year ended)		

Note.—The type of resolution authorising the issue will depend on the provisions of the company's Articles. It may be necessary in the first place for the Nominal Capital to be increased.

RESERVES AND PROVISIONS

The true financial position of a company may be difficult or impossible to assess owing to absence of information or insufficient distinction being made between the various classes of reserves or provisions. The following notes are intended as a general guide to the reader in preparing a Balance Sheet so that the financial position of the company is not obscured by the inaccurate treatment of reserves and provisions.

Sometimes the expression "reserve" is used to describe the bringing into account of sums set aside for specific requirements, commitments, contingencies, and the shrinkage in value of existing assets. These adjustments are, however,

more properly described as "provisions," as suggested in Chapter VII, the term "reserve" being used to denote amounts set aside out of profits and other surpluses which are not intended to meet any specific liability, commitment, or contingency, but are free to strengthen generally the financial position of the company.

Part IV of the Eighth Schedule to the Companies Act, 1948, restricts the use of the word "Provision" to any known liability of which the amount cannot be determined with substantial accuracy. Where the amount of a known liability is ascertainable, the item should be described as a liability or accrual and grouped with creditors in the Balance Sheet.

Provisions for depreciation and diminution in values of assets should be deducted from the assets to which they relate and shown accordingly in the Balance Sheet.

The sub-division of reserves under a variety of headings is not generally necessary. The broad principle to apply is to divide reserves not normally regarded as available for distribution as dividend from those of a revenue nature from which dividends may be declared.

The term "Reserve Fund" refers to amounts placed to reserve and invested in marketable and earmarked assets outside the business.

Allocations to reserve form an important factor in the growth of most companies, and a prudent Board of Directors will make adequate appropriations from profits for the purpose of strengthening a company's reserves to such a degree that its resources may be strong enough to meet any contingencies which the future may reveal.

Sometimes the proportion of profits to be carried to reserve is fixed by the Articles, but usually the company is governed in the matter of reserves by an article containing similar provisions to those in Table A, which empower the directors to set aside out of the profits of the company, before recommending any dividend, such sums as they think proper to form a reserve or reserves which shall, at the discretion of the directors, be applicable for meeting contingencies, or for equalising dividends, or for any purpose to which the profits of the company may be properly applied. Provided the directors act bona fide and in the interests of the company, their action in transferring profits to reserve cannot be upset by the shareholders.

The Eighth Schedule to the Companies Act, 1948, provides that if the amounts are material, the source of any increase in capital or revenue reserves (other than provisions for depreci-

ation, renewals, or diminution in value of assets) must be shown in the Accounts or Directors' Report. Conversely, the destination of any sums taken from reserves must be indicated. It should also be noted that under Section 157 of the Companies Act, 1948, the Directors' Report must show the amount which they propose to carry to the Reserve Fund, General Reserve, or Reserve Account shown specifically on the Balance Sheet.

As the reserve is fed by the annual transfers representing corporate savings by the shareholders, it tends as time passes to become an important and permanent feature of the financial arrangements. The share capital no longer represents the true capital employed in the business, and for this reason distributions of bonus shares from the reserve, as already discussed, may be made at the proper time. The property of the company is not increased by the operation, but the capitalisation converts the reserve into a part of the company's permanent capital and therefore makes it immune from a call to meet a future deficiency in earnings.

EXAMPLE OF ALLOCATION TO GENERAL RESERVE

The Directors of D. E. F., Ltd., resolved on March 31st, 19—, to transfer £5,000 to General Reserve from the balance shown by the Appropriation Account. At the Annual General Meeting held on May 15th, 19—, the proposed allocation was confirmed.

The following Journal entries will indicate the book-keeping procedure :

		Dr.	Cr.
19—			
Mar. 31	Profit and Loss Appropriation Account	Dr.	£ 5,000
	To General Reserve		£ 5,000
	(Being transfer to General Reserve as per directors' resolution of March 31st, 19—, and confirmed at the Annual General Meeting held on May 15th, 19—.)		

Chapter XIV

THE FINAL ACCOUNTS

PRESENTATION AND INTERPRETATION

THE final accounts of a Private Limited Company are usually more detailed than those which are presented to the shareholders in a Public Company ; but nevertheless, it is important that the facts should be grouped and summarised in as clear a manner as possible to avoid over-elaboration of detail.

The attention of the accountancy profession has been concentrated for some years prior to the Companies Act, 1948, on the best form of presentation of the accounts of companies. The results are reflected in that Act and the particular attention of readers is called to the contents of the Eighth Schedule, Part I of which has been given in full as an appendix.

Apart from these requirements, the matters given below deserve attention if the accounts are to be of the maximum utility to the business man who requires facts and figures to be presented to him in a concise and readily understandable manner.

The break between Trading (or Manufacturing) Account and Profit and Loss Account should be carefully considered, so as to include in the first section all true manufacturing costs (in the case of a manufacturing business), comprising not only the direct expenses but also a proper charge for rent, lighting, and supervision appertaining to the manufacturing side of the business as distinct from the commercial or selling side.

Any abnormal non-recurrent debit or credit items should be clearly indicated on the face of the accounts, preferably including them in the third or Appropriation Section, thereby enabling the true net profit or loss for the year to be readily ascertained.

Legislative direction has now been given to the modern and useful method of including in the accounts the corresponding amounts of the items in the preceding year, thus facilitating comparison of one year with another.

The fixed assets in the Balance Sheet should be shown at

cost as per the last Balance Sheet, plus cost of additions, or less sales during the year, and less aggregate provisions for depreciation to date of the Balance Sheet. The aggregate amount of the company's investments (other than trade investments) must be shown separately and subdivided between quoted and unquoted investments with a note of the aggregate market value of the quoted investments. Current assets follow and sub-totals shown.

On the opposite side of the Balance Sheet the items are grouped under (a) Share Capital plus (b) Capital and Revenue Reserves, including unappropriated profits, (c) Long-term liabilities, and (d) Current liabilities, including provision for accrued expenses.

An example of a Balance Sheet drawn up on these lines is shown on pages 142 and 143; shillings and pence are omitted.

COMPARATIVE RESULTS AND PERCENTAGES

In order to facilitate comparisons between one period and another, the plan is sometimes adopted of expressing the various expenses, individually or in significant groups, as percentages of the total sales for the period. It is thus possible to see at once whether any expenses have increased more than proportionately to an increase in turnover; such a method will assist in locating any waste or inefficiency. It will be found, normally, that as turnover increases, the percentage of factory rent, salaries, and other standing charges will decrease, but wages may increase more than proportionately where the larger output involves expensive overtime.

Wastage and leakage of goods and errors in stock valuations may be revealed by abnormal fluctuations in the cost of the goods manufactured and sold. Such fluctuations are readily seen if the cost is expressed as a percentage of the total sales. In order to compute the cost of the goods a calculation is required as shown on the next page. (The figures have been taken from the Trading Account shown in Chapter VIII.)

The sales amounted to £11,050 os. 3d., and therefore the cost of the goods sold represents 75·82 per cent. and the Gross Profit 24·18 per cent. of the total sales.

As mentioned in Chapter VIII, if the goods produced by the business in question were valued at trade buying prices, the profit earned by the factory could be separately ascertained, in which case the cost of the goods manufactured could be

expressed as a percentage of the value of the factory production. When a business is solely manufacturing the figures are taken from the Manufacturing Account and the cost of the goods produced expressed as a percentage of the total sales.

COMPUTATION OF COST OF SALES

	£	s.	d.
Opening Stock of Finished Goods	2,895	4	10
Add Prime Cost of Goods Manufactured	2,483	10	8
Purchases, less Returns	6,090	2	2
Carriage on Purchases	20	3	4
	11,489	1	0
Less Closing Stock of Finished Goods	3,110	15	0
Cost of Goods Sold	£8,378	6	0

Apart from the percentage statements considered above, the following percentages may be calculated for the purposes of comparison :

(1) The percentage of Gross Profit to Sales ; this should be reasonably consistent, any large variations being investigated. The cost of sales and gross profit being complementary percentages, any abnormal variations may reflect wastage and leakage or errors in valuations of materials and stock as suggested above, although variations will occur if the markets have been subject to wide fluctuations in prices during the period covered by the accounts.

(2) The percentage of Net Profit to Sales or Gross Profit as a check on the expenses incurred.

(3) The percentage of Net Profit (*a*) to Issued Share Capital and (*b*) to Capital employed, i.e., Share Capital, Reserves, and Undistributed Profits, to determine if a fair return is being earned on the money invested in the business.

(4) On the Balance Sheet, the percentage of Fixed and Current Assets to Total Assets to ensure proper distribution of capital.

WORKING CAPITAL

The working capital of a company represents the difference between the liquid or current assets of the business (i.e., cash

19— (Previous year)			£	£
		<i>Share Capital :</i>		
		Authorised :—		
		50,000 6% Cumulative Preference Shares of		
50,000		£1 each	50,000	
50,000		50,000 Ordinary Shares of £1 each	50,000	
			<u>£100,000</u>	
		Issued :—		
		50,000 6% Cumulative Preference Shares of £1		
50,000		each, fully paid	50,000	
35,000		35,000 Ordinary Shares of £1 each, fully paid	35,000	
				<u>85,000</u>
85,000		<i>Revenue Reserves :</i>		
		General Reserve	5,000	
5,000		Reserve for future Income Tax based on profits		
5,000		for year to date	4,000	
7,000		Profit and Loss Account, Balance unappropriated	10,000	
				<u>19,000</u>
				<u>104,000</u>
£102,000				
		<i>Long-term Liabilities :</i>		
		First Mortgage Debentures at 4½%	5,000	
5,000		Second Mortgage Debentures at 5½% (secured		
		by specific and floating charges over the		
		Company's assets)	5,000	
				<u>10,000</u>
£10,000				
		<i>Current Liabilities and Provisions :</i>		
		Creditors and accrued expenses	6,320	
10,776		Bills Payable	1,925	
3,420		Current Taxation	3,000	
3,000		Members for :		
		Preference dividend, less tax, for year to date	1,605	
1,605		Proposed Ordinary dividend of 5%, free of		
		tax, for year to date	1,750	
1,750		Unclaimed dividends	50	
50				<u>14,650</u>
				<u>£128,650</u>
£20,601				
£132,601				

and those assets which in the normal running of the business will be turned into cash) and current liabilities. Liquid assets may also be described as those in the *cycle* of production commencing with cash for the purchase of materials turned into finished goods and sold, creating book debts which ultimately become cash again.

The method of grouping the assets and liabilities shown in

31st MARCH, 19—

19—
(Previous year)

£		£	£
	<i>Fixed Assets :</i>		
10,000	Goodwill, at cost	10,000	
31,000	Freehold Land and Buildings, at cost	34,000	
35,000	Plant and Machinery, at cost (£40,000), less provision for depreciation to date (£8,000)	32,000	
13,550	Furniture and Fittings, at cost (£15,000), less provision for depreciation to date (£1,900)	13,100	
5,000	Motor Vehicles, at cost (£7,100), less provision for depreciation to date (£3,070)	4,030	
<u>£97,550</u>			<u>93,130</u>
	<i>Current Assets :</i>		
16,680	Stock-in-Trade and Work-in-Progress, as certified by the Managing Director	18,350	
9,531	Debtors (£9,255), less provision for doubtful debts (£410)	8,845	
2,366	Investments in Government Securities, at cost (market value at date £2,500)	2,366	
6,474	Cash at Bank and in Hand	5,950	
<u>£35,051</u>			<u>35,520</u>
 <u>£132,601</u>			 <u>£128,650</u>

the example clearly indicates that the working capital of the company is £20,870, arrived at as follows :

	£
Current assets	35,520
Less current liabilities and provisions	14,650
	<u>£20,870</u>

All liabilities payable immediately or in the near future must be taken into account in the calculation; for example, any redeemable preference shares which it is proposed to repay during the current year out of profits should be deducted.

