THE PRINCIPLES OF MODERN BOOKKEEPING.

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OF

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PREFACE.

THIS book does not profess to deal exhaustively with the subject of Bookkeeping as an art, attention being concentrated on its spirit, rather than on its form. All systematic bookkeeping is based on a principle, but on one which modern abbreviations necessarily tend to obscure. The book is an attempt to set forth this principle, and to show that, however obscured it may be, yet it exists, and must be thoroughly grasped by anyone who would become proficient in the art. Such forms as are employed are used only to illustrate the text—they are not given as dogmatic instances of how any particular bookkeeping problem should be solved. The principle is explained and insisted upon, and it is left to the reader, or his teacher, to apply this principle in any desired direction.

I have received, and gratefully acknowledge, valuable criticisms and help from Mr. T. G. Mellors, F.C.A., Mr. R. B. Baggaley, A.C.A., Mr. H. G. Howitt, A.C.A , and my managing clerk Mr. J. W. Billson, who have been good enough to read the book in manuscript or proof.

WM. R. HAMILTON.

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CHAPTER I.

INTRODUCTORY.

THE keeping of books of account is generally considered as a means to an end, rather than as an end in itself—a means to the proper ascertainment of the position of the business concerned in relation to its various affairs, so far as this can be shown by figures From this point of view the shorter the means adopted to secure a result the better. Bookkeeping to-day is not what it was fifty or a hundred years ago, as it has been affected by the general desire to shorten labour The result is that, although good modern bookkeeping is much more efficient than the bookkeeping of a bygone age, yet the very brevity which is its advantage is apt to obscure the principles upon which it is founded.

But though to the owner of a business the keeping of books is only a means to an end, yet to the bookkeeper or to the accountant, books are the tools with which he works, and he needs therefore to have complete familiarity with them—a familiarity which can only be attained when he has so grasped the principle on which they are kept as to be able to apply it to every conceivable transaction.

The end to be achieved in bookkeeping is the accurate recording of the minimum amount of financial information with which the business immediately concerned can be successfully carried on. In every business there is a minimum of financial information necessary for bare existence. Beyond this minimum there is (especially in manufacturing businesses) a vast amount of information, of an analytical sort, which books may, if necessary, be devised to afford. But, as bookkeeping costs money, the question of how much of this possible information should be produced is (or ought to be) governed solely by the cost of obtaining it in relation to its value when obtained. Thus division into departments is a commercial necessity in a large store, and it pays to arrange the books accordingly. It would be equally possible so to arrange them as to ascertain the amount of sales for each hour of the day, or to separate from the general sales those made to customers apparently of foreign nationality. But the information, however interesting it might be, would not be worth the trouble (*i.e* the cost) which it involved.

Whatever be the amount of bookkeeping adjudged necessary, accuracy is a condition which must be attained. As books are kept by human agency, with all its liability to error, it is impossible to accept the work of the bookkeeper, as it comes fresh from his hand, as beyond all question accurate. It is needful to apply some check. If this check can take the form of separating his work into two parts which ought to be equal, and ascertaining periodically that they are equal, that is obviously much better than merely revising what he has done, in the order in which he has done it.

The system of check which answers all requirements and is at the bottom of all efficient bookkeeping is that which is known as "Double Entry."

There are many people who, if asked what double-entry meant, as applied to bookkeeping, would say that it meant entering everything twice. And so far are they from being wrong that, carried to its fullest extent, it really means entering everything four times—twice in the Journal and twice in the Ledger. The idea underlying the word "double" in the term is that it takes two to make a transaction, and that any particular trader entering into a transaction with another person ought to record it both as regards himself and as regards the person with whom he deals. This method of recording a transaction is frequently stated as though it were an axiom. But it is no such thing; it is (or was) nothing but a question of practical convenience, for there is no inherent reason why an entry of a sale in a man's Day Book should not be used for the double purpose of recording the transaction as it affects him and also as it affects the customer, and in nearly all modern books this is what, in effect, is done. Nevertheless, the principle of double-entry is at the bottom of all bookkeeping, and it is necessary to understand thoroughly the long and formal way of keeping books before short cuts can be taken with safety.

CHAPTER II.

BOOKS IN EVERYDAY USE BRIEFLY DESCRIBED. DAY-BOOK—INVOICE BOOK—CASH BOOK—LEDGER.

It is assumed that the reader has some practical familiarity with at least the simpler kinds of commercial books, and that he is aware that there is a method by which their accuracy can be demonstrated. It is easy to perceive that there is some kind of system in them. Some books, it may be seen, are written up from day to day or from hour to hour. As various events happen, so are entries made. The receipt and payment of cash are recorded in a book kept for such things; while there is another book kept for recording credit sales—*i.e.*, sales effected which are not paid for at the time but are charged to the customers; and yet another book for recording the purchases made by the business.

Obviously there is here some kind of specialisation which forbids the mixing up of cash with sales, or purchases with either. It is also obvious that each of these books is arranged in chronological order.

But these books do not exhaust the set. There are other books, called Ledgers, which are also in common use but are not of necessity entered up from day to day, though they may be. (The word "Ledger" comes from the old Dutch "leggen" to lie, and the idea is that of a book kept normally in one place.) The Ledger patently differs from the other books. It is divided into a number of accounts mostly headed with the name of a person or firm, and these accounts contain entries relating both to cash and to goods. Moreover, each account has two columns, and a very casual inspection shows that in each account which is that of a person or firm, these columns are in more or less agreement with each other as to amount.

It can easily be ascertained that the entries in the Ledger are derived from the other, or chronological, books. It differs from these other books in that it is not kept in chronological order, but that, as has been said, it is divided up into a great number of accounts. The arrangement, in short, is analytical. If it is desired to find out what happened in the business on a certain day, say the 1st of May, a reference to the various chronological books for that day will give the information at once. If it is desired to find out, not what happened on a particular day, but what has happened as regards a particular person, say John Thompson, with whom the business has dealings, the Ledger is the book to refer to, and the place in the Ledger to turn to is the page headed with John Thompson's name.

Here there is an evidence of system which anyone having access to books may easily see—two classes of books, one arranged chronologically, the other analytically; while the chronological books have the further evidence of system, that they are themselves so divided that each class of transaction has a book to itself.

It may be stated at this point, to be emphasised later, that in all well-kept books the entries in the two classes of books exactly correspond when taken as a whole. Every item in the chronological books goes into the Ledgers, and the Ledgers contain nothing which has not come from the chronological books.

This exact correspondence of the two classes of books looks like double-entry, and indeed it is. But though it is an evolution from, and improvement upon, the original double-entry, it is *not* the original; and this original, cumbrous in practice, but simple in theory, must be understood by everyone who desires to attain proficiency in the art of bookkeeping.

The chronological books vary with the business concerned, both in name and in number. The book used to record the sales is generally known as the "Day Book," but it may be called by another name, such as the "Sales Day Book," or the "Sales Journal." And so far from there being of necessity only one book, there may be several, or even dozens, in use. Where there are departments or some classification of sales, there may be a Day Book for each department or class. Each department again may have several Day Books, perhaps one for Mondays, Wednesdays, and Fridays, and another for the other days. Moreover, in these days of cards, loose-leaf books, carbon copies, and other devices, the Day Book may not be a book at all in the older use of the word. Further, the transactions forming the subject of the entries need not be the actual delivery of tangible goods. A professional man sells services, not goods, and his Day Book—which he almost certainly does *not* call by that name—records the details of the services rendered. Then there are special businesses, such as banking, where what is sold is the use of money, the charge for which is called interest; insurance, where protection from some risk is given in return for a premium; estate owning, where the use of property is sold in return for rent, and many others. But it is the substance, not the form, which is important in dealing with a principle, and the point to bear in mind is that in all businesses which sell on credit, whether this sale be of goods or services, there is some record kept of the delivery of these goods or services—a record which is the warrant for making a charge through the Ledger against the person liable to pay. In all that follows the record of sales made on credit, however it may be kept, is called the "Day Book."

Even as the Day Book records *sales* made on credit, so the Invoice Book records *purchases* made on credit. The Invoice Book has also many names, such as the "Purchase Day Book" or "Purchase Journal," and it has likewise many forms. Indeed, it has more variations than the Day Book. In every business a Day Book—a record of credit sales—is of prime necessity to the very existence of the business. It is no desire for accuracy, or economy, or system, which makes a man record his sales—it is a case of "no Day Book, no business." But an Invoice Book is not in the same position. Anyone buying largely on credit would be foolish not to keep one; but not to keep one, or to keep it imperfectly, though likely to be expensive, is not fatal, for the transaction which should be the subject of the buyer's Invoice Book has already been the subject of the seller's Day Book, and if the buyer is not certain of what he owes, the seller may be trusted to tell him. Hence the Invoice Book, not being the product of stern necessity, has more elasticity about it, and is sometimes used for purposes over and above its primary one. But for the present purpose the Invoice Book means the book or books, or other material, used to record the credit purchases.

The book known as the Cash Book is seldom described by any other name. Like the Day Book and the Invoice Book, it may have many divisions. Thus, in large businesses, the point is quickly reached at which it is necessary to have one book or set of books for cash received and another for cash paid. The Cash Book will be described more fully at a later stage (p. 30) for it has a peculiar place in the double-entry system—it is sufficient at this point to understand that by the term "Cash Book" is meant the book or books which contain the record of all cash received and paid, whether in coin or through the bank.

These three books—Day Book, Invoice Book, and Cash Book—in their various forms are capable of dealing with nearly all the transactions of most businesses. But not with quite all; there still remain transactions—generally few in number, but often very important—for which they are not suited. If there are a considerable number of these transactions which are similar in character, a special book with an appropriate name will probably be kept for them. But these may be, and all other transactions are, entered in a book called the Journal—a book which is but a shadow of its former self, though it still retains its power of recording any kind of transaction whatsoever. It is the Journal which is the beginning of double-entry, and to know how to use it is to know the art of bookkeeping.

Before, however, dealing with the Journal, it is necessary to explain that the Ledger, like the chronological books, may be, and generally is, divided into several parts. It is common to have a Ledger reserved for customers' accounts, called the Sold Ledger; and this, again, may be divided into several volumes on one of many principles—*e.g.*, alphabetically, or by countries, or by districts covered by particular travellers. It is also usual to have a Bought Ledger in which are the accounts of "furnishers"—*i.e.*, those firms who supply goods to the business. Then there is usually a Nominal Ledger, which will be dealt with later; and this, again, is often subdivided, a part of the information which would otherwise be kept in it being kept in a Ledger which is under lock and key and is called the Private Ledger. Possibly the Ledger, or part of it, may be a series of cards kept in a box. But all these divisions are for practical convenience only—there is no fundamental principle involved in them.

If a business is a simple one, and there is, during any given period, an absence of any transactions other than those which are normal and regular, it is very easy to learn mechanically the actions required to balance the books at any time. But such a slender knowledge does not avail to deal with those exceptional cases which are all but certain to arise; nor is it likely that this slender stock of knowledge will prove to be useful outside of the business in which it was acquired. But once get hold of a principle, not as a formula but as a living truth, and this can be applied in any circumstances.

CHAPTER III.

THE PRINCIPLE OF THE JOURNAL ENTRY.

THE principle of Double Entry is admirably summed up in its name, for it implies a double record of each business transaction in a chronological record called the "Journal," the entries in which are posted to the Ledger. The Ledger now, as always, is the recipient of all the entries in the chronological books and of nothing else, and in that sense time has not touched it; the difference is in the books in which those primary entries are made.

The double-entry of our forefathers knew but one chronological book, the Journal. This one book took the place of all the specialised books which are now employed, and in it was entered every transaction, of whatever nature, exactly as it occurred. The Journal, therefore, for any given day showed every transaction which had occurred during that day. Every payment or receipt of cash, every movement of goods inwards or outwards, was made the subject of an entry containing both a debit and a credit, and in this form was duly recorded in the Journal. Probably this practice was never carried out in its entirety in a large business, but it is only by conceiving of it as being carried out that the principle can be thoroughly grasped.