Should the current assets be less than the current liabilities, a deficiency of working capital is indicated and this may have serious, even disastrous, results on the business. At the best it means that the directors will have difficulty in finding the funds to pay the creditors, and may lose cash discounts. At the worst it may mean, unless additional capital can be introduced or temporary assistance by way of a bank loan obtained, that the company will have to be wound up owing to its inability to meet liabilities as and when they arise, although it may, ultimately, pay 20s. in the £ when all its assets are realised.

A well-founded and efficiently managed company should always maintain a supply of working capital sufficient both to enable it to meet its current liabilities and to provide a surplus to take advantage of any exceptional opportunities for stock purchases or to meet adverse times.

READING THE ACCOUNTS

The adequate supply of liquid working capital is one of the first features to regard when considering a set of accounts presented for criticism. Another important matter is the rate of turnover, i.e., the number of times the average stock is absorbed in sales during the year. A comparatively low or declining rate of turnover may indicate that a larger stock is being maintained than is necessary for the needs of the business or that the stock is obsolete.

Variations in the rate of the Gross Profit year by year may indicate inaccuracy in stock-taking, while a declining rate needs careful investigation since it may be due to inefficiency in the buying or manufacturing departments or a mistaken sales policy. A tabulated percentage statement for a series of years will indicate the trend of expenses, and large increases in the percentages under the various headings should be carefully observed as this is often an indication of inefficiency in management.

Another useful test to apply to the accounts of a business selling on credit is the ratio of the debtors to sales, especially where monthly figures are available. If debts outstanding tend to increase out of proportion to sales, this may be due to slackness in sending out statements and following up collec-

tions. Similarly, if the proportion of outstanding creditors to total credit purchases is increasing, especially if discounts received are declining, over-buying may be suspected or the need for increased working capital brought to the attention of the management.

CONSIDERATIONS ON PURCHASE OF A BUSINESS

Where accounts are being examined in connection with a possible purchase of a business, or of shares in a company, the considerations mentioned in connection with the reading of accounts must, of course, be borne in mind. The accounts for a number of years will normally be available for the use of the proposed purchaser, and it is advisable to tabulate items both in figures and in percentages, for, say, the last five years, eliminating from the Profit and Loss Accounts any abnormal or non-recurrent items so as to arrive at the normal business Net Profit.

The purchase price of Goodwill is usually based on the average Net Profits, after making deductions for a reasonable rate of interest on the capital employed and for management services rendered by the proprietors where their salaries have not been charged in the accounts. Having ascertained the average normal Net Profits less the deductions mentioned above, the Goodwill may be valued at one to, say, three times the annual profits. No attempt will be made in this book to put forward suggestions as to the number of years' purchase, as this question can only be decided after a careful investigation of the facts of each particular case and having regard to general trading conditions at the time. A feature of particular importance, however, is the *trend* of the profits, a steady upward movement being an indication of an increasing Goodwill value.

The valuation of stock will need special attention ; a large increase in the gross profit percentage in the last year may indicate over-valuation of the final stock.

The adequacy of the provision for depreciation on the various assets will need to be considered in assessing the profits earned in the past, and the accounts produced may require adjusting if insufficient allowance has been made. On a sale it is usual for the assets to be examined and valued by an outside expert ; his report will be a valuable guide in arriving at a reasonable charge for depreciation and also in estimating what capital will be needed in future years for renewal and replacement of existing equipment.

Where capital is being introduced to enable loans to be paid off and to provide additional working capital, adjustments must be made, in estimating profits earned, for loan interest which will be avoided in future, and also for additional cash discounts where these are likely to be available.

On the other hand, a reasonable rate of interest will be expected on any new capital introduced.

An important matter arising outside the accounts is the question of securing continuity of management, where this is desired, by retaining the services of some of the existing directors, or continuing service agreements with employees.

The value of the business, and of a proportionate share therein, will be based on the worth of fixed assets (as valued), current assets, less liabilities to be taken over, and plus a reasonable sum for Goodwill based on past earnings as adjusted.

Apart from the points already mentioned, many other questions arise when the purchase of a business is being considered. The following are among the matters which require careful attention.

Reasons for Sale. Sometimes financial and other troubles necessitate a business being sold, in which case it is important to consider if this reason has caused any irreparable damage to the standing and reputation of the business.

Personality of Vendor. The personality of the vendor, or the directors of a vendor company, may be a dominant factor in the past success of the business, and the question arises whether a change of ownership will be detrimental to future trading. A reasonable chance of future success may be assured if the vendor or present directors will continue their services until the new proprietorship is firmly established.

Location of Premises. Localities often change in character, so that a good locality may become a bad one from the point of view of a retail business. In a new locality, the possibility of reasonably rapid development should be examined. A retail business relying on passing customers must be well situated; on the other hand, a wholesale or manufacturing business may not require premises in a shopping area, but would necessarily require them to be conveniently situated for road and rail transport facilities.

Contracts. Any existing or new contracts which will be carried out by the new proprietorship should be carefully considered as to conditions, prices, etc.

Trade Marks, Patents, and Copyrights. These should be investigated by Patent Agents, and an opinion as to value obtained.

Future Finance. The conditions of a particular trade or business may indicate that considerable future financial commitments may be necessary so that the business may succeed, and it would obviously be unwise to proceed with the purchase unless adequate finance can be provided for future requirements. Interest charges on present and future capital should be taken into consideration in estimating future profits.

The foregoing matters do not purport to be exhaustive, but merely to indicate the importance of a comprehensive review of all factors arising on the purchase of a business or a share therein, and apply wholly or partly whether the business is that of a sole proprietor, partnership, or a private limited company.

Chapter XV

DEPARTMENTAL ACCOUNTS

WHERE a business deals in different classes of commodities, conveniently divided into separate groups, it is frequently desired that the Trading and Profit and Loss Accounts shall be arranged in such a way as to permit the results in the different sections or departments to be separately ascertained. This arrangement has many advantages : it enables the efficiency of departmental managers to be judged ; by having regard to the departmental ratios of gross profit, the management is able to trace serious leakages ; it indicates the directions in which expansion is to be recommended ; and if and when the business of a department is being sold, the system enables the price to be fairly fixed.

The extent to which departmentalisation is to be carried varies considerably in practice. In some cases only the Manufacturing or Trading Account is analysed in this manner ; in other concerns the Profit and Loss charges are spread over the departments and an arbitrary basis of allocation sometimes found and applied to charges such as Directors' Fees, Debenture Interest, and the like, so that the final Net Profit balance is traced to the departments earning it.

DEPARTMENTAL SUBSIDIARY BOOKS

The rulings of the various subsidiary books have already been considered, and, for the purpose of preparing a departmental Trading Account, all that is necessary is to provide columns in the Purchases, Sales, Returns Inwards and Outwards Day Books to divide the entries between the departments. The posting of these departmental Day Books follows the usual principles as explained in Chapter III. The Purchases and Sales Accounts in the Nominal Ledger are ruled with departmental columns to which are posted the periodical (usually monthly) totals from the relative columns of the Day Books.

Simple illustrations of Purchases and Sales Day Books are

given on pages 150 to 153 with the items divided between Drugs, Medical Requisites, and Chemists' Sundries departments. The departmental Purchases and Sales Accounts in the Nominal Ledger are also shown. Owing to limit of space, one item only is entered in each department, but this should be sufficient to illustrate the principle of departmental division.

Departmental Returns Outwards (Purchases Returns) and departmental Returns Inwards (Sales Returns) Day Books are not illustrated, as the rulings are identical with those of the departmental Purchases and Sales Day Books.

The nature of the business and the method of management may call for separate Day Books for each department instead of a single or group of analysed Day Books, especially where there are several departments, or where the volume of entries in each department is large. With separate books the work may be allotted to a number of clerks and carried out expeditiously. The "Copy Invoice" type of Day Book illustrated in Chapter III may be found convenient where separate books are required.

In large businesses where the cost of installing accounting machines may be justified, the departmental division of the Day Books can be carried out by direct analysis on the machines, and makers of these machines will gladly demonstrate the methods to readers who are interested.

DEPARTMENTAL CASH BOOKS

As in the case of the Day Books, the proper recording of cash received and paid in departmental books is effected by means of suitably ruled books.

Cash Received. The ruling of the Cash Received Book must be arranged so as to provide departmental analysis columns for Cash Sales and Discounts allowed. Where the sales of the business are effected for cash, and not on credit, a single Cash Received Book, as illustrated in Chapter II, may be used to record the receipts of a limited number of departments. The book is written up from the departmental records on the lines suggested in that chapter.

In cases where the sales are also effected on credit, it is not normally possible to divide the cash sales by means of analysis columns between more than, say, two departments in the one Cash Received Book owing to limit of horizontal space. When the departments exceed this number the division between the departments is made by means of a Cash Sales Summary which

DEPARTMENTAL PURCHASES

Date	Inv. No.	Name	L/F	Details		
19—				£	s.	d.
Jan. 2	1	M. Brown, Ltd. . . .		35	4	5
" 4	2	" " " . . .		41	7	8
" 16	3	" " " . . .		34	7	6
" 3	4	J. Oslo & Co. . . .	10	11	8	7
" 15	5	" " " . . .		54	3	2
" 31	6	" " " . . .		28	8	6
" 31	7	" " " " . . .		33	4	1
" 10	8	O. Richards . . .	14	18	4	8
" 20	9	" " . . .	31	3	17	5

PURCHASES ACCOUNT (IN

Dr.

		Fol.	Total	Drugs	Medical	Chemists' Sundries
			£ s. d.	£ s. d.	£ s. d.	£ s. d.
19— Jan. 31	To Sundries as per Purchases Book .	53	260 6 0	110 19 7	127 4 4	22 2 1
" 31	" Departmental Transfers . .	21	30 0 0		22 0 0	8 0 0

Monthly Totals follow

	£3,551 7 6	£1,831 15 0	£1,180 3 8	£539 8 10
--	------------	-------------	------------	-----------

is prepared daily from the departmental cash sales records. The total cash sales of all departments is agreed with the total cash taken by the cashier and entered in the Cash Sales column of the Cash Received Book, each day.

For the purpose of posting the cash sales to the departmental Sales Account in the Nominal Ledger at the posting date (usually at the end of each month), a schedule of

DAY BOOK

Départments

Total			Drugs			Medical Requisites			Chemists' Sundries		
£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.
110	19	7	110	19	7						
127	4	4				127	4	4			
22	2	1							22	2	1
£280	6	0	£110	19	7	£127	4	4	£22	2	1

N.L.20

NOMINAL LEDGER)

Cr.

		Fol.	Total			Drugs			Medical			Chemists' Sundries		
			£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.
19—														
Jan. 31	By Sundries as per Returns Outwards Book	23	10	2	2	3	1	6	1	8	7	5	12	1
„ 31	„ Departmental Transfers	21	30	0	0	22	0	0	8	0	0			

Monthly Totals follow

Dec. 31	„ Trading A/c	N.L. 173	3,422	10	8	1,732	18	6	1,164	8	7	525	3	7
			£3,551	7	6	£1,831	15	0	£1,180	3	8	£539	8	10

the Daily Cash Sales Summaries must be prepared and the total of this schedule agreed with the total of the Cash Sales column in the Cash Received Book for the period.