It is a fact, and an obvious one, that a business transaction has two sides—one as it affects the particular trader whose books are the subject of consideration at the moment, and the other as it affects the person he is dealing with. (Exceptions, or apparent exceptions, may be found by the inquiring, but that does not affect the general truth of the statement or its practical utility.) Suppose A. to sell goods to X. on credit. To the extent of this sale (call it £5) A. becomes the creditor of X., while X. becomes the debtor of A. These are facts, quite irrespective of whatever entries may or may not be made in the books either of A. or X. As A. has parted with goods and has at the moment received nothing in return (being content with the fact of the indebtedness of X.), common prudence causes him to keep some written record of the transaction. However simple the entry may be, it is a putting in writing of what, if A. put it in words, he would, in effect, express thus—

"X. is my debtor for £5" (adding, doubtless, particulars as to the goods which made up the £5).

But exactly the same idea could be expressed thus—

"I am a creditor of X. for £5."

Double-entry, through the medium of the Journal, expresses both ideas. It assumes that these transactions shall be posted twice in A.'s Ledger—once to the debit of X., and once to the credit of A.; though, in practice, as will be explained later, the latter account is never called A. simply, but is called "Goods Account" or "Sales Account," or some such name. But, whatever the name, the account is really A. in some guise

For the purpose of his books, X. on his part would, if he recorded the transaction, give expression to this idea—

"A. is my creditor for £5,"

but he could also put it this way—

"I am A.'s debtor for £5."

And if he kept his books in the double-entry of our forefathers he would give effect to both of these ways of putting it, by crediting A.'s account in his Ledger, and by debiting himself, only he would not call the account which he debited by his own name, but would probably call it "Goods Account," or, perhaps, "Purchases Account."

Turning to A.'s books again, the actual wording employed in recording the transaction might be thus:—

X., *Dr.* to Goods Account £5 0 0

(with, of course, date and details), and this amount could be posted twice—once to the debit of X., and again to the credit of Goods Account. But, as a matter of practical convenience, it was found better to have two columns—one for the debit and one for the credit, and to make the entry thus:—

X.	*Dr.*	£5 0 0	
To Goods Account	*Cr.*	...	£5 0 0

The precise form and wording, and the position of the cash columns in relation to the wording and to each other, are all matters of detail. Clearness and a separation of debits from credits are the essentials.

A little reflection will show that this principle can be applied to every transaction. Obviously the purchase of goods can be similarly treated, the entries being the reverse of those necessary in the case of a sale. So with cash. Suppose X. pays the £5 he owes A., the receipt by A. of this sum makes X. a creditor for this sum, and therefore makes A. his debtor. It should be noted with reference to the statement that X. thus becomes a creditor for £5 (and it is an excellent thing to note in all bookkeeping affairs), that it is well to deal with one thing at a time. Many persons hastily reading the statement would say that X. did not become a creditor by paying £5, for he was already a debtor for that sum, and that the payment only cleared his indebtedness. But the whole transaction from A.'s point of view—the selling of goods of the value of £5 to X. and getting paid for them—is really made up of two transactions, one of which made X. a debtor for £5, while the other made him a creditor for £5. These two transactions being placed against each other cancel each other, but in reality they are quite distinct.

The Journal entry of the transaction would therefore be:—

Cash ...	...	...	*Dr.*	£5 0 0	
To X.	...	...	*Cr.*	...	£5 0 0

adding the date and any particulars that might be desired.

The possibility of journalising various kinds of transactions is shown more fully in the next chapter.

CHAPTER IV.

THE APPLICATION OF THE JOURNAL ENTRY TO A SERIES OF TRANSACTIONS.

It is common in bookkeeping examination papers to meet with questions, which take the form of a narration of a number of transactions, described in colloquial language. Such a question, setting forth the dealings of one William Jones, is here taken as an illustration of the way in which the Journal *may* be applied to record any transaction. It is not to be supposed that the Journal *ought* to be so applied; the illustration is given, as is explained more fully in the next chapter, solely to show the connection between modern bookkeeping and that journalisation which lies at its root. The candidates are asked to enter these transactions in the necessary books, and if they did what the examiner wanted them to do, they would open a Day Book in which they would enter all the sales; an Invoice Book in which they would enter all the purchases; and a Cash Book, with three columns, which would show cash transactions, bank transactions, and discount. The Day Book and the Invoice Book they would post in detail to the Personal Accounts in the Ledger, and the totals would be posted to a Sales Account and Purchases Account respectively. The Cash Book would be posted in detail to the Ledger.

While it is a convenience to have three chronological books running simultaneously, as in the above instance, it is not a necessity. The above transactions could with propriety be put through a Journal, and in the olden days would, in fact, have been entered in a Journal and not in the specialised books now commonly used.

Here are the transactions as given in the examination paper (in italics), and below each transaction is given the Journal entry applicable to it :—

TRANSACTIONS JOURNALISED IN FULL.

1910			£	£
Jan. 1.	*Commenced business with Cash Capital £2,500.*			
	Cashier	Dr.	2,500	
	To Wm. Jones, Capital Account ..	..		2,500
Jan. 1.	*Paid to Bank, £2,350.*			
	Bank	Dr.	2,350	
	To Cashier	..		2,350
Jan. 3.	*Bought Goods from James Harrison & Co., £540.*			
	Wm. Jones, Purchases Account ..	Dr.	540	
	To James Harrison & Co.	..		540
Jan. 3.	*Sold Goods to William Adams, £480.*			
	Wm. Adams	Dr.	480	
	To Wm. Jones, Sales Account ..	..		480
Jan. 7.	*Bought Goods from W. Smith & Co., £645.*			
	Wm. Jones, Purchases Account ..	Dr.	645	
	To W. Smith & Co.	..		645
Jan. 8.	*Paid Wages in Cash, £8.*			
	Wm. Jones, Wages Account	Dr.	8	
	To Cashier	..		8
Jan. 8	*Sold Goods to H. Allan & Co., £535.*			
	H. Allan & Co.	Dr.	535	
	To Wm. Jones, Sales Account ..	..		535
Jan. 10.	*Received Cheque from Wm. Adams (discount £12). £468.*			
	Cashier	Dr.	468	
	Wm. Jones, Discount Account ..	Dr.	12	
	To Wm. Adams	..		480

TRANSACTIONS JOURNALISED IN FULL (*continued.*)

1910			£	£
Jan. 10.	*Paid to Bank, £468.*			
	Bank	Dr.	468	
	To Cashier			468
Jan. 11.	*Paid to James Harrison & Co. by Cheque (discount £27). £513.*			
	James Harrison & Co.	Dr.	540	
	To Bank			513
	To Wm. Jones, Discount Account			27
Jan. 12.	*Paid ¼ year's Rent to 31st March 1910, in cash, £40.*			
	Wm. Jones, Rent Account	Dr.	40	
	To Cashier			40
Jan. 13.	*Bought Goods from H. Kershaw, £740.*			
	Wm. Jones, Purchases Account ..	Dr.	740	
	To H. Kershaw			740
Jan. 15.	*Paid Wages in Cash, £8.*			
	Paid Office Expenses in Cash, £7.			
	Wm. Jones, Wages Account	Dr.	8	
	Wm. Jones, Office Expenses Account	Dr.	7	
	To Cashier			15
Jan. 17.	*Sold Goods to H. Hobson, £320.*			
	H. Hobson	Dr.	320	
	To Wm. Jones, Sales Account			320
Jan. 19.	*Sold Goods to William Adams, £160.*			
	William Adams	Dr.	160	
	To Wm. Jones, Sales Account			160
Jan. 21.	*Sold Goods to H. Allan & Co., £250.*			
	H. Allan & Co.	Dr.	250	
	To Wm. Jones, Sales Account			250
Jan. 22.	*Paid Wages in Cash, £8.*			
	Paid Office Expenses in Cash, £5.			
	Wm. Jones, Wages Account	Dr.	8	
	Wm. Jones, Office Expenses Account	Dr.	5	
	To Cashier			13
Jan. 25.	*Paid W. Smith & Co., by Cheque (discount £32). £613.*			
	W. Smith & Co.	Dr.	645	
	To Bank			613
	To Wm. Jones, Discount Account ..			32
Jan. 26.	*Received Cheque from H. Allan & Co. (discount £15). £520.*			
	Cashier	Dr.	520	
	Wm. Jones, Discount Account ..	Dr.	15	
	To H. Allan & Co.			535
Jan. 26.	*Paid to Bank, £520.*			
	Bank	Dr.	520	
	To Cashier			520
Jan. 29.	*Paid Wages in Cash, £8.*			
	Paid Office Expenses, £4.			
	Wm. Jones, Wages Account	Dr.	8	
	Wm. Jones, Office Expenses Account	Dr.	4	
	To Cashier			12
			£11,796	£11,796

As has been explained, and as will be seen from this illustration, every Journal entry must have at least two parts, one being the name of the account to be debited, the other the name of the account to be credited, and often a third may be necessary to give some account of the nature of the transaction. This part is called the "narration," and in practice some of the above entries would require to be amplified by such a narration. Thus the entries referring to the sale of goods require to be amplified by appending the details of the sales, as is done in an ordinary Day Book.

It will be noticed that each transaction is made the subject of a double entry, and it is easy to see that, if these entries are correctly posted to the Ledger, the result is bound to be that the aggregate of the total postings to the Ledger, as ascertained by extraction, is on each side £11,796. If, therefore, every transaction in a business be journalised in this fashion, the material for an automatic check on the correctness of the books is at hand. (Note that the modern fashion is to extract Ledger *balances*, not totals, as being quicker, but the old way was first to extract totals, and from these totals to deduce the balances.)

The value of the check thus afforded is subject to at least two qualifications. First, two mistakes or two groups of mistakes of the same amount, but operating in opposite ways, would, if they occurred on the same side of the books, escape detection.

Thus, suppose that one of the postings to the debit of a customer was £10 too little, and that in adding up another account, say Purchases Account, to ascertain the total which had gone to the debit of it, a mistake were made in the addition which resulted in the amount being put down as £10 too much, the extractions of the debit postings as a whole would still amount to £11,796, and the books would be passed as correct. Probably, however, at least one of the mistakes would be stumbled upon in the course of time, rendering necessary a search for the other, but, in the meantime, the customer's account might have been rendered for the wrong amount and paid. This kind of mistake may appear fanciful. It is not common, but it is not so rare as a mathematician would predicate of it, because some mistakes—notably one of 10s. in an addition—are often made, and, when made, are as likely to be made in one direction as another.

The other respect in which the check falls short of perfection is that it is a check in the lump only, not in detail. It shows that the postings have been made to the right *side* but not necessarily to the right *account*. Goods sold to A. may be debited to B., and the totals as extracted will still be correct.

These two weaknesses—two or more mistakes exactly balancing, and postings to wrong accounts —are not to be charged as special weaknesses of double-entry. They are inherent in all systems as at present worked, though there are ways of minimising the danger of them. But it cannot be too clearly understood that the introduction of a system is one thing, and the working of it another. The best of systems breaks down when carelessly worked. A counting-house is not saved by the adoption of a good system of bookkeeping alone. There must be system in all that leads up to the entries to be made in the books, and (what is much more difficult) this system must be carefully and intelligently worked.

Turning now to the specimen Journal entries as given above, there are two peculiarities in these particular entries which would not occur in practice, even though they were being put through the Journal. The first of these peculiarities is that, where the word "cash" is commonly employed, the word "cashier" has been used. It gives a clear idea of the cash transactions if they are thought of as going through the hands of a cashier, who is responsible for, and is therefore debited with, all that he receives, and is entitled to be discharged and credited in respect of all that he pays. There is no difficulty in thinking of a bank as something outside of the trader, and for the purpose of understanding the entries affecting cash, it is well to think of the cashier as occupying a position in relation to a business similar to that occupied by the bank.