As already mentioned, the discounts allowed to customers will require to be analysed between the various departments, and this may be done by means of analysis columns in the Cash Received Book where there are a limited number of

DEPARTMENTAL

Date	Name	Particulars	L/F
19— Jan. 2	J. East	3 Stethoscopes @ 12s. 6d. each Less 10% Trade Discount .	
		28 lb. of Compound Liquorice Powder @ 8d. per lb. . . .	
„ „	C. North	14 lb. of Cotton Wool @ 1s. 2d. per lb. 5 gallons of Liquid Paraffin @ 6s. 9d. per gallon 10 gallons of Distilled Water @ 6d. per gallon Less 5% Trade Discount .	29
„ „	R. South	5 lb. of Tincture of Opium @ 4s. 3d. per lb. 2½ doz. tubes of Tooth-paste @ 5s. per doz.	61

Daily

Dr.

SALES ACCOUNT (IN

Date		Fol.	Total	Drugs	Medical Requisites	Chemists' Sundries
			£ s. d.	£ s. d.	£ s. d.	£ s. d.
19— Jan. 31	To Sundries as per Returns Inwards					
	Book	8	25 2 6	10 2 6	9 10 0	5 10 0
Feb. 28	„ do. do. .	12	18 10 1	11 8 4	3 10 0	3 11 9

Monthly Totals follow

Dec. 31	„ Trading A/c. .		4,660 11 9	2,521 3 2	1,891 9 6	247 19 1
			£4,900 17 6	2,650 6 0	£1,940 3 2	£310 8 4

SALES BOOK

Departments

Details	Total	Drugs	Medical Requisites	Chemists' Sundries
£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.
1 17 6 3 9				
1 13 9			1 13 9	
18 8		18 8		
	2 12 5			
16 4			15 6	
1 13 9		1 12 1		
5 0				4 9
2 15 1 2 9				
	2 12 4			
1 1 3		1 1 3		
12 6				12 6
	1 13 9			

entries follow

£376 14 8	£187 5 6	£163 10 7	£25 18 7
-----------	----------	-----------	----------

N.L.51

NOMINAL LEDGER)

Cr.

Date		Fol.	Total	Drugs	Medical Requisites	Chemists' Sundries
			£ s. d.	£ s. d.	£ s. d.	£ s. d.
19—						
Jan. 31	By Sundries as per					
	Sales Book .	60	376 14 8	187 5 6	163 10 7	25 18 7
Feb. 28	„ do. do. .	90	408 3 4	210 3 1	174 1 6	23 18 9

Monthly Totals follow

£4,900 17 6	£2,650 6 0	£1,940 3 2	£310 8 4
-------------	------------	------------	----------

departments. Here again, in businesses where there are more than, say, two departments, a separate analysed summary of the discounts should be prepared each day and a schedule of these daily summaries made at the end of the month for posting to the Discounts Allowed Account in the Nominal Ledger.

It will be appreciated that where there are many hundreds of entries to be divided between a large number of departments, a considerable amount of work will be involved in segregating the discounts allowed to customers. For this reason the discounts may be entered in one column only and divided between the departments at the end of the month on the basis of the sales by each department. Care should be exercised, however, in instances where the rate of discount varies between the departments, and an adjustment should be made in the division accordingly.

Cheque Payments. The cheque payments which require to be divided departmentally are those items which are posted to the Nominal Ledger. It is not practicable so to divide all the expenses of a business at the time the entries are made in the Cash Payments Book. Apportionments are made as between the departments at the end of the financial year from the details shown in the Nominal Ledger Accounts on recognised bases, as explained later in this chapter.

It is obvious from a study of the various rulings of a Cash Payments Book shown in Chapters II and V that the amount of horizontal space in the usual size account book is not sufficient to permit separate departmental columns for each class of item (usually expenses) posted to the Nominal Ledger, especially where there is more than one Bought Ledger column. It is therefore necessary for the departmental division of those items which are capable of direct apportionment to be made by means of separate analyses for posting to the Nominal Ledger.

Discounts received will require to be divided between the departments, and it is recommended that this should also be done by means of a separate analysis where space is not available in the Cash Payments Book for separate columns. On the other hand the discounts may be entered in one column and divided between the departments at the end of the month or accounting period. The suggested basis of division is according to the purchases of each department.

Petty Cash. It is obviously impracticable to rule the Petty Cash Book departmentally, as the number of expenses

columns required is already sufficient to cover the usual size book. Separate Petty Cash records will, therefore, be required for each department where petty cash is disbursed.

DEPARTMENTAL TRANSFERS

In a departmental business, especially where raw materials are used, stock is often taken from one department for use in another. The number and value of these transfers will determine the book-keeping method of recording the transactions. Where the items are numerous, a special Departmental Transfer Journal is recommended. The ruling of this book is shown on pages 156 and 157, and its object is to summarise particulars of goods transferred from one department to another. At the end of the month the totals are ascertained and the Purchases Account of the original buying department is credited with the value of the goods transferred and the Purchases Account of the department to which the goods have been transferred is debited.

The department issuing the stock will prepare a Stock Issue Note and the department receiving the stock will prepare a Stock Receiving Note, both Notes being sent to the Counting House where the reciprocal Notes are agreed and the Departmental Stock Transfer Journal written up accordingly.

When the departmental transfers are few in number and value, the records can be passed through the Journal Proper, as and when the transfers are made.

These departmental transfers of stock should be made preferably at cost prices to the original buying department. This will present little difficulty where the stock is transferred in its original state, but where the goods have been manufactured by a particular department, careful consideration must be given as to what constitutes "cost." In such cases it is submitted that cost represents the cost of the raw materials, plus manufacturing labour and an equitable proportion of the factory expenses. The nature of some businesses requires the addition of an amount estimated to cover the cost of handling the stock in its original buying department. No objection can be raised to this addition where definite expense has been incurred in handling and storing the stock, but care must be taken to see that the amount of this "loading" is eliminated from the value of the stock in hand which is brought into the final accounts at the end of the year.

Dr.

Date	Particulars	Drugs	Medical Requisites	Chemists' Sundries

The monthly totals on the debit side are posted to the debit totals on the credit side are posted to the credit of the

The attention of readers is directed to the specimen Trading and Profit and Loss Accounts on pages 158 and 159. The value of the information to be derived from preparing accounts in departmental form is widely appreciated in practice. Once the subsidiary books have been suitably arranged on the lines already indicated and the method of dividing the various expenses between the departments is understood, the preparation of the final departmental accounts presents little difficulty.

Owing to restriction of space, the comparative figures of the previous year have not been shown in the example on pages 158 and 159. These figures would be shown in practice in order to facilitate comparison and to comply with the Companies Act, 1948, if the accounts are to be laid before the company in general meeting in this form.

156

STOCK TRANSFERS

Cr.

Date	Particulars	Drugs	Medical Requisites	Chemists Sundries

as shown on the Stock Transfer Notes, are entered in the made on the credit side in the columns of the departments

of the departmental Purchases Account and the monthly departmental Purchases Account in the respective columns.

Account represent direct allocations obtained from the relative accounts in the Nominal Ledger which have been compiled from suitably ruled subsidiary books.

Some of the charges in the Profit and Loss Account may also be apportioned by direct allocation. For example, the salaries of the individual members of the clerical staff may be directly allocated and a summary prepared in the Salaries Book for posting to a departmentally ruled Salaries Account in the Nominal Ledger. Other charges may be more complex and the debits in the respective Nominal Accounts cannot be departmentally divided at the time the postings are made. In such cases the amount standing to the debit of the expense account in the Nominal Ledger is apportioned between the departments at the end of the financial year as indicated in the following notes, for which purpose the items have been conveniently divided into groups.

Group A. In the first group are those expenses relating to the building maintenance, which may be apportioned over the

departments by reference to the floor space occupied. In this section are included Rent, Rates, Mortgage Interest, Building Repairs, Depreciation of Fixtures and Fittings, and the like; in making the apportionment some allowance may be made for the fact that one department is on the ground floor and another department on, say, the second floor: this

*A. B. & COMPANY, LIMITED.**TRADING AND PROFIT AND LOSS ACCOUNTS*

Group (D.A. = Direct Allocation)		Total	Drugs	Medical Requi- sites	Chemists' Sundries
		£	£	£	£
	To Stock-in-Trade—April 1st, 19—	2,934	1,483	850	601
D.A.	„ Purchases, <i>less</i> returns	9,033	4,272	2,878	1,883
D.A.	„ Carriage Inwards	51	27	14	10
D.A.	„ Factory Wages and National Insurance	1,105	665	268	172
D.A.	„ Factory Fuel	135	72	29	34
	„ Gross Profit carried down	2,071	1,116	562	393
		<u>£15,329</u>	<u>£7,635</u>	<u>£4,601</u>	<u>£3,093</u>
A.	To Rates	73	37	18	18
A.	„ Repairs to Buildings	26	13	7	6
D.A.	„ Heating and Lighting	34	17	8	9
C.	„ Insurance	21	12	5	4
B.	„ Travellers' Commission and Expenses	231	105	80	46
B.	„ Advertising	46	21	16	9
B.	„ Carriage Outwards	44	20	15	9
B.	„ Motor Delivery Expenses	122	57	41	24
B.	„ Office Salaries and National Insurance	462	251	115	96
B.	„ Printing, Stationery, Postage, and Tele- phone	119	54	41	24
D.	„ Sundry Trade Expenses	21	10	6	5
B.	„ Discounts allowed	73	33	26	14
A.	„ Mortgage Interest	90	45	23	22
D.	„ Audit and Professional Fees	40	20	10	10
D.A.	„ Bad Debts	28	—	19	9
	„ Depreciation:				
A.	„ Furniture, Fixtures, etc., @ 5%	21	10	6	5
B.	„ Motor Van @ 20%	32	15	11	6
D.A.	„ Interest on Assets employed	300	160	80	60
	„ Balance carried down	425	297	83	45
		<u>£2,208</u>	<u>£1,177</u>	<u>£610</u>	<u>£421</u>
	To Directors' Fees				105
	„ Debenture Interest				150
	„ Net Profit carried down				620
					<u>£875</u>

may be allowed for by reckoning each square foot on the ground floor as equal to, say, two on the second floor. Lighting and Heating may also be apportioned on this basis, but a more accurate method is in proportion to the lamps or points provided. Where separate meters are installed in each department definite figures can be obtained.

FOR THE YEAR ENDED MARCH 31st, 19—

Group (D.A. = Direct Allocation)		Total	Drugs	Medical Requi- sites	Chemists' Sundries
D.A.	By Sales, <i>less</i> returns	£12,446	£6,106	£3,846	£2,494
	„ Stock-in-Trade—March 31st, 19—	2,883	1,529	755	599
		£15,329	£7,635	£4,601	£3,093
D.A.	By Gross Profit brought down	2,071	1,116	562	393
	„ Discounts Received	137	61	48	28
		£2,208	£1,177	£610	£421
	By Balance brought down				425
	„ Interest charged to departments				300
	„ Dividends (<i>less</i> tax) on Investments				138
	„ Transfer Fees				12
					£875
	By Net Profit brought down				£620

Group B. In this group are expenses which are equitably allocated in proportion to sales value, including such items as travellers' commission and expenses, carriage outwards, delivery expenses including depreciation on delivery vehicles, advertising, and discounts allowed. Where the ratio of gross profit to sales varies considerably in the departments the allocation should be made on the Gross Profit earned in preference to sales. Office and administration charges are usually apportioned on the basis of the sales.

Group C. Fire and other Insurances on goods, Stores Expenses, and the like may be apportioned over the departments on the basis of average stocks held.

Group D. In addition to the expenses in the groups already considered, there are items of a miscellaneous nature. For these it is necessary to adopt a basis having relation to the nature of the expenses, in some cases a purely arbitrary or "quota" allocation being accepted.

The question of interest may arise where the assets employed are of considerable value. Each department may be charged with interest on the average assets employed in the department, including a proportion of the stock, buildings, plant, and machinery, or other capital assets. If this is done, it can at once be seen to what extent the departments are producing more or less a normal return on the capital invested. The total interest charged is brought down to the credit side in the final section of the Profit and Loss Account as shown in the example.