The second peculiarity is that, to such accounts as Capital, Sales, Office Expenses, and the like, there is prefixed the name of the trader, William Jones. This is done in order to show clearly that the entry in which it occurs is a purely technical one, made only for the purpose of obtaining a contra to the transaction as it affects the outsider. It is always desirable that books should be kept in such a way that their technical accuracy can be demonstrated, and this (as mentioned above) was achieved in double-entry bookkeeping as originally practised by doing that which, in effect, duplicated the entries in the books. Thus, in the case of a sale, a customer was debited, which is obviously necessary and correct, and some other nominal or fictitious account was credited. But if a nominal entry is to be raised against every real one, it is easy so to divide the nominal entries into classes as to make them afford at any time some information as to the progress of the business. The nominal accounts are therefore split up into such headings as may be found convenient, such as Purchases, Sales, Wages, and the like. Thus, the first Journal entry records the fact that Wm. Jones brought into the business a capital of £2,500, which is handed to his cashier. The cashier is therefore a debtor for this sum and Wm. Jones a creditor. It is, however, convenient to show that this amount differs from those passing through other nominal accounts by being in respect of capital, and this is done by crediting an account called "William Jones, *Capital Account.*" In ordinary practice one would not use the proper name, but would describe the account simply as "Capital Account." Following the Journal entries it will be seen that, according to the fourth one, Jones sells goods to the value of £480 to Wm Adams. Wm. Adams is undoubtedly a debtor, and Wm. Jones thereby becomes a creditor. He is, as a matter of bookkeeping, a creditor for this £480, exactly in the way in which he is a creditor for £2,500 in respect of the capital he brought in. But the credits arise out of transactions of a different nature, and therefore an account is raised called "Wm. Jones, *Sales Account*," which is the account which is for the moment credited with the amount of the sales. Purchases are treated in the same way as sales, except that the transaction is of the opposite nature. It will be shown later (page 80) that all these nominal accounts ultimately find their way into and are part of the Capital Account, and that they are only kept separate till stock-taking for the purpose of analysis. This division of accounts is dealt with more fully in Chap. IX.

CHAPTER V.

SOME DISADVANTAGES OF THE OLD STYLE OF DOUBLE-ENTRY—HOW IT HAS BEEN SIMPLIFIED.

THE fault of the system of complete journalisation is that it is too cumbrous, as anyone who reads the Journal entries in the preceding chapter can see for himself. Even if such a reader knew nothing of bookkeeping, he could not fail to form the impression that there was a great deal of repetition, and that a competent person ought to be able to produce an equally good result with less expenditure of energy. Whatever our forefathers may have been capable of doing, it would not now be possible for any ordinarily intelligent bookkeeper to pass all his transactions of every description through a Journal without its occurring to him very quickly that most of the entries fell into a few well-defined classes. Thus, to take the case of the sales, there would be numerous entries, all exactly similar in character, with which the customer was debited and Sales Account credited, for the entries on the credit side of the Sales Account in the Ledger would be of precisely the same number as the entries to the debit of the individual customers' accounts. Any thoughtful bookkeeper would, therefore, very quickly devise a special book to contain sales alone. He would see at once that, if he had such a special Journal for sales, there was no object in crediting Sales Account in the Ledger with the amount of each individual sale, but that the object could be perfectly well achieved by omitting the credit entry, and by posting the total of the Sales Journal at each stocktaking period in one sum to the credit of a Sales Account. If there were a thousand sales, the method of treating them by formal Journal entries would involve two thousand entries of the amount of each sale, all of which would require to be posted; whereas the method of treating them in a separate Sales Journal involves only a thousand and one entries. In this way there came into existence the modern Day Book, which is the portion dealing with sales, of the old-fashioned Journal. So far as the labour involved in the bookkeeping is concerned, the change from Journal entries to Day Book is a change from double-entry to single-entry, or rather from fourfold-entry to double-entry, plus only the trifling additional labour of posting the total to the credit of the Sales Account.

Except in a few instances, the practice of putting sales through the Journal is now entirely at an end, but occasionally one may find a trace of the old practice lingering in the custom which some firms have of making a Journal entry of the total of their sales. Thus, suppose the total of the

Day Book to come to £10,000, the simplest way to deal with this amount is to post it direct to the credit of the Sales Account in the Private Ledger, or whatever Ledger the Sales Account is kept in; but one may still find firms who, instead of doing this, make Journal entries in some such form as this:—

Sundry persons	*Dr.*	£10,000	
To Sales Account			£10,000
For Sales for year ending 31st December 1910.			

The debit is not posted because it has already been posted in individual items through the Day Book, but the credit is posted to the Sales Account. This practice of bringing all totals into the Journal, and posting them from there to the Ledger, is common on the Continent.

There is a class of transaction met with in every business which is not shown in the specimen entries in Chapter IV.—the class known as "Returns." Everyone who sells goods finds that from time to time some of them are returned. Looked at from the other side, everyone who *buys* goods occasionally returns some of them. If a trader sell goods which are duly charged to the customer but are ultimately returned, this return, which is a cancellation of the sale, must be provided for. How this is recorded is a matter for each business to decide for itself, but it can be done, and is probably best done, by keeping the record of returned sales quite apart from the sales, either in a separate book or in a separate portion of the Day Book. As sales are posted to a customer's debit, returned sales go to his credit, and the total of them goes to the *debit* of a Sales Account.

The net result would be the same if these returned sales were treated as purchases, which in a sense they are. But, for statistical reasons, if not for bookkeeping ones, it is well for every business to know its net sales for any given period, and this could not be done if goods sold and then returned were mixed up with the purchases.

All that has been said above as to sales, Day Books, and returned sales, applies also to purchases, Invoice Books, and returned purchases.

Not only was the system of complete journalisation very cumbrous, involving as has been shown, nearly double the necessary work in respect of purchases and sales, but it had another disadvantage fatal to its adoption in a concern of any size. This lay in the fact that there was only one book in which to record all the transactions, and it can easily be seen that it was seldom convenient, and often impossible, to arrange that this book should lie where the transactions actually took place. Doubtless this difficulty was overcome in practice by keeping Draft or Waste Books, which formed the raw material for the Journal entry. But such a system is bad, for it involves double work and needless risk of error in the process of copying. It is spoken of in the present tense, for in some form it still exists, and, indeed, is to be met with fairly frequently. It is, for instance, a common thing for a firm to keep an Order Book as well as a Day Book, and often the keeping of these two books is a necessity. But there are many cases where the Day Book is so nearly a repetition of the Order Book that by a slight modification one book will serve both for Order Book and Day Book, thus lessening both trouble and risk of error. Similarly (though this does not strictly concern a system of bookkeeping) a carbon copy of the entry as it is made in the Day Book can be utilised as the invoice to be despatched to the customer.

In a business of a simple character, where every entry was originally journalised, the elimination from the Journal of the entries relating to purchases and sales left very little in the Journal, except entries relating to cash. If, instead of these cash entries in the Journal, a Cash Book were employed, it might be thought that the cash was being treated in the same way as the purchases and sales had been. But this is not so; there is a difference which it is well to understand. In the old system there was, of necessity, a very long account in the Ledger, called the "Cash Account,' or, as it is called in the illustrations given in Chapter IV., "Cashier." This account was, in fact, the Cash Book, for it contained a complete record of all receipts and payments. It seems to have occurred to some ingenious soul that, if that part of the Ledger which contained the Cash Account were to be bound separately from the rest of the Ledger, the Journal entry relating to the cash might safely be, not shortened, but entirely dispensed with, and that any entries relating to cash might then be made direct in the Cash Account portion of the Ledger, the corresponding entry on the other side in the other portion of the Ledger being made when convenient. Though, as a matter of course, the Cash Book is treated as a chronological book in the same way as a Day Book and an Invoice Book are treated, yet it must have struck all bookkeepers at times that in some respects it differs from these books. It has something which smacks strongly of a Ledger Account, and, in fact, in balancing the books as a whole, the cash balance must be brought into account. This is because, strictly speaking, it *is* a Ledger Account. In order that the books may balance, any entry made on the debit side of the Cash Book must in due course find its way to the credit side of the Ledger, and *vice versâ*, and the balance, as mentioned above, must be brought into account, being a true Ledger balance. When, therefore, a bookkeeper is making an entry in the Cash Book, what he is really doing is to make a one-sided entry in the Ledger, and when he posts that entry he is making a direct transfer from one Ledger Account to another. Both of these things—making a one-sided entry, and making a direct Ledger transfer—are cardinal sins in bookkeeping, but in the case of the Cash Account (*i.e.*, the Cash Book) it is a universally recognised and highly convenient practice, which has many advantages and no disadvantages.

The making of Journal entries in respect of cash receipts and payments has gone, and the Cash Book is now universal. Strictly speaking, the making of payments by cheque has no connection with the cash. The cashier is concerned with the amounts which have come into his hands, including those which he disposes of by payment into the bank, and he is also concerned with the cash which he withdraws from the bank, but technically he is not concerned with the payment made to a furnisher by cheque. But until not so many years ago the practice was almost universal, where a furnisher was paid by cheque, of entering the cheque as a receipt of cash from the bank, and then entering it on the opposite side as a payment to the furnisher. In this way all the transactions affecting the bank found a place in the Cash Book, and when they were posted to the Bank Account in the Ledger that account constituted a complete record of the bank transactions. But again it occurred to someone that, if an additional column were placed in the Cash Book, the bank transactions could be entered direct into this column, which would have the effect of doing for the bank transactions what had already been done for the cash transactions. In all well-kept books of businesses of any size there are now separate columns in the Cash Book for the cash and bank respectively, and therefore the Cash Book is, strictly speaking, made up of two Ledger Accounts—the Cash Account and the Bank Account, and both balances must be taken into account as Ledger balances at stocktaking.

There is no reason why the system of separate columns for cash and bank transactions should be limited to only one column for the bank. There may be as many columns as there are Bank Accounts, of which a business frequently has several. Also as many businesses are too large to be worked with only one Cash Book, transactions which in smaller businesses would be entered in separate columns would in such concerns be entered in separate books.

Just as some businesses are too large for the cash transactions to be recorded in a Cash Book with columnar divisions, so are some too small. The old system of entering a payment by cheque as a receipt from the bank, and posting it to the credit of the Ledger Account kept for the bank is obviously cumbrous, but it is extremely simple and is very easy to explain. In spite, therefore, of its cumbrousness, it may be the best system for a small business where the bookkeeping is a side issue done by some clerk not specially skilled in the art.

Such a method of using the Cash Book is in effect to use it as a form of Journal (though the postings are made from debit to credit), and, indeed, it is not infrequent to find that the Cash Book is thus used to journalise items which have little or no reference to either cash or bank transactions.

Few businesses are without the book which goes by the name of the "Petty Cash Book." It may, or may not, be a book to be reckoned with for the purpose of balancing. It is dealt with specially in Chapter XIV.

To complete the tale of the Cash Book, one other portion of it must be mentioned—the discount column. It is obvious that, if the cash is going to be entered in a Cash Book, it is a waste of time to make separate Journal entries for the various discounts allowed to and by the business, (though there are firms who still do this), and therefore there is a column in the modern Cash Book on either side, in which is entered the discount appertaining to each cash transaction. While, however, the cash and bank entries in the Cash Book are, strictly speaking, one-sided Ledger entries, the Cash Book, in so far as it records discounts, is a true Journal, and the totals of the discounts must be posted to the Ledger in the way which is done with the totals of the sales and purchases.

The fact that there are still to be found firms who make entries for their discounts in their Journal instead of utilising a column in the Cash Book, is only one instance out of many which show how hardly the old system of complete journalisation dies. Unless a system has been thoroughly revised and brought up to date it will often be found to contain some relic of the old days when time was of less value than is now the case.

CHAPTER VI.

THE PLACE OF THE JOURNAL IN MODERN BOOKKEEPING.

Applied to the particular transactions set out in Journal form in Chapter IV., the introduction of a Day Book, Invoice Book, and Cash Book would provide a place for every transaction, and leave nothing for the Journal. What, then, is the place of the Journal in modern books?

Before discussing this question, it is perhaps desirable for something to be said in favour of the old method of double-entry, as in the last chapter a good deal has been said against it. But the objections have been to it as a practice, not as a principle Whatever short cuts a bookkeeper may find it well to adopt, he must base them all on the fundamental principle that for each debit he must have a credit, and *vice versa*. The debit need not be immediately followed by the corresponding credit, but sooner or later, in one form or another, the credit must be made in order to arrive at a balance. If it is desired to take the Sales out of the Journal and to keep a Day Book for them—which is, of course, the right thing to do—the posting of the sales to the debit of customers is, taking the operation by itself, a one-sided thing to do, and the necessity of making the other side of the entry must be borne in mind, *i.e.*, the books are not complete as regards sales till an amount equal to the aggregate of the sums which have gone to the debit of Personal Accounts has gone to the credit of Sales Account.