In addition to the allocated charges there are likely to be certain expenses which may not be capable of division between the departments, such as debenture interest and directors' fees. Where a fair basis of allocation cannot be applied, these charges should be grouped in the final section of the Profit and Loss Account, as shown.

Income, other than from sales, needs careful consideration and should, if possible, be credited to the departments responsible for the transaction. For instance, discounts received will be allocated to the departments according to the actual amounts allowed on their respective purchases, or by direct allocation according to the purchases of each department.

Amounts received which cannot be divided should be credited to the final section of the Profit and Loss Account. Apart from the credit for departmental interest which has already been explained, the example shows Dividends from Investments and Transfer Fees, which are items that cannot be apportioned between the departments.

Chapter XVI

BRANCH ACCOUNTS

FROM an accounting point of view a branch may be regarded as a department situated at a distance. Many of the considerations which were discussed in connection with departmental accounts have equal application to branches, especially as to the apportionment of administrative expenses and the separate ascertainment of the financial result of the transactions of each branch.

Whereas the departments of a business are usually in the same building so that control and supervision may be continuously exercised, branches are normally situated at a considerable distance from each other and from Head Office; the degree of independence accorded to branch managers is increased correspondingly. In some instances a branch is allowed full independence, the manager being responsible for the purchases and sales and cash received and paid, in which case a full set of books is kept by the branch. At stated periods financial returns are sent to Head Office for incorporation in the Head Office books on lines indicated later in this chapter.

At the other extreme of branch accounting policy is the branch which is subject to the maximum Head Office control. Each branch is supplied by Head Office with goods for sale at fixed prices, cash received being banked each day by the branch manager for the credit of Head Office account. Payments are made from Head Office, except incidental expenses which are met from a petty cash imprest supplied and maintained by Head Office. The function of such a branch is therefore one of a selling agency.

Between these two extreme types of branch management there are many other methods of control varying according to the nature of the business and the number of branches. For the purposes of this chapter the two extreme types of branches will be discussed, as the principles adumbrated will be of general application and subject only to variation in matters of detail.

MAXIMUM HEAD OFFICE CONTROL

Where the branch simply acts as a selling agency the goods are usually supplied by Head Office for sale at fixed prices, the cost price being known only at Head Office. On any given date the Head Office is able to ascertain from its books the value of the goods at selling price which have been sent to the branch and not yet sold. Stock is taken by the branch managers weekly or monthly and a return is made to Head Office for the purpose of agreement with its records. Unexpected visits to the branches are made by Head Office inspectors, who take stock and count the cash in hand, the sum total of which must correspond with the amount standing to the debit of the branch in the Head Office books.

This system of branch accounting, supported by the supervision of the inspectors, works well in practice and affords a reliable check on the honesty and efficiency of branch managers. The method is especially suitable in cases where there is a number of branches each dealing in goods of a certain nature, the prices of which—if not liable to fluctuation—may be fixed in advance.

BRANCH RECORDS. The records to be kept at the branch are very simple and usually comprise the following :

Goods Requisition Book. This book is used when ordering goods from Head Office and is arranged so that three copies may be taken by means of carbon paper. Two copies are sent to Head Office and the third kept in the book by the branch manager. Head Office retains one copy for the purposes of writing up its own records, and the other copy is sent back to the branch as an invoice for the goods ordered.

Returns and Allowances Book. When goods are returned to Head Office for any reason, or an allowance is claimed in respect of damage or loss of weight, etc., particulars are entered in this book, which is similar in ruling and form to that of the Goods Requisition Book.

Sales Records. A record of the sales is usually sent by the branch manager to Head Office in the form of a weekly summary showing the daily bankings made to the credit of the Head Office bank account. A duplicate of the pay-in slip is sent each day to Head Office, or the slips for the week attached to the weekly return. If necessary, arrangements can be made with the bank to supply a three-fold pay-in book, the third slip being retained by the branch as a voucher for the amount remitted to Head Office.

Stock Records. As already mentioned, stock is taken by the branch managers weekly or monthly, and a stock return is made to Head Office: a practical example is shown on page 164.

Disbursements. The payments made by the branch managers are usually confined to wages and petty cash expenditure, all other payments being made by Head Office. The payments by the branch are effected from a standing cash float kept by the manager. A suitably ruled carbon-copy book is used for this purpose, the top copy together with supporting vouchers being sent each week to Head Office, which remits to the branch the amount spent, thus keeping the branch float at the imprest amount.

HEAD OFFICE RECORDS. A Branch Ledger will be required, containing a separate account for each branch, the relationship of the Head Office to the branch being regarded as that of a creditor and debtor. If readers will bear this relationship in mind, they will readily understand the principles of branch accounting. The postings to the Branch Ledger are made from the following books:

Branch Supplies Journal. This journal is written up on the day the goods are dispatched from the Goods Requisition Notes received from the branches. A suggested form of ruling is shown which may require variation according to the number of branches and the nature of the business. The periodical totals at cost and selling prices are debited to the account of each branch in the Branch Ledger and credited to the Goods Sent to Branch Account.

Branch Returns and Allowances Journal. Particulars of goods returned from, or allowances made to the branches for price reductions, etc., are entered in this journal from the details shown by the Returns and Allowances Notes. The ruling follows that of the Branch Supplies Journal, and the periodical totals are credited to the account of each branch in the Branch Ledger, and debited to the Goods Sent to Branch Account.

Branch Remittance Book. This book is suitably ruled to show the name of the branch and the amount remitted to Head Office, and is written up from the duplicate pay-in slips received from the branches each day. The total cash received from all branches daily is shown by the Branch Remittance Book and is entered in the main Cash Received Book. The periodical (weekly or monthly) totals of cash received are credited to the accounts of the branches in the Branch Ledger.

Branch Expenses Journal. The function of this journal is to

classify and record the branch expenses as shown on the wages and petty cash returns sent by each branch to Head Office at the end of the week. The weekly cash refund to each branch is shown in the main Cash Payments Book, but space in that book will not generally permit of a detailed analysis. For this reason a suitably ruled Expenses Journal is required, cross-referenced with the entries in the main Cash Book, and the expenses are posted from this journal to the debit of the relative expense accounts in the Nominal Ledger of the Head Office.

Branch Ledger Folio : 18

Branch : HONITON

STOCK RETURN FOR WEEK ENDED....., 19—

	Selling Prices	
Stock as per last return	£ 345	This space may be used for depart- mental analysis if necessary and possible.
Add Stock received during week :		
Requisition No. 31	85	
" " 32	86	
	516	
Less Returns and Allowances :		
Advice No. 74	12	
	504	
Less Sales for week as per Sales Summary herewith	193	
Stock on hand	311	
" " " (as taken)	310	
Deficiency	1	
Surplus		

Manager's signature.....

For Head Office use.

Cost of Stock on hand

£
206

Entered in Branch Ledger by.....Examined by.....

Branch Ledger. As already mentioned, the Branch Ledger contains an account for each branch. The entries on the debit side are in respect of the stock in hand at each balancing date (end of each week or month) and the goods sent to the particular branch during the period as shown by the Branch Supplies Journal. The goods sold are entered on the credit side as represented by the cash received from the branch, and as recorded in the Branch Remittance Book. The goods returned from, and the allowances made to the branch, in accordance with the details recorded in the Branch Returns and Allowances Journal, are also credited.

An illustration of an account in the Branch Ledger dealing with the Honiton branch is shown on page 166. The balance of the Selling column will represent the value of the stock in hand at selling prices and should agree in amount with the weekly or monthly stock record sent by the manager, thus effecting the necessary check on the stocks carried by the branch. Any variations in selling prices will require an adjustment of the figures in the Selling column in order to balance that column at the end of the period. In practice, small deficiencies are possible at stock-taking time, especially in the case of commodities sold by weight; such deficiencies are written off, after consideration by the management, in the form of a credit entry in the Selling column, as shown by the example on page 167. These adjustments will not affect the Cost columns, as variations in selling prices will be ultimately reflected in the figure of Gross Profit, and any deficiency or surplus is automatically taken into consideration in the stock valuation and again ultimately reflected in the figure of Gross Profit. The cost price of the goods sent to the branch and the cost price of the stock in hand having been extended to the Cost columns, the balance will show the gross profit earned by the branch during the period.

Goods Sent to Branches Account.—A Goods Sent to Branches Account is required recording cost prices only. The cost of goods supplied to the branches by Head Office as shown by the Branch Supplies Journal is credited, and the cost of goods returned or allowances made, as shown by the Branch Returns and Allowances Journal, is debited in convenient totals. The credit balance on the Goods Sent to Branches Account is transferred to the credit of Head Office Purchases Account at convenient dates. An example dealing with the Honiton, Barnstaple, and Bideford branches is shown on pages 166 and 167.

	Branch No.	Branch	Requisition No.
19—			
Jan. 1	1	Honiton.	31
" 2	2	Barnstaple	14
" 2	3	Bideford	82
Details follow covering a			

Note.—The Cost and Selling Column totals are Column totals only credited to the Goods Sent to

Dr.

HONITON BRANCH

		Fol.	Selling	Cost
19—			£	£
Jan. 1	To Stock b/f. .	✓	345	212
" 31	" Supplies .	21	171	114
" 31	" Gross Profit .	✓		81
			£516	£407
Feb. 1	To Stock c/d. .	✓	310	206

Dr.

GOODS SENT TO

		Fol.	£	£
19—				
Jan. 31	To Sundries as per Branch Re- turns and Allowances Journal :			
	Honiton .		10	
	Barnstaple .		6	
	Bideford .	12	11	
				27
" 31	" Transfer to Purchases A/c	NL 36		262
				289

SUPPLIES JOURNAL

Honiton		Barnstaple		Bideford	
Cost	Selling	Cost	Selling	Cost	Selling
£ 17	£ 25	£ 36	£ 44	£ 50	£ 75
114	171	80	125	95	140

period of a week or month.

debited to the individual Branch Accounts and the Cost Branches Account.

ACCOUNT

Cr.

		Fol.	Selling	Cost
19—			£	£
Jan. 31	By Cash Received.	14	193	193
" 31	" Returns . .	6	12	8
" 31	" Stock c/d. .	✓	310	206
" 31	" Deficiency .	✓	1	
			£516	£407

BRANCHES ACCOUNT

Cr.

		Fol.	£	£
19—				
Jan. 31	By Sundries as per Branch Sup- plies Journal:			
	Honiton . .		114	
	Barnstaple .		80	
	Bideford .	21	95	
				289
				289

Inter-branch Comparisons. The gross profit earned by each branch having been ascertained by reference to the Branch Accounts in the Branch Ledger, it is a comparatively easy matter to arrive at the net profit of a branch by taking into account the branch expenses as shown in the Branch Expenses Journal and adding a "loading" to cover Head Office expenses. In practice this information is shown on suitably ruled analysis sheets and submitted to the directors at regular intervals, thus providing useful inter-branch comparisons for relative efficiency.

Sales on Credit. In certain classes of businesses the branch, although under maximum Head Office control, may be permitted to effect sales on credit to approved customers and the accounting system already outlined will require additional records. It is assumed, as is usually the case, that the sales are invoiced and the amounts collected by Head Office. At the end of each day an advice will be sent by the branch to Head Office showing details of the goods sold and the name and address of the customer. The Branch Weekly Sales Return is suitably ruled to record, in addition to the cash sales, the sales effected on credit, and is agreed with the daily sales or credit advices received from the branch.

At the Head Office a Branch Sales Journal will be kept and written up from the advices received from the branch and the invoices sent to the customers. The account of the customer is debited and the Branch Account credited in periodical totals. When the customer pays his account the amount is entered in the main Cash Received Book at Head Office and the account of the customer credited in the usual way. Where the sales on credit by the branches are considerable, it is usually found convenient to keep a separate Sales Ledger to record the customers' accounts of each branch and to apply the self-balancing method to each ledger. In other cases a single Sales Ledger may be found sufficient for the purpose.