Put in another way, the value of a grasp of double-entry in its fullest form lies in the ability thereby given to resolve any transaction whatsoever into its component parts of debtor and creditor. Let the student of bookkeeping once grasp the fact that there is no transaction which cannot be recorded in the form of a Journal entry, and he will soon find out for himself the transactions which need to be so recorded, and those for which an abbreviated form may be employed. But till he grasps the fact he is as a navigator without a compass.

Turning now to the place of the Journal in modern books, it may be said, broadly speaking, that where there are a great many transactions of a similar nature it will be found convenient not to pass these through the Journal, but to have a separate book for them. The method of dealing with bills is a case in point. Where the giving of bills is a regular feature of the business, there is generally a Bills Payable Book, the amount of each bill being posted to the debit of the firm to whom it is given, and the amounts being again posted, either individually or in periodical totals, to the credit of a Bills Payable Account in the Ledger. But where the giving of a bill is a rare occurrence, there may be no Bill Book, or it may be used as a memorandum only, and in that case the technical entry may very properly be made through the Journal—" A.B. *Dr.* to Bills Payable." Sometimes it will be found that the Bill Book has a column for cash paid, as well as one for the amount of each bill as given. In such a case the Bill Book becomes one of the Ledgers, and the balance must be extracted for the purpose of balancing, the amount of the balance being what the balance of the Bills Payable Account in the Ledger would have been had one been kept.

This method of dealing with bills may at first sight appear rather confusing, especially where they are renewed, but all difficulties disappear once the principle is firmly grasped that every transaction, however complicated, is capable of being resolved into one or more Journal entries, and that every record, to be correct, must be a Journal entry or an abbreviation of one. Thus, take the case of a firm who have given a bill for £500, which falls due on March 4th. They arrange for its renewal for three months, and agree that the new bill should include, say, £6 10s. for interest and stamp, so that it is for £506 10s. There are here three distinct transactions, which, if entered in full, would involve three Journal entries. Though they may, in fact, be entered differently, yet the entries can only be an abbreviation of the Journal entries—the *principle* of the Journal entry must be there. The first transaction is the cancellation of the old bill. The original transaction debited the creditor, and credited Bills Payable Account. The entry on the return of the bill is the opposite —"Bills payable, *Dr.* to A. B., £500." This leaves matters as they were before the bill was drawn. The next entry is "Interest" (or some expense account)—"*Dr.* to A.B., £6 10s.," this being the interest to be paid for the renewal. There is, then (on March 4th), £506 10s. at the credit of A.B., and, this being the amount of the new bill given, the final entry is, "A.B., *Dr* to Bills Payable, £506 10s.," If the bill is duly met on June 7th, the cash paid to meet it goes to the debit of Bills Payable Account, and the transaction is at an end.

The procedure as to Bills Receivable is on the same lines, with the difference (which sometimes introduces a complication) that, whereas bills payable are seldom paid till they are due, the cash for a bill receivable may be, and often is, received on the day the bill is received, irrespective of when it is due. This is because the bill is discounted—of course, at some cost, which is properly a payment for interest (of the same nature as interest on a bank overdraft), but is sometimes entered in the Cash Book as though it were a discount allowed to the person from whom the bill was received.

Another class of transaction, which it may, or may not, be convenient to enter in the Journal, is that of Commissions. If a firm is acting as agent for a number of concerns, it will generally be found convenient to have a special book in which to enter the commissions, but an occasional commission may very well go through the Journal. Many firms use their Day Book and Invoice Book to pass through any debit or credit which does not represent actual cash passing. This brings about the correct result, but the system may easily be so employed as to cover up a transaction when it is very desirable that it should be plainly shown.

Still another class of transaction which either may, or may not, be found in the Journal, is that which deals with Consignments. Some firms occasionally make consignments; others make them regularly as a matter of course. Like every other class of transaction, they may be put through the Journal, but it may be more convenient to have a special book for them, and this book may be, and sometimes is, so arranged as to perform a number of functions at one operation. But all these operations, however many there may be, are only so many contracted Journal entries. In such a case, as in all others which present any difficulty, the procedure, in order to verify the soundness of the principles upon which the entries are made, is to resolve the whole of the transaction into its component parts, and to see whether the record, as a whole, produces in some form the result which would have been produced had these component parts each been made the subject of a Journal entry.

When the process of devoting a separate book to each class of transaction which occurs frequently, has been carried to its fullest extent, there still remain certain transactions which, unless they are made by direct transfer from one account to another in the Ledger, must go through the Journal. It is, for instance, not infrequent for a firm both to buy from, and sell to, one person. Neither is it infrequent in such a case to have two accounts—one dealing with the purchases and the other dealing with the sales. If the balance only is paid on the settlement, the person dealt with is debited with the cash paid to him in the account kept for him in the Bought Ledger. It is, however, necessary to bring into the debit of this account the amount standing to his debit in the Sold Ledger, and this is done by transfer from the one account to another. Such a transfer is a proper subject for a Journal entry. The entries by which, at stocktaking, the nominal accounts are transferred to the Profit and Loss Account cannot well be made in any of the books in ordinary use, and they may therefore be properly made through the medium of the Journal.

To put it shortly, it is not now possible to say off-hand what entries in any business are, or should be, made through the Journal. All one can say is that there goes through the Journal a record of all those matters affecting Ledger Accounts for which a special book is not provided.

It will be seen that the Journal as now employed is but a shadow of its former self. In every ordinary business by far the greater number of transactions (perhaps 99 per cent.) which could form the subject of Journal entries are now made in the Cash Book, Day Book, and the like. As regards the number of transactions, therefore, the Journal is usually a small affair. But although the entries are few, they are, or may be, very important in character. All the entries going through any one of the specialised books—*e.g.*, the Day Book—are presumably of one character. But the modern Journal in the nature of things deals with selected transactions—with just those transactions which are not alike, and have no general principle in common, except their ability to be expressed both as debits and credits. Thus a Journal entry, which on its technical side is a mere debit and credit posting, may be found to be the record of some very important transaction somewhat out of the ordinary course.

The modern Journal being at best a small book in relation to the other books, (for if it is a large one, that only shows that specialisation has not been carried far enough, and that there is more in the book than there need be) there will often be found cases where there is no Journal at all. In a business of a simple nature almost the only Ledger entries not provided for by the ordinary everyday books are those necessary to close the books when stock is taken and a balance struck. But these are just the entries which it may not be convenient to record in a book which is necessarily more or less open to the inspection of anyone in the counting-house. They are, therefore, often made by direct transfer in the Ledger from one account to another. Like all other departures from the rigour of double-entry, this is quite permissible so long as the person making the entries realises exactly what he is doing, for it should always be remembered that books exist for the benefit of the business, and for that purpose only.

From all that has been said above it will be gathered that double-entry, in the sense of entering twice, is, for all practical purposes, a thing of the past. It is often said of accountants that they make additional work for a bookkeeper, and that is sometimes true. But it is also true that the additional work does not arise to any appreciable extent from there being additional entries to make. It arises from the fact that once the books are on a (so-called) double-entry basis, the bookkeeper is called upon to balance them periodically (a thing which he has probably never previously done), and therefore errors have to be looked for which, in the easy-going days before the system was introduced, would have passed unchallenged. This, of course, makes more work than was formerly the case, but not more work than ought to have been the case.

The point may again be emphasised that the principle of double-entry bookkeeping is not only that of double-entry (whether in detail or in the contracted form which has been discussed), but also lies in the complete separation of the Journal from the Ledger. (The word "Journal" here is used to signify not only the Journal proper, but also all those books which contain the chronological record, as opposed to the analytical.) Every entry, of whatever nature, must first of all find a place in the chronological books. The Ledger, therefore, is in no case a book of original entry—it should contain nothing which is not to be found in the chronological books. Put in this way, the principle appears both intelligible and simple, and good bookkeeping on the technical side lies, to a very great extent, in carrying out the principle rigidly.

CHAPTER VII.

SUMMARY OF THE PRECEDING CHAPTERS.

It is, perhaps, desirable at this point to summarise shortly the argument running through the preceding chapters.

The original double-entry at the point of time —which is probably an imaginary one—at which it had been perfected theoretically, but had not been submitted to the practical abbreviations which are now all but universally employed, recognised that it was both possible and desirable to conceive of every transaction as affecting the trader himself as well as the person he was dealing with. It recognised also that this conception of a dual interest was capable of being recorded in writing through the medium of the Journal entry. It further recognised that the first thing to do in the endeavour to obtain completeness in bookkeeping was to record chronologically in the Journal, in the dual form of a debit and a credit, every transaction exactly as it occurred. Further, that if all these entries were posted into the Ledger, and if the Ledger contained nothing but these entries, it was certain that a balance could be obtained, and ought to be obtained.

The two distinguishing features may be stated thus:—

(*a*) The double entry (in the Journal).

(*b*) The keeping of a Journal and of a Ledger, each distinct from the other, but each complementary to the other.

It will be observed that there are really two double entries—*i.e.*, each transaction is entered four times. The two-sided record in the Journal is an obvious double entry, but to post everything into the Ledger is to make another double entry, thus making four entries in all.

The old style of double-entry recognised more than is mentioned above—it recognised that the portion of the Journal entry which affected the trader himself could be so arranged as to provide not merely a technical check, but also valuable statistical information. This is dealt with in Chapter IX.; up to this point bookkeeping has been considered only as a means of ensuring from day to day a technical accuracy capable of demonstration.

The only fault of the old style of double-entry is that it is too long. Theoretically it is perfect; it has the completeness of a mathematical proposition. When a man takes stock he wants to know the answer to two questions: "How do I stand?" and "How have I arrived at this position?" The answer to the first question is to be found in the

Balance Sheet, and to the second in the Profit and Loss Account. The aggregate of that portion of each Journal entry which affects the individuals whom the trader is doing business with, is the Balance Sheet; while the aggregate of that portion of each entry which affects the trader himself, is the Profit and Loss Account. (The latter portion of this statement is subject to certain exceptions, relatively few in number, but as a general proposition it is correct.)

But because each separate transaction *can* be stated from two points of view, it is not, therefore, necessary to do it. The recognition of this is the feature of modern double-entry bookkeeping. It has been shown in Chapter VI. how the original Journal has had taken from it class after class of transactions in order that, by their being kept in specialised books, time might be saved. It has been shown, too, how this has gone on to such an extent that there is little of the Journal left. Double-entry as a theory is as important as ever; but, as a practice, the amount of work involved, relatively to the whole work necessitated by the bookkeeping, is trifling.

But always must the good bookkeeper have in his mind the conception of the Journal entry, and the consequent correspondence of debit with credit. Whatever short cuts he may make, he must come back to the main road sooner or later. More than this, he must, if he would be thoroughly efficient, be able to come back to it at any moment. Whatever specialised books he may be in the habit of keeping, he should be able to record *any* transaction through the Journal instead of through the book he usually employs for the purpose. That it should be necessary to do this is very improbable, but the ability to do it should be there.

CHAPTER VIII.

SOME SPECIAL POSSIBLE ABBREVIATIONS.

In books of quite a simple character, kept on modern lines, there is, as a rule, no difficulty in seeing why they balance—no difficulty, that is, to anyone with a general familiarity with books of account. The Day Book totals go periodically to a Sales Account in the Ledger, the Invoice Book totals to a Purchases Account, and the cash posted to the Ledger from the debit side of the Cash Book patently equals that posted from the credit side, with the exception of the balances (if any) at the beginning and end of the period dealt with. Note here that the frequency with which Day Book (or Invoice Book) totals are posted to the Ledger is a matter of convenience only; no principle is involved. Convenience generally suggests the posting of monthly totals, but the posting may be done weekly, or yearly, or it may be done at the end of each Day Book, or at the end of each page of the Day Book. This matters nothing, so long as the total for the year (or whatever the period may be) finds its way in some form to the Ledger.

At this point it is convenient to state for future brevity that, while the expression "the

Journal" has a special meaning, all the chronological books into which later developments have divided the Journal may be grouped together and described generally as "the Journals." When this term is used in the remainder of this book, it must be taken to mean the chronological books taken as a whole, by whatever names they may be called individually, as opposed to the Ledgers, which are the analytical books.

As a rule, however extensive the operations of a business, and however many specialised books there may be, there is a strict line drawn between the Journals and the Ledgers. Everything is entered twice—once in one or other of the Journals, and again (in the form of a posting) in the Ledgers. But this is not always so. Business operations are so varied that, whatever the general rule may be, there are always concerns which, owing to special circumstances, cannot—or, more generally, need not—follow the usual routine.

Assume, for instance, the case occasionally met with among manufacturing concerns of a business which has a very few customers—say half a dozen—with each of whom a large business is done. Here, instead of putting all the sales through a Day Book in chronological order in the usual way, it will probably be better to have six Day Books—one for each customer—or to have one Day Book which is so divided as to provide a separate portion of the book for each customer. There is no objection to such a proceeding where, as would be the case in the counting-house of such a business, it is necessarily well understood. Directly this division of the Day Book is introduced, the futility of posting it to the Ledger in detail is at once seen—the analysis of the sales among the various customers is, in the very nature of the division adopted, already made. and detailed Ledger postings are mere repetition. It suffices, therefore, if the Day Book totals for each customer are carried to his Ledger Account periodically, say once a month; and as the work of posting these totals periodically is a mere trifle, it may be said that, for all practical purposes, a sale is only entered once, instead of twice as in most books, and four times as in the old style of double-entry.

Instead of entering up the sales in the manner above described, in a Day Book, and posting the totals to the Ledger, the Day Book may itself be called the Ledger and treated as such, cash being posted to the credit of each account as is done in ordinary books. Of course, the totals of the amounts debited to the various customers would also have to go to the credit of a Sales Account.

A combination of the usual method with the abbreviated one just described is quite possible and by no means uncommon. Where there are many customers, of whom one is of special importance in the number of transactions effected with him, it is quite possible to keep a special Day Book for him, of which the totals only go to the Ledger, while the other customers are dealt with in the usual way by Day Book entered up chronologically and posted item by item.

The reason for the Day Book and Invoice Book being quite separate books is that it is unusual for a purchase to be sold exactly in the form in which it is purchased. Often the identity is completely lost, as where so much metal becomes a machine, or so much flour a loaf. In other businesses—as in distributive ones—while the purchases go through no process of manufacture, yet they are sold in quantities which differ from those in which they are purchased. Thus, cloth bought by the piece is sold by the yard. For these reasons it is either quite impossible, or practically so, to earmark a sale against a particular purchase—impossible that is, as a matter of systematic bookkeeping. Therefore, the Invoice Book and Day Book go on their respective ways independently of one another till a stock-taking occurs, when their relation to each other is disclosed. But though this is true of most businesses, it is not true of all—there are some which sell what they buy in the form and volume in which they buy it. Some grain merchants do this, and so do firms which buy in this country against indents received from customers abroad.

In such cases it may be practicable to make one book do both for purchases and sales. The book would, of course, require to give the name both of creditor and debtor, the amount for which the goods were purchased, and that for which they were sold. But the description of the goods is common ground, and such a book, where practicable, has the advantage of showing at a glance that each item bought has been charged to a customer.

The two illustrations given above are intended to show how elastic a system may be if it is devised and worked by someone who is desirous of doing away with all unnecessary work, and has also complete command of the principle at the bottom of bookkeeping Such a person recognises, as every good bookkeeper should recognise, that the books are subservient to the business, and that he is master of the books.

CHAPTER IX.

REAL AND NOMINAL ACCOUNTS.

In the preceding chapters double-entry bookkeeping has been treated mainly as a system designed to afford a check upon the work of the bookkeeper. It has been shown that by this system, either in its old, or in its modern abbreviated form, each transaction is resolved into two parts—one treating it as it affects the outsider dealt with, and the other as it affects the trader himself. But stress has been laid on the former portion of the entry—the portion affecting the outsider—and the latter portion has not been looked at in detail.

The point has, however, been touched upon in Chapter IV, which showed the journalisation of a series of transactions. Most Journal entries, as has been shown (not all), deal with transactions in such a way as to show them on one side as they affect the particular outsider dealt with, and on the other as they affect the trader himself. The two parties may be described as "Outsider" and "Self" respectively. Modern abbreviations have obscured this fact, but have not altered it. In order that the utmost statistical benefit may be got out of the books, it is customary to split up the "Self" portion of the entries into as many portions as there are classes of facts required. Thus, a sale is correctly journalised, technically, by the entry "John Smith *Dr.* to Self £20," just as a purchase may be journalised as "Self *Dr.* to Thomas Brown £50." But it is just as easy to split the "Self" account into portions, one dealing with sales and another with purchases. All this has been shown in Chapter IV, where the name of the trader, "William Jones," precedes that portion of each Journal entry which affects himself. There is no limit to the extent to which this splitting up may be carried; each form of income and expenditure which it is desired to keep separate may have a separate account. No principle is involved and no rule can be laid down, as businesses vary greatly. Thus, for instance, in one concern the expenditure on travelling may be so trifling that it is included with the oddments which go by some such name as "General Expenses," while in another it may be so great as to render a separate account highly necessary. The same may apply to postage, cablegrams, advertising, or any other form of expenditure. On the other side of the Ledger a single account for all sales may suffice for one firm, while another finds it desirable to have a number of accounts dividing the sales according to departments, or on some other principle found to afford useful information.

It is easily seen that in a transaction which might be journalised thus—"John Smith *Dr.* to Sales £20," there is an essential difference in the two Ledger accounts to which these items are posted. The account called "John Smith" is a genuine one—a record of his indebtedness, which the debtor himself would recognise and the law take cognisance of. In short, the entry on the debit side of the Ledger corresponds to a real debtor. But the entry on the credit side does not correspond to a real creditor; there is no person called "Sales" who will come down on the unfortunate trader in whose books the entry is made, insisting on being paid £20. The account is a nominal one, raised for the private purpose of the trader himself. Hence, accounts of the former class are called "real" accounts, while those of the latter class are called "nominal" accounts.

It is sometimes stated that the difference is not between "real" and "nominal" accounts, but between "personal" and "impersonal" accounts. This, however, is not so; for while every "personal" account is a "real" one, not every "impersonal" one is a "nominal" one, for some accounts which, so far as mere words go, are "impersonal" are, in fact, "real."

The distinction between "real" and "nominal" accounts does not depend on the name of the account, but on the fact behind the account. Thus, even as John Smith's account is a real one, because John Smith actually owes £20, so is "Plant" Account a real one, because it represents the value of plant which is actually in existence, as an account so called would normally do. The balance of the Cash Account (or, in modern books, the balance of the Cash Book) is also a real account, because there is the cash balance behind it. The distinction between impersonal accounts which are "real" and those which are "nominal" causes no difficulty in practice. What should be specially noted is that whether or not an account is a real one is a matter of fact and not of terminology.

CHAPTER X.

THE TRIAL BALANCE.

Double-Entry being designed to afford a check on the correctness of the entries, it is an essential part of the system to apply this check. This is done by extracting all the Ledger balances and ascertaining whether the debit balances do in fact agree in total with the credit ones. The list of balances prepared to show this is known technically as the "Trial Balance."

To prepare a Trial Balance looks a simple thing to do; and so it is, if the transactions are few and the books well kept. But that it has pitfalls many a bookkeeper knows to his cost.

Under the old system of complete journalisation a Trial Balance could be extracted at any moment, provided only that such Journal entries as were posted were so posted both as to debit and credit. So long as this was done, the debit and credit postings could not fail to agree in the aggregate, granted that no clerical mistakes were made. But in modern double-entry, it is necessary, before beginning to take out a Trial Balance, to make sure that the totals of the Journal, Day Book, Invoice Book, &c., are all posted to the appropriate accounts in the Nominal or Private

Ledger. If this were not done the double-entry would not be effected. Under the old system, too, the Trial Balance consisted in extracting the Ledger *totals* instead of the *balances* as is now done, for (as was shown on p. 21) where there is complete journalisation the Ledger totals, allowing for the balances at the beginning, must agree with the Journal totals. It is not possible, in modern books, to see at a glance the total which has gone into the Ledgers for any given period, and it is, on the whole, quicker to disregard this total and the Ledger totals, and to deal with Ledger *balances* only, though a medium of locating an error is thus sacrificed.

A Trial Balance is a balancing of the books for some given period—generally a year or six months. It must be assumed that at the starting point of this period the books were either begun (as in the case of a new business) or that they had at that starting point been balanced off, so that the period began fair—*i.e.*, with the debit balances equalling the credit ones. Granted such a starting point, it is, or ought to be, a simple matter to make a list of all the balances at the close of the given period, putting the debit balances in one column, and the credit ones in another. If all the work on the books has been correctly done the two sides will correspond, and the Trial Balance—*i.e.*, the trial of the balances—has proved their accuracy.

It may very well be the case that a Trial Balance is extracted for the sole purpose of checking the accuracy of the books up to a given point, and that, this being done, the posting proceeds as before. There are many firms who, though they take stock and prepare a Balance Sheet once a year only, yet have a Trial Balance taken out half-yearly, quarterly, or even monthly, merely as a check. The Trial Balance now being considered, however, is assumed to be the preliminary to the preparation of a Balance Sheet. Such being the case, while it is true that, strictly speaking, the taking out of the list of balances is all that is required, it is also true that, as the whole of the Ledgers must be gone through, the opportunity should be utilised to see that, as far as possible, the various Ledger accounts answer to the actual facts of the individual accounts. The bookkeeper should look at each account from two points of view—first, What is the balance of the account as it stands? and second, Is this balance the amount which the balance of the account ought to be? Thus, suppose the bookkeeper on taking out his balances finds that there is standing to the debit of Peter Jones & Co., of Portsmouth, £51 8s. 6d. This, so far as it goes, is a fact to be reckoned with. But suppose also that he happens to know that Peter Jones & Co. of Portsmouth are not allowed credit for over £20, and suppose, further, that the firm deals largely with Peter Jones & Co., of Northampton, it will strike him as probable that goods supplied to the Northampton firm have been posted to the account of the Portsmouth one. If he is wise, he does not interrupt his extraction of the balance to verify the point, but he makes a note of it to be looked into on the conclusion of his task. In short, a competent bookkeeper ought to know approximately what the balance of each personal account *ought* to amount to, and to note the accounts which appear to him to need further looking into. For it may be repeated here that a Trial Balance, *per se*, does no more than demonstrate that what has gone to the debit has also (though perhaps in another form) gone to the credit. It distinguishes between the sides of the Ledger, but does not distinguish between the various accounts.

The following is a Trial Balance—a very simple one—taken out at the point at which the books are stopped preparatory to the preparation of a Balance Sheet, with this single exception (made for the sake of brevity) that it is assumed that before it was taken out the Sold Ledger was gone through, and all debts believed to be bad were written off to a Bad Debts Account in the Nominal Ledger—*i.e.*, the particular debtor's account was credited, and Bad Debts Account debited by means of a Journal entry, this being a kind of transaction for which the modern Journal is properly employed.

The Debtors and Creditors in the Sold and Bought Ledgers respectively are not shown in detail. These Ledgers are assumed to be kept strictly for Personal Accounts, so that in each Ledger every account is of the same character. All impersonal accounts, whether real or nominal, are kept in the Private, or in the Nominal Ledger. In practice the proper Ledger folio would be prefixed to each balance extracted from these Ledgers, but in the illustration they are numbered consecutively for convenience of reference.

TRIAL BALANCE.—31st DECEMBER 1911.

(The last Balance Sheet is assumed to have been struck on 31st December 1910.)