BRANCHES AS INDEPENDENT UNITS

In cases where the branches operate independently of Head Office, a complete set of books is kept at each branch on the usual book-keeping principles.

Readers will appreciate that the policy of independence accorded to the branches should only be applied where there is implicit trust in the integrity and book-keeping abilities of the branch managers and their staffs. Complete supervision and control by Head Office is not possible, but a system of

periodical examination of the branch books by Head Office Inspectors and the ascertaining of the trading results at more frequent intervals than once a year will usually enable leakages and inefficiency to be detected.

HEAD OFFICE RECORDS. The books at Head Office do not reflect the trading results of the branch until the necessary records are sent by the branch at the end of the accounting period. Throughout the year a certain number of mutual transactions usually occur such as the supply of goods by Head Office and remittances to or by Head Office. These mutual transactions between the branches and Head Office are recorded in the same way as similar transactions with outside parties, the relationship being simply that of debtor and creditor.

In the Head Office books a Branch Ledger Account will be kept for each branch. Goods and property sent to the branch are debited; goods returned to, and cash received by Head Office are credited. The goods supplied to the Branches by Head Office are credited to a Goods Sent to Branches Account, and returns and allowances debited to complete the double-entry. The credit balance on Goods Sent to Branches Account is transferred to the credit of Purchases Account as in the case of the Maximum Head Office Control system already considered.

Where the number of transactions is considerable, accounts subsidiary to the Branch Ledger Account should be kept for each Branch. For instance, the goods sent to the branch may be debited to a Branch Supplies Account, returns and allowances credited to the same account, and the balance transferred to the debit of the Branch Account at the end of convenient periods. In the same way remittances received from the branch may be credited, and remittances sent to the branch debited to a Branch Remittances Account, and the balance transferred to the Branch Account. These accounts are simply subordinate to the Branch Account and may be dispensed with where the volume of transactions is small.

BRANCH RECORDS. In addition to the usual Ledger Accounts, the Nominal Ledger at the branch will contain a Head Office Account and, if necessary, a Head Office Supplies and Remittances Account, all of which will record reciprocal entries to those in the Head Office books. For example, the Head Office Account is credited with goods, property, and remittances received from Head Office, and debited with goods

TRURO BRANCH

(In the Head Office)

			£	s.	d.	£	s.	d.
19—								
April	1	To Balance at Branch b/f:						
		Cash	400	0	0			
		Book Debts	2,010	0	0			
		Stock	1,483	0	0			
		Fixtures and Fittings	200	0	0			
		Motor Van	75	0	0			
			✓			4,108	0	0
	1	„ Transfer from Suspense A/c—Cash in transit re-transferred	J/12			80	0	0
March	31	„ Goods supplied branch to date	78			1,200	0	0
	31	„ Remittances sent to branch to date	51			160	0	0
						5,608	0	0
	31	„ Branch Trading A/c:						
		Sales for year	J/31			6,106	0	0
		Closing Stock	„			1,529	0	0
						7,635	0	0
	31	„ Branch Profit and Loss A/c:						
		Discounts received	J/32			61	0	0
	31	„ Balance, Creditors at Branch, c/d:	✓			790	0	0
						£14,094	0	0
April	1	To Balance at branch b/d:						
		Cash	551	0	0			
		Book Debts	2,100	0	0			
		Stock	1,529	0	0			
		Fixtures and Fittings	190	0	0			
		Motor Van	60	0	0			
			✓			4,430	0	0
	1	„ Transfer from Suspense A/c—Cash in transit re-transferred	J/40			60	0	0

HEAD OFFICE

(In Truro)

			£	s.	d.	£	s.	d.
19—								
March	31	To Balance, Creditors, b/f:	✓			850	0	0
	31	„ Remittances to Head Office to date	43			1,300	0	0
	31	„ Goods returned to Head Office to date	10			35	0	0
						2,185	0	0
	31	„ Balance c/d.:						
		Cash	551	0	0			
		Book Debts	2,100	0	0			
		Stock	1,529	0	0			
		Fixtures and Fittings	190	0	0			
		Motor Van	60	0	0			
			✓			4,430	0	0
						£6,615	0	0
April	1	To Balance, Creditors, b/d:	✓			790	0	0

ACCOUNT

Ledger at Exeter)

19—				£	s.	d.	£	s.	d.
March	31	By Balance, Creditors at Branch, b/f:	✓				850	0	0
"	31	" Remittances received from branch to date .	97	1,320	0	0			
"	31	" Transfer to Suspense A/c—Cash in transit .	J/20	60	0	0			
							1,380	0	0
"	31	" Goods returned by branch to date . . .	71				35	0	0
							2,265	0	0
"	31	" Branch Trading A/c:							
		Opening Stock	J/31	1,483	0	0			
		Purchases for year	"	4,272	0	0			
		Other Trading A/c items	"	764	0	0			
							6,519	0	0
"	31	" Branch Profit and Loss A/c:							
		Expenses paid by branch	J/32	695	0	0			
		Depreciation—							
		Furniture and Fittings	"	10	0	0			
		Motor Van	"	15	0	0			
		Interest on assets at branch	"	160	0	0			
							880	0	0
"	31	" Balance at branch c/d:							
		Cash		551	0	0			
		Book Debts		2,100	0	0			
		Stock		1,529	0	0			
		Fixtures and Fittings		190	0	0			
		Motor Van		60	0	0			
			✓				4,430	0	0
							£14,094	0	0
April	1	By Balance, Creditors at Branch, b/d:	✓				790	0	0

ACCOUNT

Branch Books)

19—				£	s.	d.	£	s.	d.
April	1	By Balance b/f.:							
		Cash		400	0	0			
		Book Debts		2,010	0	0			
		Stock		1,483	0	0			
		Fixtures and Fittings		200	0	0			
		Motor Van		75	0	0			
			✓				4,168	0	0
March	31	" Goods supplied by Head Office to date .	93				1,200	0	0
"	31	" Remittances from Head Office to date .	61				160	0	0
							5,528	0	0
"	31	" Profit and Loss A/c—Net Profit for year .	J/11				297	0	0
"	31	" Balance, Creditors, c/d:	✓				790	0	0
							£6,615	0	0
April	1	By Balance b/d.:							
		Cash		551	0	0			
		Book Debts		2,100	0	0			
		Stock		1,529	0	0			
		Fixtures and Fittings		190	0	0			
		Motor Van	✓	60	0	0			
							4,430	0	0

returned and remittances sent to Head Office. The credit balance of the Head Office Account in the branch books will therefore be equal in amount to the debit balance of the Branch Account in the Head Office books. At the end of the year, or other agreed period, the branch extracts from its books a Trial Balance, and prepares a Branch Trading and Profit and Loss Account and a Balance Sheet. These documents are sent to Head Office for incorporation of the trading results of the branch in the Head Office books, so that the latter may contain complete information regarding the transactions of the business as a whole.

The profit earned or the loss incurred by the branch is transferred to the Head Office Account in the branch books and the balance on this account shown on the liabilities side of the Branch Balance Sheet in lieu of the usual Capital Account. The balance on this account is, in effect, the capital invested in the branch to the extent that it has been disclosed by Head Office, and represents the excess of assets over liabilities at that particular branch.

C. D. & CO., LTD.

BALANCE SHEET

19 -- (Previous year)		Head Office (Exeter)	Branches		Total
			Truro	Helston	
£		£	£	£	£
	<i>Share Capital :</i>				
	Authorised :—				
	5,000 6% Cumulative Preference Shares of £1 each	5,000			
	5,000 Ordinary Shares of £1 each	5,000			
<u>£10,000</u>		<u>£10,000</u>			
	<i>Issued :—</i>				
	4,600 6% Cumulative Preference Shares of £1 each, fully paid . .	4,600	—	—	—
8,600	4,000 Ordinary Shares of £1 each, fully paid	4,000	—	—	8,600
	<i>Revenue Reserves :</i>				
1,500	Profit and Loss Account, Balance unappropriated	1,434	297	83	1,814
<u>10,100</u>		<u>10,034</u>	<u>297</u>	<u>83</u>	<u>10,414</u>
	<i>Long-term Liabilities :</i>				
1,400	Mortgages at 5% (Secured on Freehold Premises, per contra)	—	900	500	1,400
	<i>Current Liabilities and Provisions :</i>				
2,075	Creditors and accrued expenses . .	969	790	430	2,189
	Head Office Accounts (as per contra)	—	5,003	1,419	—
<u>£13,575</u>		<u>£11,003</u>	<u>£ 6,990</u>	<u>£2,432</u>	<u>£14,003</u>

Items in Transit. Although in theory the balances on the reciprocal Head Office and Branch accounts should agree, in practice it is found that there are invariably transactions during the last few days of the accounting period which have been passed through the branch books but not through the Head Office books, and vice versa, for example, cash sent by the branch on March 31st, but not received by Head Office until April 1st. Again, goods sent and charged by Head Office on March 31st may not be received by the branch until April 1st.

These items should be transferred to a "Suspense" or "Items in Transit" Account so that the reciprocal balances of the Head Office and the Branch Accounts may agree. At the beginning of a new period the items on the Suspense Account are re-transferred to the Branch Account in the Head Office Ledger.

When preparing the final accounts the items on the Suspense Account must be included in the Balance Sheet under appropriate headings; thus, goods in transit will be shown as such at cost under "Stock-in-Trade"; cash in transit will feature under the heading "Cash at Bank and in Hand."

MARCH 31st, 19—

19— (Previous year)		Head Office (Exeter)	Branches		Total
			Truro	Helston	
£		£	£	£	£
4,000	<i>Fixed Assets:</i>				
	Freehold Premises, at cost	1,750	1,500	750	4,000
1,150	Goodwill, at cost (£1,500), less amounts written off to date (£350)	—	1,000	150	1,150
480	Furniture and Fittings, at cost (£600), less provision for depreciation to date (£193)	165	190	52	407
160	Motor Vans, at cost (£400), less pro- vision for depreciation to date (£274)	36	60	30	126
£5,790		£1,951	£2,750	£982	£5,683
	<i>Current Assets:</i>				
2,850	Stock-in-Trade, as certified by Man- aging Director	870	1,529	750	2,949
3,875	Debtors and payments in advance	1,200	2,100	450	3,750
	Cash at Bank and in Hand	760	551	210	—
1,060	Cash in Transit	—	60	40	1,621
	Branch Accounts (as per contra):—				
	Truro	5,003	—	—	—
	Helston	1,419	—	—	—
£7,785		£9,052	£4,240	£1,450	£8,320
£13,575		£11,003	£6,990	£2,432	£14,003

An illustration is given on pages 170 and 171 of a Branch Account in the Head Office books and the reciprocal Head Office Account in the branch books.

Final Accounts in Head Office Books. On receipt of the branch accounts, Head Office opens in its books a "Branch Trading and Profit and Loss Account" and transfers the items thereto by means of Journal entries. The formula for these Journal entries is as follows :

(1) *Debit* Branch Trading Account and *credit* Branch Account with Opening Stock and Purchases and other Trading Account items.

(2) *Credit* Branch Trading Account and *debit* Branch Account with Sales and Closing Stock.

(3) *Debit* Branch Trading Account and *credit* Branch Profit and Loss Account with the Gross Profit.

(4) *Debit* Branch Profit and Loss Account and *credit* Branch Account with the expenses met by the branch out of its income.

(5) *Debit* Branch Profit and Loss Account and *credit* Branch Account with depreciation written off assets employed at the branch, and interest on the assets of the branch where interest is taken into consideration.