	£	s	d	£	s	d
Bought Ledger (per list)				1,751	1	6
Sold Ledger (do.)	2,972	14	2			
Private Ledger :—						
1. Capital Account (unaltered during year)				3,407	4	2
2. Fixtures and Furniture (unaltered during year)	115	0	0			
3. Stock (as it stood on 31st December 1910)	2,175	12	6			
4. Purchases	10,028	4	2			
5. Sales				13,331	13	8
Nominal Ledger :—						
6. Customers' Discount	386	19	6			
7. Furnishers' Discount				310	6	7
8. Salaries	617	6	0			
9. Sundry Expenses	86	8	3			
10. Rent, Rates, Taxes and Insurance ..	203	16	10			
11. Travelling Expenses	369	5	11			
12. Bank Charges	14	15	11			
13. Carriage	247	0	3			
14. Legal and Professional Costs ..	1	5	0			
15. Bad Debts	167	4	5			
16. Bad Debt Reserve				200	0	0
17. Stationery and Packing Material ..	140	3	10			
18. Bills Payable				197	17	7
Bank Balance, per Cash Book	1,670	2	11			
Cash Balance do.	2	3	10			
	£19,198	3	6	£19,198	3	6

It has necessarily been assumed that the above Trial Balance is correct, but to get one correct is not generally an easy matter, if the transactions are many. This book is not designed to enter into the processes by which errors can be minimised, and, when made, detected, but it may be noted that some possible sources of error are:—

1. The Journals may be wrongly cast—if, for instance, a mistake is made in the addition of the Day Book, the amounts posted in detail to the debit are not the same in total as the amount posted to the credit.

2. The entries in the Journals may be posted wrongly as to amount, or the posting of some item may be forgotten.

3. Ledger accounts which have been ruled off during the year as being square may not be really so.

4. A mistake may be made in adding up in the Ledger the items which constitute the balance.

5. In going through the Ledger to extract the balances a balance may be altogether overlooked.

6. A debit balance may be put upon the list as a credit one, or *vice versa*.

7. The Trial Balance itself may be wrongly added up.

This is a long list, yet it deals only with what may be called normal sources of error. All things are possible in a set of books, especially where there is carelessness or inexperience. And it omits one source which ought never to occur, but the possibility of which cannot be disregarded—an error in the starting point.

The use to which the Trial Balance is put is shown in the next chapter.

CHAPTER XI.

THE BALANCE SHEET—PRELIMINARY WORK.

All authorities are agreed that a necessary preliminary to the preparation of a Balance Sheet is the extraction of a Trial Balance. But from that point to the completion of the formal Balance Sheet and Profit and Loss Account there is no such agreement. Indeed, there could not well be. Partly this is because businesses vary much in their bookkeeping necessities, partly because the work of completion, at least where it is done by professional accountants, is done by experts, to whom the subject is familiar, and who often work under much pressure as to time. Therefore, it must not be assumed that the following description of the work of preparing a Balance Sheet is to be taken as a dogmatic statement of what must be done, or the way in which it must be done; all that is claimed is that the procedure which is described in this chapter illustrates the fundamental principles which must be observed if the required result would be attained.

Referring then to the Trial Balance given in the preceding chapter, the first thing to do is to see whether any of the balances may be at once disposed of by transferring them to another account. In this case there are none to be so treated, but in practice there are generally a few. Thus, there may have been a few purchases bought for ready money which it was not convenient at the time to post direct to the Private Ledger. In such a case there would be an account in the Nominal Ledger called Cash Purchases, and as the amount is not going to figure in the final accounts as a separate item it may as well go at once, by means of Journal entry or direct transfer, to the Purchases Account in the Private Ledger, the Trial Balance being altered accordingly.

Having thus cleared the Trial Balance as much as possible, the next process is to find out what facts require to be duly recorded before the record of the year's transactions is complete—how far, in short, the Trial Balance fails in being a complete presentment of the actual state of affairs. This is done partly by going through the accounts of the Private and Nominal Ledgers (it will be remembered that it is assumed that the balances of the Bought and Sold Ledgers represent only true creditors and debtors), and partly by going through any other information in the counting-house in any form in which it is available. For instance, the Legal and Professional Costs Account (No. 15) shows a debit balance of £1 5s. If the concern has an auditor (as is assumed) it is evident that the account as it stands may show the truth, but surely, considering the smallness of the amount, not the whole truth, and from some source the necessary information to complete it must be forthcoming.

Let it be assumed that from various sources the facts have been brought together for inclusion in the Balance Sheet and Profit and Loss Account. Before dealing with them as a whole there is a technical point which should be made clear. One of the facts to be dealt with later (selected only as an illustration) is that at 31st December there was an amount of £6 15s. 3d. accrued in respect of salaries. This is the amount of the salaries for the odd days between the last pay-day of the business and the end of the calendar year. When salaries are paid, the usual and proper course is to enter the payment on the credit side of the Cash Book, posting it to the debit of Salaries Account in the Ledger. But this is an abbreviation, and is none the less so in that it is a desirable one. If the transaction were set out in full, there would be two entries instead of one, for what has actually happened is that (1) I have become through my Salaries Account a debtor of my employee (call him James Thompson) for the amount of the salary when due (say £5 for the week's salary), and (2) this debt has been wiped out by payment of cash. Put in technical form the entries would be :—

Salaries	*Dr.*	£5 0 0	
To James Thompson			£5 0 0
For Salary for week ending June 21st.			
James Thompson	*Dr.*	£5 0 0	
To Cash			£5 0 0

Thompson would have, of course, a Ledger Account in the ordinary way.

This method of entry would in ordinary circumstances be quite unnecessarily long, because usually a salary is not paid until it is due, and is paid when it is due. The personal account may therefore be dispensed with. But when a Balance Sheet is about to be prepared, there is generally some salary accrued for an odd number of days or weeks from the date of the last payment to the date of balancing. This accrued amount, which is one of the liabilities of the business, must be taken into account in the books in some form. It can be done in any one of at least four ways, three of which are as follow :—

1.—A Journal entry may be made, debiting Salaries Account and crediting Personal Accounts (one being opened for each employee) with the proportion of salary accrued.

2.—A shorter way is to open a joint account for all the salaried employees, debiting Salaries Account with the total amount and crediting the joint account.

3.—A still shorter way is to lump together all the accrued amounts of every description, of which salaries is only one, and by means of a Journal entry to debit each account (Salaries, Carriage, Bank Charges, Rates, or whatever the account may be) with its particular accrued amount, crediting an account called "Suspense Account," which would be a real account representing true liabilities.

(*Note.*—As to how to make such an entry, what a Suspense Account is, and how such a Suspense Account as is meant above, once opened, is to be closed, see Chapter XVI.)

There is a fourth way in which accrued amounts, such as salaries, may be dealt with, which is easier and clearer than any of the foregoing three. This method is to consider the nominal account—Salaries—as being, at the balancing point, a real account to the extent of the liability accrued for the odd period. Thus the amount at the debit of Salaries Account in the Trial Balance given in Chapter X is £617 6s., while the amount accrued is taken as £6 15s. 3d. Two facts are therefore clear: (1) that the total expense for salaries during the year is £624 1s. 3d.; and (2) that there is a liability at December 31st of £6 15s. 3d. If an entry is made (possibly through the Journal, but more probably by direct transfer) debiting Profit and Loss Account and crediting Salaries Account with £624 1s. 3d., then, as there is only £617 6s. at the debit of the account, the effect is to leave a credit balance in the Salaries Account of £6 15s. 3d., which, as it represents a real liability, is brought down as a credit balance, and therefore forms one of the balances with which the next year begins. It will be seen that this is a very simple way of dealing with such a case; no Journal entry or transfer is necessary, and the liability in respect of each account is clearly shown in the account itself. It may be objected to on the theoretical ground that it temporarily transforms a nominal account into a real one, but practical convenience outweighs this argument. Indeed, in all bookkeeping matters, once utility is proved, the theorist has no case unless he is prepared to revert to the old system of complete journalisation.

It is now time to tabulate the facts as to the state of affairs on December 31st 1911, which, it is assumed, have been brought to light from various sources for the purpose of being used to supplement the Trial Balance. They are as follows, the numbers referring to the distinctive numbers preceding the items in the Trial Balance:—

2.—Fixtures and Fittings. £15 is to be written off to reduce the value to £100.

3.—Stock. The stock, as taken at 31st December, amounts, according to the Stock Sheets, to £2,227 9s. 5d. This supersedes the balance of £2,175 12s. 6d. which was the amount of the stock at the preceding 31st December.

6.—Customers' Discount. It is decided to reserve 2½ per cent. on the Sold Ledger balances (£2,972 14s. 2d.) to provide for discounts to be allowed. The amount is £74 6s. 4d.

7.—Furnishers' Discount. It is decided to reserve 2½ per cent. on the Bought Ledger balances (£1,751 1s. 6d.) to provide for discounts to be received. The amount is £43 15s. 6d.

8.—Salaries. There is £6 15s. 3d. accrued.

10.—Rent, Rates, Taxes, and Insurance. The proportion of rates accrued is £12 18s. 9d. On the other hand, the proportion of insurance paid in advance is £10 14s. 2d. This latter amount is an asset.

11.—Travelling Expenses. There is an asset here of £26 for the unexpired portion of season tickets.

13.—Carriage. There are amounts due to the various railway companies—£22 17s. 3d. in all.

14.—Legal and Professional Costs. There is a liability of £21.

16.—Bad Debt Reserve. The reserve stands at £200, but, as it is desired to raise it to £250, a further provision of £50 must be made.

17.—Stationery and Packing Material. There is a stock of material in hand of the value of £16 9s. 6d.

There is nothing owing for Bank Charges (No. 12), because the date of balancing coincides with that of the balancing of the bank's own books.

Summarised, the foregoing information is as follows :—

1.—New assets and liabilities to be introduced :—

	Asset £	s	d	Liability £	s	d
3.—Stock (new)	2,227	9	5			
8.—Salaries				6	15	3
10.—Rent, Rates, Taxes, and Insurance ..	10	14	2	12	18	9
11.—Travelling Expenses	26	0	0			
13.—Carriage				22	17	3
14.—Legal and Professional Costs				21	0	0
17.—Stationery, &c. (new Stock)	16	9	6			

2.—Provision to be made for diminution of liabilities or assets already in the books :—

	Diminution of Liabilities £	s	d	Diminution of Assets £	s	d
2.—Fixtures and Fittings				15	0	0
3.—Stock (old)				2,175	12	6
6.—Customers' Discount				74	6	4
7.—Furnishers' Discount	43	15	6			
14.—Bad Debt Reserve				50	0	0

The next chapter shows how these facts, which at the moment exist as memoranda only (and may, as a whole, be distinguished as the "Memorandum") are introduced into the books.

CHAPTER XII.

THE BALANCE SHEET—(continued). THE CLOSING OF THE BOOKS.

With the Trial Balance and the Memorandum of the further information required, the point is now reached at which it is possible to prepare a Balance Sheet and a Profit and Loss Account. Of course, all the information contained in the memorandum must be given effect to in the books before they are closed for the year; but it is not necessary, and it is often not convenient, to record it before the accounts are prepared. With this information in a tabulated form it is easy to supplement the Trial Balance, and to set forth the whole of the available facts in an intelligible form. This is done in the following statement. The first pair of columns is a mere recopying of the Trial Balance; the second pair, which are headed "Balance Sheet," show each "real" account in the Trial Balance as it will appear when the supplementary information in the Memorandum is given effect to; and the third pair, headed "Profit and Loss Account," show each "nominal" account similarly supplemented by information from the Memorandum. It will be noticed that any departure from the Trial Balance columns in the Balance Sheet and Profit and Loss Account columns is a double one, so that, taking each line by itself, the balance of the Balance Sheet and Profit and Loss Account figures taken together is always the same as the Trial Balance figure.

TRIAL BALANCE

Amplified so as to include all known Liabilitie

No.	Name of Account	Notes
	Bought Ledger	
	Sold Ledger	
	Private Ledger :—	
1	Capital Account	
2	Fixtures and Fittings	£15 to be written off ...
3	Stock	New Stock, £2,227 9 5
4	Purchases	
5	Sales	
	Nominal Ledger :—	
6	Customers' Discount	Make reserve of £74 6 4
7	Furnishers' Discount	Make Reserve of £43 15 6
8	Salaries	Accrued, £6 15 3 ...
9	Sundry Expenses	
10	Rent, Rates, Taxes and Insurance	Accrued, £12 18 9 In advance, £10 14 2
11	Travelling Expenses	In advance, £26 ... ...
12	Bank Charges	
13	Carriage	Due, £22 17 3 ... ...
14	Legal and Professional Costs	Due, £21 .. ..
15	Bad Debts	
16	Bad Debt Reserve	To be increased to £250 ...
17	Stationery and Packing Material	Stock, £16 9 6 ... ...
18	Bills Payable	
	Bank Balance per Cash Book	
	Cash Balance do.	
	Balance of the Balance Sheet columns and also of the Profit and Loss Account columns	

31st December 1911.

and Assets at date and then analysed.