(6) *Debit* Branch Profit and Loss Account and *credit* expenses accounts with any Head Office expenses chargeable to the branch.

(7) *Credit* Branch Profit and Loss Account and *debit* Branch Account with discounts and other sundry items of income received by the branch.

(8) *Debit* Branch Profit and Loss Account and *credit* General (i.e., Head Office) Profit and Loss Account with the Net Profit of the branch, or the reverse entry if a loss has been incurred.

In preparing the Profit and Loss Account for the business as a whole, branch items and Head Office items may be added like to like, and the accounts submitted will show the one set of figures only ; or the Branch and Head Office Profit and Loss Accounts may be prepared separately or in columnar form, the net profits being combined in the General Profit and Loss Account of the whole concern.

COMBINED BALANCE SHEET

In the Head Office books the balance of the Branch Account will exactly equal the balance of the Head Office Account in the Branch Balance Sheet. Both balances are omitted from

the total columns of the combined Balance Sheet as they cancel out. In their place the detailed liabilities and assets of the branch are shown added to similar items at the Head Office and other branches. Sometimes it is not considered advisable for the branch to know the full amount of capital invested in such fixed assets as Goodwill, Premises, etc., or such liabilities as mortgages secured on the branch premises. Referring to the Truro Branch Account (in the Head Office Ledger) and the reciprocal Head Office Account (in the Truro Branch Books) shown on pages 170 and 171, it will be noticed that the balances on these accounts do not include the value of Goodwill, £1,500, and Freehold Premises £1,500 on the one side, or the Mortgage on Freehold Premises £900 on the other side, as shown in the combined Balance Sheet on pages 172 and 173. These items appear in separate accounts in the Head Office Private or Nominal Ledger and are brought into the combined Balance Sheet at the accounting date.

The example of a combined Balance Sheet given on pages 172 and 173 shows the assets and liabilities of the Head Office and two branches in columnar form. Where there is a large number of branches the comparative figures are usually conveniently grouped on separate schedules so that the relative efficiency of each branch may be seen by the Control Management at Head Office. Such detail is not normally placed before the shareholders, to whom a Balance Sheet is presented with the figures as shown in the total columns of the example.

The Trading and Profit and Loss Accounts are drawn up in similar form. If readers will refer to the Departmental Trading and Profit and Loss Accounts of A. B. & Co., Ltd., shown on page 158, and substitute the Head Office and names of the branches for the departmental headings, they will obtain a picture of a combined Trading and Profit and Loss Account of a Head Office and two branches.

The figures shown in the specimen Head Office and Branch Accounts on page 170, and the combined Balance Sheet on page 172, have been constructed on the hypothesis that the "Drugs" department refers to the Truro branch of the business to emphasise the prefatory explanation that a branch may be regarded as a department situated at a distance.

Appendix

EIGHTH SCHEDULE TO THE COMPANIES ACT, 1948

BALANCE SHEET

2.—The authorised share capital, issued share capital, liabilities and assets shall be summarised with such particulars as are necessary to disclose the general nature of the assets and liabilities, and there shall be specified

- (a) any part of the issued capital that consists of redeemable preference shares, and the earliest date on which the company has power to redeem those shares ;
- (b) so far as the information is not given in the profit and loss account, any share capital on which interest has been paid out of capital during the financial year, and the rate at which interest has been so paid ;
- (c) the amount of the share premium account ;
- (d) particulars of any redeemed debentures which the company has power to reissue.

3.—There shall be stated under separate headings, so far as they are not written off

- (a) the preliminary expenses ;
- (b) any expenses incurred in connection with any issue of share capital or debentures ;
- (c) any sums paid by way of commission in respect of any shares or debentures ;
- (d) any sums allowed by way of discount in respect of any debentures ; and
- (e) the amount of the discount allowed on any issue of shares at a discount.

4.—(1) The reserves, provisions, liabilities, and fixed and current assets shall be classified under headings appropriate to the company's business :

Provided that

- (a) where the amount of any class is not material, it may be included under the same heading as some other class ; and
 - (b) where any assets of one class are not separate from assets of another class, those assets may be included under the same heading.
- (2) Fixed assets shall also be distinguished from current assets.
- (3) The method or methods used to arrive at the amount of the fixed assets under each heading shall be stated.

5.—(1) The method of arriving at the amount of any fixed assets shall, subject to the next following sub-paragraph, be to take the difference between

- (a) its cost or, if it stands in the company's books at a valuation, the amount of the valuation ; and
- (b) the aggregate amount provided or written off since the date of acquisition or valuation, as the case may be, for depreciation or diminution in value ;

and for the purposes of this paragraph the net amount at which any assets stand in the company's books at the commencement of this Act (after deduction of the amounts previously provided or written off for depreciation or diminution in value) shall, if the figures relating to the period before the commencement of this Act cannot be obtained without unreasonable expense or delay, be treated as if it were the amount of a valuation of those assets made at the commencement of this Act, where any of those assets are sold, the said net amount less the amount of the sales shall be treated as if it were the amount of a valuation so made of the remaining assets.

(2) The foregoing sub-paragraph shall not apply

- (a) to assets for which the figures relating to the period beginning with the commencement of this Act cannot be obtained without unreasonable expense or delay ; or
- (b) to assets the replacement of which is provided for wholly or partly
 - (i) by making provision for renewals and charging the cost of replacement against the provision so made ; or
 - (ii) by charging the cost of replacement direct to revenue ; or
- (c) to any investments of which the market value (or, in the case of investments not having a market value, their value as estimated by the directors) is shown either as the amount of the investments or by way of note ; or
- (d) to goodwill, patents or trade marks.

(3) For the assets under each heading whose amount is arrived at in accordance with sub-paragraph (1) of this paragraph, there shall be shown

- (a) the aggregate of the amounts referred to in paragraph (a) of that sub-paragraph ; and
- (b) the aggregate of the amounts referred to in paragraph (b) thereof.

(4) As respects the assets under each heading whose amount is not arrived at in accordance with the said sub-paragraph (1) because their replacement is provided for as mentioned in sub-paragraph (2) (b) of this paragraph, there shall be stated

- (a) the means by which their replacement is provided for ; and
- (b) the aggregate amount of the provision (if any) made for renewals and not used.

6.—The aggregate amounts respectively of capital reserves, revenue reserves and provisions (other than provisions for depreciation, renewals or diminution in value of assets) shall be stated under separate headings :

Provided that

- (a) this paragraph shall not require a separate statement of any of the said three amounts which is not material ; and
- (b) the Board of Trade may direct that it shall not require a separate statement of the amount of provisions where they are satisfied that that is not required in the public interest and would prejudice the company, but subject to the condition that any heading stating an amount arrived at after taking into account a provision (other than as aforesaid) shall be so framed or marked as to indicate that fact.

7.—(1) There shall also be shown (unless it is shown in the profit and loss account or a statement or report annexed thereto, or the amount involved is not material)

- (a) where the amount of the capital reserves, of the revenue reserves or of the provisions (other than provisions for depreciation, renewals or diminution in value of assets) shows an increase as compared with the amount at the end of the immediately preceding financial year, the source from which the amount of the increase has been derived ; and
- (b) where
 - (i) the amount of the capital reserves or of the revenue reserves shows a decrease as compared with the amount at the end of the immediately preceding financial year ; or
 - (ii) the amount at the end of the immediately preceding financial year of the provisions (other than provisions for depreciation, renewals or diminution in value of assets) exceeded the aggregate of the sums since applied and amounts still retained for the purposes thereof ;the application of the amounts derived from the difference.

(2) Where the heading showing any of the reserves or provisions aforesaid is divided into sub-headings, this paragraph shall apply to each of the separate amounts shown in the sub-headings instead of applying to the aggregate amount thereof.

8.—(1) There shall be shown under separate headings

- (a) the aggregate amounts respectively of the company's trade investments, quoted investments other than trade investments and unquoted investments other than trade investments ;

- (b) if the amount of the goodwill and of any patents and trade marks or part of that amount is shown as a separate item in or is otherwise ascertainable from the books of the company, or from any contract for the sale or purchase of any property to be acquired by the company, or from any documents in the possession of the company relating to the stamp duty payable in respect of any such contract or the conveyance of any such property, the said amount so shown or ascertained so far as not written off or, as the case may be, the said amount so far as it is so shown or ascertainable and as so shown or ascertained, as the case may be ;
- (c) the aggregate amounts of any outstanding loans made under the authority or provisos (b) and (c) of sub-section (1) of section fifty-four of this Act ;
- (d) the aggregate amount of bank loans and overdrafts ;
- (e) the net aggregate amount (after deduction of income tax) which is recommended for distribution by way of dividend.

(2) Nothing in head (b) of the foregoing sub-paragraph shall be taken as requiring the amount of the goodwill, patents and trade marks to be stated otherwise than as a single item.

(3) The heading showing the amount of the quoted investments other than trade investments shall be sub-divided, where necessary, to distinguish the investments as respects which there has, and those as respects which there has not, been granted a quotation or permission to deal on a recognised stock exchange.

9.—Where any liability of the company is secured otherwise than by operation of law on any assets of the company, the fact that that liability is so secured shall be stated, but it shall not be necessary to specify the assets on which the liability is secured.

10.—Where any of the company's debentures are held by a nominee of or trustee for the company, the nominal amount of the debentures and the amount at which they are stated in the books of the company shall be stated.

11.—(1) The matters referred to in the following sub-paragraphs shall be stated by way of note, or in a statement or report annexed, if not otherwise shown.

(2) The number, description and amount of any shares in the company which any person has an option to subscribe for, together with the following particulars of the option, that is to say :

- (a) the period during which it is exercisable ;
- (b) the price to be paid for shares subscribed for under it.

(3) The amount of any arrears of fixed cumulative dividends on the company's shares and the period for which the dividends or, if there is more than one class, each class of them are in arrear, the amount to be stated before deduction of income tax, except that,

in the case of tax-free dividends, the amount shall be shown free of tax and the fact that it is so shown shall also be stated.

(4) Particulars of any charge on the assets of the company to secure the liabilities of any other person, including, where practicable, the amount secured.

(5) The general nature of any other contingent liabilities not provided for and, where practicable, the aggregate amount or estimated amount of those liabilities, if it is material.

(6) Where practicable the aggregate amount or estimated amount, if it is material, of contracts for capital expenditure, so far as not provided for.

(7) If in the opinion of the directors any of the current assets have not a value, on realisation in the ordinary course of the company's business, at least equal to the amount at which they are stated, the fact that the directors are of that opinion.

(8) The aggregate market value of the company's quoted investments, other than trade investments, where it differs from the amount of the investments as stated, and the stock exchange value of any investments of which the market value is shown (whether separately or not) and is taken as being higher than their stock exchange value.

(9) The basis on which foreign currencies have been converted into sterling, where the amount of the assets or liabilities affected is material.

(10) The basis on which the amount, if any, set aside for United Kingdom income tax is computed.

(11) Except in the case of the first balance sheet laid before the company after the commencement of this Act, the corresponding amounts at the end of the immediately preceding financial year for all items shown in the balance sheet.

PROFIT AND LOSS ACCOUNT

12.—(1) There shall be shown

- (a) the amount charged to revenue by way of provision for depreciation, renewals or diminution in value of fixed assets ;
- (b) the amount of the interest on the company's debentures and other fixed loans ;
- (c) the amount of the charge for United Kingdom income tax and other United Kingdom taxation on profits, including, where practicable, as United Kingdom income tax any taxation imposed elsewhere to the extent of the relief, if any, from United Kingdom income tax and distinguishing, where practicable, between income tax and other taxation ;
- (d) the amounts respectively provided for redemption of share capital and for redemption of loans ;

- (e) the amount, if material, set aside or proposed to be set aside to, or withdrawn from, reserves ;
- (f) subject to sub-paragraph (2) of this paragraph, the amount, if material, set aside to provisions other than provisions for depreciation, renewals, or diminution in value of assets or, as the case may be, the amount, if material, withdrawn from such provisions and not applied for the purposes thereof ;
- (g) the amount of income from investments, distinguishing between trade investments and other investments ;
- (h) the aggregate amount of the dividends paid and proposed.