Trial Balance		Balance Sheet		Profit and Loss Account	
Dr.	*Cr.*	*Dr.* (Assets)	*Cr.* (Liabilities)	*Dr.*	*Cr.*
£ s d	£ s d	£ s d	£ s d	£ s d	£ s d
...	1,751 1 6	...	1,751 1 6		
2,972 14 2	...	2,972 14 2			
...	3,407 4 2	...	3,407 4 2		
115 0 0	...	100 0 0	...	15 0 0	
2,175 12 6	...	2,227 9 5	...	2,175 12 6	2,227 9 5
10,028 4 2	...	...	...	10,028 4 2	
...	13,331 13 8	...	...	...	13,331 13 8
386 19 6	...	...	74 6 4	461 5 10	
...	310 6 7	43 15 6	...	...	354 2 1
617 6 0	...	...	6 15 3	624 1 3	
86 8 3	...	...	...	86 8 3	
203 16 10	...	10 14 2	12 18 9	206 1 5	
369 5 11	...	26 0 0	...	343 5 11	
14 15 11	...	...	...	14 15 11	
247 0 3	...	...	22 17 3	269 17 6	
1 5 0	...	...	21 0 0	22 5 0	
167 4 5	...	...	...	167 4 5	
...	200 0 0	...	250 0 0	50 0 0	
140 3 10	...	16 9 6	...	123 14 4	
...	197 17 7	...	197 17 7		
1,670 2 11	...	1,670 2 11			
2 3 10	...	2 3 10			
19,198 3 6	19,198 3 6	7,069 9 6	5,744 0 10	14,587 16 6	15,913 5 2
...	...	...	1,325 8 8	1,325 8 8	
	£	7,069 9 6	7,069 9 6	15 913 5 2	15,913 5 2

If the reader has followed the foregoing processes he will have perceived that the guiding principle has been the separation of real from nominal accounts, and that in the analysed Trial Balance this has been so completely effected that the Balance Sheet and Profit and Loss Account have been prepared almost automatically. Assuming (as is necessary) that the assets are taken at their true value, and that all liabilities are included, then of every item of assets in the Balance Sheet there may be answered in the affirmative this question: Does it stand for a real asset—something for which there is value? Similarly, every item of liabilities in the Balance Sheet is a true liability; something which must sooner or later be paid. On the other hand, the items in the Profit and Loss Account cannot stand these tests. The amounts in that account represent neither true assets nor true liabilities, and their failure to stand the test is the true mark of their being nominal accounts.

Further, it will be seen on reflection that, although the two kinds of balances are so different, they come from the same stock, and are complementary to each other. Each transaction which has entered into the making of the balance of a real account has also entered into the making of a balance of a nominal account. Thus, to give the most obvious illustration, the Sold Ledger balances (which are, of course, debits) are the product of, *inter alia*, the posting of the individual sales, which in total make up the balance at the credit of the nominal account called "Sales." It may be noted here, however, that it is not invariably the case that a transaction affects both a real and a nominal account. "Cash" and "Plant" are both real accounts, and an expenditure of cash on plant affects real accounts only—it does not touch the nominal ones.

The one apparent exception to the reality of the real accounts is the balance of £3,407 4s. 2d. at the credit of the Capital Account. But there is a very substantial reality behind this account, for it is the balance of the other real accounts with which the year began—*i.e.*, the assets exceeded the liabilities on 1st January by £3,407 4s. 2d.; or, to put it in another way, on a realisation at face values there would have been a net cash surplus of that amount. That is reality enough.

It will be seen, on reference to the analysed Trial Balance, that the Balance Sheet columns and those of the Profit and Loss Account alike result in a balance of £1,325 8s. 8d. This is the profit of the year, because it is the amount by which the surplus of real assets over real liabilities has increased during the year.

It is the ascertainment of the amount by which a man's capital has increased during the year which is the ultimate test of the amount of profit earned. If, as in the instance given, a business has in it at the beginning of the year a surplus of assets over liabilities of £3,407 (omitting shillings and pence), if no capital is withdrawn during the year and no fresh capital is brought in, and if, finally, the surplus at the end of the year is £4,732, then, books or no books, double-entry or single-entry, the profit for the year is £1,325. It might be thought that, since this is so, the time spent on the nominal side of the bookkeeping was wasted. But such is not the case. Unless books are regularly balanced there exists no guarantee of accuracy, nor is there any check on dishonesty. While, therefore, the extent to which the capital has increased between one stocktaking and another certainly shows what profit has been earned, it does not show what it might have been had greater care been taken ; a loss due to carelessness or fraud not being disclosed, or even hinted at.

One service, therefore, which properly kept books perform is to place a check upon carelessness and fraud. The other service is that they show, through the medium of the Profit and Loss Account, *how* the profit has been arrived at. A Balance Sheet is like an instantaneous photograph which shows, perhaps, a wide range of country, but shows it only as it appears at a particular instant. The Profit and Loss Account, on the other hand, is an itinerary—it does not show the commercial wayfarer where he is, but it does show him *how* he has travelled to the point which he has reached.

It is not likely that anyone in pursuit of beauty would look for it in the art of bookkeeping. Nevertheless, there is beauty in the perfect adaptation of ends to means, and of this beauty well-organised bookkeeping has its share. Notice in the analysed Trial Balance how each of the two sides, the real and the nominal, has gone its way during the year, and how when brought to the balance they produce similar balances, though the Balance Sheet columns are made up of real assets and liabilities, while those of the Profit and Loss Account columns are composed of unreal and arbitrarily named accounts.

Moreover, the entries needed to produce the Profit and Loss Account balances are trifling in number, compared with those required to bring about the Balance Sheet balances. It is an abuse of terms to call such a system double-entry, if by this is meant the double entering of everything. The abbreviations now introduced in all books are so great that the entries needed to produce the "nominal" side of the books are but a small fraction of those required for the "real" side.

It is, however, unnecessary to labour this point, if only for the reason that the trend of modern business is all on the side of good bookkeeping. With large concerns it is a necessity of their existence, while with smaller ones there are many causes working in the same direction—

notably the Companies Act and the Income Tax Acts.

Nothing now hinders the drawing out of a Balance Sheet and a Profit and Loss Account in the customary form. These are a mere rearrangement of the Balance Sheet and the Profit and Loss Account columns respectively in the analysed Trial Balance. But there still remains some work to do—the information contained in the Memorandum must be given effect to in the books, and every nominal account must be closed, by transfer to the Capital Account *viâ* the Profit and Loss Account. In practice these two processes would proceed simultaneously, but it is simpler to take them separately, and to take the second one first. It is necessary to open an account in the Ledger (if there be a Private Ledger it is in that book in which the account would be opened) called "Profit and Loss Account." Then, either by Journal entry or by direct transfer, this account is debited with each amount which appears in the debit column of the Profit and Loss portion of the analysed Trial Balance, the individual accounts being correspondingly credited. Take, by way of illustration, the first account in the Nominal Ledger —Customers' Discount (No. 6). In the Profit and Loss Account columns, on the debit side, there is an amount of £461 5s. 10d. An entry is, therefore, made on the *credit* side thus: "1911 Dec. 31, By

Profit and Loss Account £461 5s. 10d.," giving, of course, the proper reference—either the Journal folio or the page in the Private Ledger on which the Profit and Loss Account appears. This process, applied to all the amounts in the debit column, and the reverse process applied to those in the credit column, must result in the Profit and Loss Account in the Private Ledger containing all the items which are in the Profit and Loss columns of the Trial Balance, and therefore in its ending with a credit balance of £1,325 8s. 8d. But how has it left the Private and Nominal Ledgers? It will be seen that it has left them with, and only with, the balances shown in the Balance Sheet columns of the Trial Balance. Thus, to take again the Customers' Discount Account. At the point of the first extraction of the balances there was a debit of £386 19s. 6d. Since then there has been made an entry on the credit side (the transfer to Profit and Loss Account) for £461 5s. 10d. The result is now a credit balance of £74 6s. 4d., which is the needed amount, it having been decided to reserve that sum against discounts to be allowed to debtors on payment. Take, again, Account No. 12, Bank Charges. This had £14 15s. 11d. at its debit; but as that is also the amount in the Profit and Loss columns, it receives exactly this amount by transfer to the Profit and Loss Account, and is therefore squared, and, for the time being, ceases to exist. This is correct, for there is nothing owing to, or by, the business in connection with the account.

The method of treating the Stock Account is clearly shown in the illustration, but as the method of dealing with it often presents difficulties to students, a special section is devoted to the subject in Chapter XVI.

The next process is actually to strike the balances as they now exist in the Private and Nominal Ledgers (with the exception of the Capital Account in the Private Ledger), ruling off the accounts and bringing down each balance in the usual way. It is assumed that the Bought and Sold Ledger balances have similarly been brought down, if it is possible so to do, which is not always the case. But the balances in the Private and Nominal Ledgers require some little special attention—the nature of the amount constituting the balance should be briefly indicated, as the account itself does not disclose what the balance ought to be. Thus, turning once more to the Customers' Discount Account, technicalities are complied with if, on the debit side, before striking the balance, there are the words "To balance £74 6s. 4d.," and on the credit side, after the account has been ruled off, the words "By balance £74 6s. 4d." But against one or other of these amounts should be put some such explanation as "2½ per cent. on Sold Ledger Balances £2,972 14s. 2d." So with the other accounts.

In the case of Rent, Rates, Taxes, and Insurance Account (No. 10), it will be noticed that there are accrued amounts due both to and by the business. In such a case it is well to bring down two balances—one on the debit side, and the other on the credit.

At this stage every account in the books save two has either been closed or has had its balance struck. These two are the Capital Account, which has a credit balance of £3,407 4s. 2d., and the newly-opened Profit and Loss Account. which has a credit balance of £1,325 8s 8d. The penultimate act of the year is to carry the amount at the credit of the Profit and Loss Account to the credit of the Capital Account, thus closing the former account, and making the balance at the credit of the latter £4,732 12s. 10d. With the ruling off of this account, and the bringing down of the balance, the year's operations are at an end, and the balances with which the year closes become those with which the new one opens.

It must be borne in mind that the above illustration is assumed to be that of a business owned by a private individual—it is neither a limited company nor a partnership. If it were either of these, it would make no difference to the principle, or to the general procedure, but it would alter the entries which directly affect the Capital Account. The point is further dealt with in Chapter XVI.

CHAPTER XIII.

THE BALANCE SHEET (concluded)—FORMAL ACCOUNTS, THE CAPITAL ACCOUNT, &c.

It is usual to gather together the balances with which the old year ends, and the new one begins, in such a way that the various items can be readily grasped and their significance understood—to prepare, in short, a Balance Sheet. In the case of the accounts which have been dealt with in the two preceding chapters the Balance Sheet would take some such form as follows:—

BALANCE SHEET, 31st December 1911.

Liabilities.		£ s d	£ s d
Sundry Creditors :—			
On Open Account ..	£1,751 1 6		
Less 2½%	43 15 6		
		1,707 6 0	
On Bills payable		197 17 7	
Carriage, Rates and Sundries ..		63 11 3	
			1,968 14 10
Capital			4,732 12 10
			£6,701 7 8

Assets.		£ s d	£ s d
Cash at Bank and in hand			1,672 6 9
Trade Debtors		2,972 14 2	
Less 2½% for discount ..	£74 6 4		
" Reserve for doubtful Accounts	250 0 0		
		324 6 4	
			2,648 7 10
Stock-in-trade			2,243 18 11
Fixtures and Fittings..			100 0 0
Insurance, etc., paid in advance			36 14 2
			£6,701 7 8

It will be noticed that the liabilities are on the left-hand or debit side, whereas in the books the balances representing liabilities are the credit ones. Why this should be has been the subject of much discussion and argument. It is, however, a matter of no real importance. Howsoever the custom arose, there it is, and merely because it is a custom it should be adhered to, as uniformity always should be adhered to in accounts unless there is a distinct gain to be obtained from diversity.