(2) The Board of Trade may direct that a company shall not be obliged to show an amount set aside to provisions in accordance with sub-paragraph (1) (f) of this paragraph, if the Board is satisfied that that is not required in the public interest and would prejudice the company, but subject to the condition that any heading stating an amount arrived at after taking into account the amount set aside as aforesaid shall be so framed or marked as to indicate that fact.

13.—If the remuneration of the auditors is not fixed by the company in general meeting, the amount thereof shall be shown under a separate heading, and for the purposes of this paragraph, any sums paid by the company in respect of the auditors' expenses shall be deemed to be included in the expression " remuneration."

14. (1) The matters referred to in the following sub-paragraphs shall be stated by way of note, if not otherwise shown.

(2) If depreciation or replacement of fixed assets is provided for by some method other than a depreciation charge or provision for renewals, or is not provided for, the method by which it is provided for or the fact that it is not provided for, as the case may be.

(3) The basis on which the charge for United Kingdom income tax is computed.

(4) Whether or not the amount stated for dividends paid and proposed is for dividends subject to deduction of income tax.

(5) Except in the case of the first profit and loss account laid before the company after the commencement of this Act the corresponding amounts for the immediately preceding financial year for all items shown in the profit and loss account.

(6) Any material respects in which any items shown in the profit and loss account are affected

- (a) by transactions of a sort not usually undertaken by the company or otherwise by circumstances of an exceptional or non-recurrent nature ; or
- (b) by any change in the basis of accounting.

INDEX

- Accountancy :
 - exact science, 61
- Adjusting Entries :
 - explanatory, 62
- Administration Expenses :
 - classification, 81
- Agreement for Sale :
 - purpose, 92-3
- Annual Accounts :
 - example, 124-5
 - general meeting, shareholders and accounts, statutory provisions, 119-20
- Annual Report :
 - example, 123
- Annual Return :
 - contents, filing, 97-8, 127
- Annuity Method :
 - depreciation, 64-5
- Appropriation Account :
 - example, 88-9
 - function, 82, 139
- Articles of Association :
 - alterations, 95
 - borrowing powers, 132
 - compulsory clauses *re* Private Company, 94
 - contents, 94-5
 - preference share rights, 130
 - reserves, 137
- Assets :
 - basis of valuation, classification, 84
 - depreciation, 134
 - grouping, 139-40, 176-7
 - stamp duty on conveyance, 91
- Auditor's remuneration, 181
- Auditors' Report :
 - examples, 89, 125
 - procedure at General Meeting, 122
 - purpose, 77
 - subsidiary companies, 122
 - supplying copies, 122
- Bad Debts :
 - journal entries, example, 31
- Bad Debts Journal :
 - function, 43-4
- Baker and Confectioner :
 - Columnar Sales Ledger, example, 38-9
- Balance Sheet :
 - branch, example, 172-3
 - comparative figures, 180
 - contents, 120, 176-80
 - Eighth Schedule contents, 176-80
 - examples, 88-9, 100, 124-5, 142-3
 - explanatory, 82-5
 - function, 78
 - signing and circulating, statutory provisions, 82-3, 122
 - submission at General Meeting, 120
 - subsidiary companies, information *re* profits and losses, 121-2
 - supplying copies, 122
 - taxation entries, 123
- Balancing :
 - Control Accounts, 43-4
 - theory, 4-5
- Bank Pass Book :
 - agreement with Cash Book, 6
- Bank Reconciliation Statement :
 - example, 14-5
- Bills of Exchange :
 - discounting, 28-9
 - function, 26
- Bills Payable Diary, 27
- Bills Payable Journal, Book :
 - example, 28-9
 - posting, 26
 - Self-balancing System, 50-1
- Bills Receivable Journal, Book :
 - example, 28-9
 - posting, 27
 - Self-balancing System, 45-6
- Bonus Shares :
 - example, explanatory, 136
- Book Debts :
 - Assignment, 107, 112
- Borrowing Powers
 - defined in Articles, 132
- Branch Accounts :
 - Balance Sheet, example, 172-3
 - branch and head office accounts, example, 170-1
 - administration methods, control, 161-2, 168-9
 - disbursements, records, 163
 - Expenses Journal, 163-4
 - Goods Requisition Book, 162
 - Goods sent to Branches Account, 163-9

Branch Accounts (*cont.*) :

- head office expenses, "loading," 168
- Independent Units, 168-74
- Inter-branch comparisons, 168
- items in transit, 173
- Journal entries, 174
- Ledger Accounts, 165-71
 - examples, 170-1
- maximum head office control, 162-8
- mutual transactions, 169
- Petty Cash and Wages Returns, 163-4
- posting, 174
- Profit and Loss Account, function, 172
- Remittances, Account, 169
 - Book, 163
- Returns and Allowances Book, 162
 - Journal, 163
 - sales records, 162
 - credit entries, 168
 - selling agency, 161-2
 - stock records, 163
 - Stock Return, example, 164
 - Supplies Account, 169
 - example, 166-7
 - Supplies Journal, 163
 - example, 166-7
 - Suspense Account, 173
 - Trading Account, function, 172
 - posting, 174
 - Wages and Petty Cash Returns, 163-4

Card Ledgers :

- use and internal check, 34-5

Cash Books :

- Cash Received Book, examples, 8-11
 - example, Self-balancing System, 46-7
- Cheque Payments Book, examples, 10-3
 - example, Self-balancing System, 50-1
- function, 3
- principles and practice, 6

Cash Float :

- method, 17

Cash Registers :

- aid to accuracy, 8

Cash Sales :

- posting, recording, 8-9

Cash Trade :

- records, 7
- suitable books, 116-7

Certificate of Incorporation :

- issue, 96

Certificate to Commence Business, 92, 96

Cheque Payments Book :

- departmental division, 154
- examples, 10-3, 50-1

Cheques :

- payments by, 10

Cinema :

- cash records, example, 12-3

Columnar Sales Ledgers :

- examples, 38-9
- function, posting, 36-7

Companies Act, 1948 :

- accounts, auditors (S.162), 77
- Annual Return (S.124-9), 97, 127
- Balance Sheet contents (S.149), 82-3, 120, 176-80
- Directors' salaries, pensions, etc., in accounts (S.196-7), 120, 181
- Directors' responsibilities, annual accounts (S.148), 77
- Eighth Schedule, 176-81
- exempt private company, 97
- financial records (S.147-53), 34, 118-9
- floating charges (S.322), 132
- loans to officers, etc. (S.197), 120
- Minute Books (S.145), 127
- Profit and Loss Account (S.148), 119-20
- proper books of account, failure to keep (S.331), 119
- reduction of capital (S.66-71), 133
- reserves (S.157), 137-8
- shareholders, limitation of members (S.28), 94, 126
- subsidiary companies (S.150-3), 120-2

Comparative Accounts :

- use, 139-40

Contingent liabilities, 180

Contract for Sale :

- contents, 93
- filing fees, 96
- stamp duty, 91-2

Control Account Ledger :

- explanatory, 44

Control Accounts :

- Self-balancing System, examples, 43, 48

- explanatory, 42-52
- totals in Balance Sheet, 83-5

Conversion into Company :

- entries, examples, 99-115

Cost of Manufacture, 79

Cost of Sales :

- computation, example, 141

Credit Entries :

- examples, 2

- Credit Trade :
 - records, 9-11
 - suitable books, 117
- Creditors :
 - Balance Sheet entries, 83
 - treatment on company formation, 91
- Cumulative Preference Shares, 130
- Debentures :
 - Mortgage debentures, floating charge, 131-2
 - registration, 132
 - rights of debenture holders, 129
 - simple or naked debentures, 132
 - specific or fixed charge, 132
 - stated in Balance Sheet, 83, 179
 - Trustees for debenture holders, 131
- Debit Entries :
 - examples, 2
- Debtors :
 - Balance Sheet entries, 84
 - treatment on company formation, 92
- Deferred Shares, 131
- Departmental Accounts :
 - advantages, 148
 - Cash Books, 149-54
 - other subsidiary books, 148-9
 - Purchases Day Book, Purchases Account, examples, 150-1
 - Sales Day Book, Sales Account, examples, 152-3
- Departmental Trading and Profit and Loss Accounts :
 - allocation and grouping of expenses, examples, preparation, 156-60
- Departmental Transfer Journal :
 - example, 156-7
 - explanatory, 155
- Depreciation :
 - consideration on purchase of a business, 145
 - entries, 66-7
 - grouping in Final Accounts, 81-2
 - legal requirements, 67, 134, 177, 180
 - provision for, 63-7
 - various methods, 64-6
- Diminishing Balance Method :
 - depreciation, 64
- Directors :
 - contract to take shares, 96
 - fees, statutory provisions, filing of Consent to Act, 96
 - Loans to Officers, etc., statutory provisions, 120
- Directors' Report :
 - annexed to Balance Sheet, 122
 - example, 123
 - submission at Annual General Meeting, 120
 - subsidiary companies, 122
- Disbursements :
 - branch, 163
- Discounts :
 - departmental division, 154
 - posting, 7
- Distribution Expenses :
 - classification, 81
- Dividends :
 - entries to record, examples, free of tax, 135-6
 - preference, arrears, 179
 - profits available, 134
- Double Entry :
 - origin, principles, 1-4
- Equal Instalment Method :
 - depreciation, 64
- Equity Shares, 130
- Errors :
 - detection by Trial Balance, 60
- Exempt private company, 97
- Expenses and Purchases Day Book, 18-9, 21-2
 - example, 20-1
- Expenses Due and Accrued :
 - examples, 68
 - explanatory, Balance Sheet and double-entry, 81-3
 - treatment, 62-3
- Factory Expenses, 79
- Filing Documents with Registrar :
 - Private Company, fees, 95-6
 - Public Company, fees, 96
- Final Accounts :
 - Auditor's duty, 77
 - Directors' approval, 85
 - grouping expenses, 156-60
 - information to be given, 83-4
 - presentation, 78, 139-40
 - purpose, 77-8
- Financial Books :
 - Statutory provisions, 118-9
- Fixed Assets :
 - depreciation, 134, 177, 181
- Float, Cash, 17
- Floating Capital :
 - loss, 134
- Floating Charge :
 - registration, 132
- Founders' or Management Shares, 131
- Furniture and Fittings Account :
 - example, 72-3

- General Meeting :
 - shareholders and accounts, statutory provisions, 119-20
- General Reserves, 136-8
 - entries in Balance Sheet, 83
- Goods Received Book, 41
- Goods Requisition Book, 162
- Goodwill :
 - in Balance Sheet, 179
 - value, on company formation, 92
 - when purchasing a business, 146
- Gross Profit, 79
 - percentage variations, 141, 144
- Head Office :
 - control, records, 162-3, 169
- Head Office Account :
 - Branch accountancy, 174-5
- Heat and Light Account :
 - example, 68-9
- Hire Purchase :
 - example of Journal entries, 31-3
- Hotel Trade :
 - Columnar Visitors' Ledger, 37, 40
 - example, 38-9
- Imprest System :
 - Petty Cash, 17
- Income and Expenditure Account :
 - submission at Annual General Meeting, 120
- Income Due and Accrued, 81-2
 - adjustment, 63
 - example, 68
- Income Tax :
 - Balance Sheet entries, 123, 180
 - profit and loss entries, 181
- Incorporation :
 - Private Limited Company, 90-2
- Initial Trading Transactions :
 - method of recording, 114-5
- Insurance Account :
 - example, 54-5
- Insurance Policy :
 - method of depreciation, 65
- Interest :
 - departmental considerations, 160
- Internal Check :
 - detection of errors, 36
- Investments :
 - Balance Sheet entries, 140, 177-80
- Invoice Book :
 - " Copy Invoice " method, example, posting, 24-5
- Invoices :
 - entries in Purchases Day Book, 18-22
- Journal Proper, 29-30
 - examples, 30-2, 101, 107, 109, 135, 136, 138, 174
- Journals :
 - function, 2-3
- Ledger :
 - function, 2
 - kinds, 4
- Limited Liability :
 - financial and statistical requirements, 118-9
- Liquid Assets, 141-4
- Loans :
 - in Balance Sheet, 83, 179
- Loans to Officers, etc., 120
- Loose-leaf Ledgers :
 - advantages, internal check, 34, 44
- Loss on Sale of Assets :
 - example of Journal entries, 32-3
- Losses Prior to Incorporation, 93
- Machinery and Plant Register :
 - purpose, 67
- Management or Founders' Shares, 131
- Manufacturing Account, 78
 - example, 84-5
- Manufacturing Cost :
 - items chargeable, 79
- Memorandum :
 - company, contents, 94
 - filing fees, 95-6
 - subscribers, 94
- Memorandum Books :
 - modern kinds, 117
 - original purpose, 2
- Minute Books :
 - Loose-leaf, 128
 - signing, 127
- Mortgage Debentures :
 - entries in Balance Sheet, 83
 - explanatory, restriction of credit, 132-3
- Mortgage Interest Account :
 - example, 70-1
- Mortgages and Charges :
 - registration fees, 97
- Motor Expenses Account :
 - example, 70-1
- Motor Vans Account :
 - example, 72-3
- Name of Company :
 - in Memorandum, 94
- Net Profit :
 - consideration on purchasing a business, trend, 145

- Net Profit (*cont.*):
 explanatory, 80-1
 percentage variations, 141
 Nominal or Private Ledger:
 arrangements of accounts, rulings,
 53-4
 balancing, 85
 examples, 102-5, 110-1
 function, 53
 posting, 56-7

 Objects of Company:
 statement in Memorandum, altera-
 tions, 94
 Omnibus, Business:
 records, 12
 Operating Businesses:
 records, 12-3
 Ordinary Shares:
 kinds, Deferred, Preferred, 130-1

 Partnership:
 conversion into Company, entries,
 99-115
 Patents:
 statement in Balance Sheet, 179
 Payments in Advance:
 double entry, 82
 examples, 68
 Personal Ledger:
 posting, 5
 Petty Cash Book, 15-7
 example, 16-7
 Imprest system float, 17
 Preference Shares:
 kinds, 130
 Redeemable, 144
 Prime Cost:
 term explained, 78
 Private Limited Company:
 advantages of incorporation, legal
 steps in conversion, 91-8
 circulating Balance Sheet, copies,
 122
 entries, 99-115
 notices of meetings, 122
 suitable books, 115-7
 Private or Nominal Ledger:
 arrangements of accounts, rulings,
 53-4
 balancing, 85
 examples, 102-5, 110-1
 function, 53
 posting, 56-7
 Profit:
 available for dividends, capital
 nature, 134
 prior to incorporation, 92

 Profit and Loss Account:
 branch accountancy, 174
 comparative figures, 139, 181
 departmental, 156-60
 example, 158-9
 Eighth Schedule contents, 180-1
 examples, 86-7, 124-5
 expenses chargeable, 81
 function, 77
 preparation, 80-2, 180-1
 submission at Annual General
 Meeting, 119
 Prospectus, or Statement in
 Lieu:
 filing, 96
 Provisions and Reserves, 62, 136-8,
 178
 Public Companies:
 circulating Balance Sheet, copies,
 notices of meetings, 122
 Purchases Account:
 departmental example, 150-1
 posting, 2
 Purchases and Expenses Day Book:
 example, 20-1
 explanatory, 18-9, 21-2
 Purchases Day Books:
 entries, postings, examples, 18-
 22
 example, Self-balancing System,
 50-1
 Purchases Ledger Accounts:
 example of balancing, 40
 Purchases Ledgers:
 types, internal check, 34, 40-1
 Self-balancing System, 48-52
 Control Account example, 48
 Purchases Returns Day Book:
 posting, 22
 Self-balancing System, 51
 Purchasing a Business:
 practical considerations, 145-7

 Realisation Account:
 construction, Journal entries,
 100-6
 Reconciliation:
 Bank Pass Book, with, 6
 Statement, 14-5
 Reduction of Capital, 133
 Register of Directors and Secretaries,
 126-7
 Register of Directors' shareholdings,
 126
 Register of Members, 126
 Register of Mortgages and Charges,
 127
 Registered Office:
 situation, Return, filing fee, 96

- Registrar of Companies :
 filing of documents, fees, Private Company, 95-7
 Public Company, 95-7
- Rent Account :
 example, 54-5
 rent from sub-let, example, 72-3
- Reserve Capital, 131
- Reserves :
 Contingencies, and general, 136-8
 entries in Balance Sheet, 83, 140
 sur-tax liability, 90
- Reserves and Provisions, 62, 136-8, 178, 181
- Return of Allotments, 96
- Returns and Allowances Book :
 Branch Accountancy, 162
- Returns Inwards Day Book :
 function, posting, 25-6
 Self-balancing System, 45
- Returns Outwards Day Book :
 function, posting, 22
 Self-balancing System, 51
- Salaries and Wages :
 records, 117
- Sale Agreement, 92-3
- Sales :
 computation of cost, 141
- Sales Account :
 departmental example, 152-3
 example, 56-7
 posting, 4
- Sales Day Book :
 entries, examples, 23-5
 example, Self-balancing System, 46-7
- Sales Ledger Accounts :
 balancing, example, 35-6
- Sales Ledgers :
 Columnar Sales Ledger, 36-40
 Control Account, example, 43
 loose-leaf advantages, 44-5
 Self-balancing System, 42-8
 types, internal check, 34-6
- Sales on Credit :
 Branch procedure, 168
- Sales Returns Day Book :
 posting, 25-6
 Self-balancing System, 45
- Self-balancing System, 42-52
 Purchases Ledger, 48-52
 Control Account, example, 48
 Sales Ledger, 42-8
 Control Account, example, 43
- Selling Expenses :
 classification, 81
- Share Capital :
 floating, 134
 general structure, kinds, registration, 129-31
 increase, 133
 lost capital, 133
 Redeemable, 144, 176
 Reduction, 133
 Registered amount, 94
 filing fees, 95
 statement in Balance Sheet, 83
- Shareholders :
 circulating accounts, 122
 limitation of numbers, 94, 126
 rights, 129-31
- Shares :
 kinds, 129-31
 options, 179
- Share Warrants, 131
- Sinking Fund Method :
 depreciation, 65
- Special Resolution :
 when required, 95, 133
- Stamp Duty :
 on Contract for Sale, 91-2
- Statement of Affairs :
 origin, 1
- Statutory Books, 126-8
- Statutory Declaration :
 filing fee, 96
- Stock :
 conversion from shares, 131
- Stock Books :
 explanatory, 74-5
- Stock-in-Trade :
 entries in Balance Sheet, 84
 Trial Balance, 78
- Stock or Stores Control System, 41
- Stock Records and Returns :
 Branch Accountancy, 163-4
- Stock-taking :
 methods, precautions, 74-6
- Stock Transfer Journal :
 departmental example, 156
 Issue and Receiving Notes, 155
- Stock Valuations :
 considerations on purchase of a business, 145
 errors, discovery, 140
- Straight Line Method :
 depreciation, 64
- Subscribers to Memorandum, 94
- Subsidiary Companies :
 provisions of the Companies Act, 120-2
- Suitable Books :
 Cash Trade, Credit Trade Memorandum books, 115-7
- Sur-tax :
 company, when liable, 90
- "Table A" :
 adoption, 94
- Trade Marks :
 Balance Sheet entries, 179

- Trading Account, 77
 example, 86-7
 preparation, debit and credit items, 79-80
 departmental example, 158-9
- Transfer Journal :
 Self-balancing System, 47, 52
- Transfer of Shares :
 restriction, 94
- Trial Balance, 4-5
 agreement, 59-61
 construction of Final Accounts, 78
 examples, 59, 113
 listing balances, 53, 58
- Trustees :
 for Debenture-holders, 132
- Turnover :
 sales, variations, 140, 144
- Unexpired Expenditure :
 adjustments, 63
 examples, 68
 double entry, 82
 ,
- Valuation Method :
 depreciation, 84
- Wages and Salaries :
 records, 117
- Working Capital :
 computation, example, 143
 dangers of deficiency, 144
 defined, 141-2

Let Jordans help you

Annual Returns

Send your completed Annual Return to Jordan & Sons, Limited, who will at once attend to the stamping and registration, advising you of any amendments which may be required.

FORM 6A (for Public, Private or Exempt Private Company), 6d.; by post 8½d.

FORM 8A (Continuation Sheets for Form 6A), 2½d.; by post 5d.

Also supplied for use with Addressing Machine.

Searches

Searches conducted by experienced investigators, on behalf of Secretaries of Companies, at all Registries and Public Departments. Reports furnished and copies of documents obtained.

Stamping, Registration and Printing

Stamping and Registration of all Company documents, e.g., Debentures, Mortgages, Printing of Notices, Proxies, Resolutions and Balance Sheets.

JORDAN & SONS, LIMITED

Company Registration Agents

116 CHANCERY LANE, LONDON, W.C.2

Telephone : HOLborn 0434.

Telegrams : Certificate, Estrand, London.

THE AUDITOR AND ACCOUNTANT AND MECHANISED ACCOUNTING

By J. H. Eurlon, F.S.A.A., F.I.M.T.A. Second Edition. Demy 8vo. Cloth. "We therefore turn to this book hopefully and find that it is a very valuable addition to the literature discussing accounting machinery from the point of view of the responsible head of an accounting department, and everyone concerned with the audit of accounts kept by machine methods will find it valuable."

—*Accountancy.*

15s. net; by post 15s. 6d.

GROUP ACCOUNTS

By D. J. Bogie, T.D., B.Com., Ph.D., C.A. A complete manual on consolidated accounts. In the preparation of consolidated accounts, the practising accountant will appreciate the novel methods of simplification explained in this comprehensive work. Much of the subject-matter is necessarily complicated, but the Author, evading none of the difficulties, reduces them to workable formulæ. Diagrams are freely used in fully-worked, practical examples.

3 gns.; postage 9d.

HOTELS: ADMINISTRATION AND ACCOUNTS

By A. R. Lewis, formerly Chief Accountant, The Gordon Hotels, Ltd., The Dorchester Hotel, Ltd., The May Fair Hotel, Ltd., The Hotel Metropole, Monte Carlo, etc. Second Edition. Crown 4to. Cloth. An up-to-date book on the management, administration and departmental methods of the modern hotel, for proprietors, managers, accountants and trainees. The needs of large and small establishments are catered for, and the book includes numerous specimen diagrams, charts and tabular systems.

20s. net; by post 20s. 10d.

JORDANS MODERN BOOK-KEEPING

By Frank H. Jones, F.L.A.A., A.C.I.S. Crown 8vo. Cloth. Text and examples are thoroughly practical and up-to-date. Outworn customs and expressions have been discarded. A special feature is made of "common mistakes to avoid." More than one-half of the seven hundred questions and exercises contained in both parts have been taken from the examination papers of the leading examining bodies.

PART 1 (*Second Edition*), for elementary students and first-year classes. 6s.; by post 6s. 5d.

PART 2, for second-year classes. 6s.; by post 6s. 6d.