The order in which liabilities and assets are set forth is a point on which there is no general agreement. It also is a point which is not of great importance, though every person who is in the practice of drawing out Balance Sheets has some principle of arrangement on which he acts: *e.g.*, the assets in the above Balance Sheet have been placed in the order of their realisability.

The Balance Sheet, it will be observed, is not a Ledger Account; it is a grouping together of all the Ledger Accounts at the point at which all nominal accounts have been closed and only real ones remain. The Profit and Loss Account, on the other hand, while it usually accompanies the Balance Sheet, is only one of the many Ledger Accounts which is selected for special treatment because of its exceptional character as a synthesis of all the nominal account transactions of the year. It is an account which is intelligible and instructive, or the reverse, according to the arrangement of the items composing it. In practice it is sometimes built up in the Ledger in an intelligible form, the items having previously been properly arranged through the medium of a draft. But the entries may be made in the Ledger in any order which is convenient, which is, generally, the order in which the accounts to be written off appear in the Ledger. There is much to be said for the adoption of this practice, leaving the suitable arrangement of the items to be set forth in the Profit and Loss Account which accompanies the Balance Sheet. But again the point is one of practice, not of principle.

It will be observed that the Profit and Loss Account has but a momentary existence. It is opened only to be immediately closed. And as it is closed by transferring its balance to the Capital Account, the net result on that account, and on the Balance Sheet, would be the same if there were no Profit and Loss Account at all, the nominal account balances being carried straight to the Capital Account. The Profit and Loss Account is interposed between the nominal balances and the Capital Account solely for the sake of clearness. If they all went straight to the Capital Account, the balance of them, which constitutes the profit, could not be ascertained at a glance, as it can be by keeping a separate account for the purpose.

Indeed, not only could the nominal accounts go direct to the Capital Account without affecting the result, but there need be no nominal accounts at all except the Capital Account. Were this done the Capital Account would be inordinately long, and quite unintelligible, and it is not to be supposed that the procedure is advocated. Its possibility is mentioned merely to emphasise the fact that one side of the double-entry is the trader himself, and that however much he may for statistical purposes split himself into Sales Account, Purchases Account, and the like, all these accounts *are* but himself in some guise, and find their abiding place in the Capital Account.

Properly arranged the Profit and Loss Account for the year, as given in the Trial Balance in the last chapter, would assume some such form as this :—

PROFIT AND LOSS ACCOUNT, for Year ending 31st December 1911.

	£	s	d		£	s	d
To Stock at 1st Jan.	2,175	12	6	By Sales	13,331	13	8
,, Purchases ..	10,028	4	2	,, Stock, 31st Dec...	2,227	9	5
,, Carriage (of Goods bought) ..	269	17	6				
,, Balance, being Gross Profit carried down ..	3,085	8	11				
	£15,559	3	1		£15,559	3	1

	£	s	d		£	s	d
To Salaries	624	1	3	By Balance brought down	3,085	8	11
,, Travelling Expenses	343	5	11	,, Discount from Furnishers ..	354	2	1
,, Rent, Rates, Taxes, and Insurance ..	206	1	5				
,, Stationery and Packing Material	123	14	4				
,, Sundry Expenses	86	8	3				
,, Bank Charges ..	14	15	11				
,, Legal and Professional Costs ..	22	5	0				
,, Bad Debts ..	217	4	5				
,, Discount allowed to Customers ..	461	5	10				
,, Depreciation of Fixtures and Fittings ..	15	0	0				
	2,114	2	4				
,, Balance, being Net Profit ..	1,325	8	8				
	£3,439	11	0		£3,439	11	0

Like the Balance Sheet, the Profit and Loss Account is much discussed as to its form. Generally it is split up into two, as is done above, the first part (which is generally known as "The Trading Account") being used to show the Gross Profit, or the difference between selling price and prime cost. It must be understood that this division into Trading Account and Profit and Loss

Account is a mere separation, always more or less arbitrary, of the Profit and Loss Account proper into two parts. It is a division often found to afford valuable information, but it does not affect the result in any way.

There is one entry generally to be found in the Profit and Loss Account of a privately owned concern, which does not appear in the foregoing account—interest on capital. This was omitted so as not to complicate the analysed Trial Balance. It is usual for a business man to charge his business with interest on the capital employed in it, before arriving at his profit. The idea is that he could have earned interest on his capital, without taking any personal trouble, by investing it, and that therefore the real profit arising from his work in his business is not the gross increase of his capital during the year, but this increase less the interest which could have been obtained from an outside investment of that amount of capital which he has locked up in his business. In theory this is correct, and in practice, where there are partners with differing capitals, the charging of interest is a useful method of recognising the difference. But where a business has only one owner, though the practice is desirable, it is obviously only a taking of money from one pocket and putting it into another. Technically the operation is achieved by debiting the Profit and Loss Account, and crediting the Capital

Account with the interest, which is usually calculated at the rate of five per cent. per annum.

The Balance Sheet, as has been stated, shows how a business stands on a given day, and the Profit and Loss Account, which usually accompanies it, shows what profit (or loss) has been made from the date of the preceding Balance Sheet. But though a trader may possess a Balance Sheet at the beginning of the year, another at the end, and a Profit and Loss Account covering the intervening period, he is not of necessity in the possession of all the information he ought to have. There may be, and there generally are, transactions during the year affecting his capital which have no place in the Profit and Loss Account. Capital in large or small sums may be, and generally is, withdrawn; and, similarly, capital may be paid in. That a clear view of the position may be obtained it is therefore necessary that the Balance Sheets and Profit and Loss Account should be accompanied by a copy or a summary of the Capital Account. To withdraw capital does not affect the profit earned—it only decreases the cash or bank balance, just as the effect of bringing in capital is to increase this balance. The owner of a business generally draws a considerable number of amounts during a year against the profit which is being earned—in short, he usually lives on his business. And he frequently pays in sundry dividends and other items. He uses the business, in fact, as a kind of banking account. It is customary to keep all these transactions in a separate account, called the "Drawing Account," or the "Current Account," and to transfer the balance of this account in one sum to the Capital Account at the end of the year. This is done for convenience only, for all drawings are a diminution of capital, and could quite properly go direct to the Capital Account. On the other hand any unusually large sums drawn out, or paid in, may very well go direct to the Capital Account instead of going through the Drawing Account. But the distinction is arbitrary, depends on the circumstances of each business, and makes no difference to the result.

Bearing in mind these transactions on Capital Account, it will be seen that the amount by which capital has increased in the year is not, by itself, a demonstration of the earning of profit. A man may find that his capital is the same in amount at the end of the year as at the beginning, but if during the year he has drawn £1,000 from the business, he must have made that sum, or his capital would have diminished instead of remaining stationary. It is for this reason that full information for the year involves a Capital Account as well as a Profit and Loss Account.

The Capital Account should show the capital at the beginning of the year according to the Balance Sheet of that date, the interest on capital, the profit according to the Profit and Loss

Account, the capital (if any) brought in during the year, and the capital withdrawn. The balance should agree with the capital shown by the Balance Sheet at the end of the year.

If in the illustration given in the last chapter the trader had charged interest on his capital at 5 per cent., and if he had withdrawn £1,000, his Capital Account would have been as follows:—

CAPITAL ACCOUNT, for Year ending 31st December 1911.

	£	s	d		£	s	d
To Amounts withdrawn during year	1,000	0	0	By Capital at 1st Jan. 1911 per Balance Sheet of that date	3,407	4	2
,, Balance, being Capital at 31st Dec. 1911 per Balance Sheet	3,732	12	10	,, Interest for year at 5 per cent. ..	170	7	2
				,, Net Profit for Year per Profit & Loss Account	1,155	1	6
	£4,732	12	10		£4,732	12	10

It will be noticed that the net profit and the interest on capital together make £1,325 8s. 8d., which is the net profit shown in the account on p. 89.

The capital at the close of the year is £1,000 less than the amount shown in the Balance Sheet on p. 85, because, by way of illustration, that amount is assumed to have been withdrawn.

PART II.

WITH the preceding Chapter, the main argument of this work comes to an end. But while the principle underlying the keeping of a normal set of books has been set forth, yet only normal circumstances have been dealt with. There are many matters, not necessarily met with, which, nevertheless do in fact enter into or affect many sets of books. Some of these will now be touched upon—not exhaustively, but only in so far as they affect the balancing of a well-kept set of books.

CHAPTER XIV.

COLUMNAR BOOKS.

It is not uncommon to find in a set of books, some which are so arranged as to analyse, item by item, the entries made in them, by means of additional columns with appropriate headings. Perhaps the Invoice Book is the one to which this practice is most frequently applied. Thus, an Invoice Book may be in some such form as this:—

No. of Invoice	Date	Name	Ledger Folio	Total	A. Dept.	B. Dept.	C. Dept.
	1912			£ s d	£ s d	£ s d	£ s d
1	Jan. 1	John Flint & Co. ..	72	15 18 0	..	15 18 0	
2	1	E. Radford & Co. ..	81	31 2 6	31 2 6		
		&c. &c.					
		Totals for month		£ 1,750 3 9	713 12 2	683 1 8	353 9 11

If there were no analysis columns, the total of £1,750 3s. 9d. would in the ordinary way be posted to the debit of a Purchases Account. Strictly speaking, the only difference which this analysis makes to the books, from the point of view of their balancing, is that, instead of posting the total of the first column, it is the total of each of the three analysis colums (which in the aggregate equal the total of the first column) which is posted—probably to a Departmental Purchases or Trading Account.

(As to the principle which should be adopted in keeping and analysing an Invoice Book, see p. 103.

The reason why it is more common to find an analysed Invoice Book than an analysed Day Book is that it is possible, and generally desirable, for every invoice to be brought to one spot for incorporation in the books through the Invoice Book, while it often happens that sales cannot be so treated, but must be entered in a Day Book the moment they are made. An analysis of sales, therefore, if needed, is generally most conveniently made by there being several Day Books, instead of by means of several columns in one book.

As to the extent to which the columnar system should be carried, it is safe to say that it should be used to illuminate, and not to darken, counsel, and to this latter purpose it may easily be unwittingly put. It may be made a valuable means of obtaining, at little cost, useful statistical information—information supplementary to that afforded by normally kept books. If, however, instead of being used to obtain additional information it is used as a substitute for the posting of individual items, its benefit may well be more than questionable. It is possible to make such a use of the system in the Cash Book, the payments being thrown out into analysis columns, to save the trouble of posting in detail to the Nominal Ledger. This, however, is not satisfactory. It is easy to look through the accounts in a Nominal Ledger, and when each account shows in detail each payment belonging to it, effective criticism is possible. But when only the totals of analysis columns are posted, the Ledger tells nothing, and details must be looked for in the Cash Book—an arduous task, which, as a plain matter of fact, no principal or responsible manager will ordinarily undertake.

Columnar analysis may be, therefore, good or bad, according to the nature of the analysis undertaken. But, even if the analysis be of a kind which is normally advantageous, it may, in particular cases, be useless. All legitimate analysis involves some trouble Before undertaking it, therefore, a trader should ask himself what he expects to get out of it, and whether the trouble will be justified by the result.

WHAT CONSTITUTES A "SET" OF BOOKS.

It might be thought that this was a question which anyone could answer, but experience proves the contrary. From the bookkeeper's point of view the "set" comprises all those books, and only those books, which are necessary for the production of a Trial Balance. These, according to the nature of the business, may be all (or most) of the books used in the business, or they may be but a small fraction of them. In manufacturing concerns there is certain to be a great number of books dealing in a preliminary way with what ultimately become entries in the Day Book, such as Time Books, Wages Books, Cost Books, &c. These are of prime importance and may have a system of their own, but they are not part of the balancing books, and could all be destroyed without interfering with them *as* balancing books. In distributive businesses, though the number of preliminary books is not so large as in manufacturing businesses, yet there are generally some (*e.g.*, Order Books) which form the basis for entries in the balancing books, but are no part of them.

The case of those books which are partly within the system and partly outside of it is more complicated. The Invoice book illustrated on p. 95 is a case in point. The book may be considered as being made up of four parts: *first*, the individual items in the first column, as posted to the Bought Ledger; *second*, the total of these items, being the total of the first column; *third*, the individual items as analysed into their several columns; and *fourth*, the totals of these columns. But, for balancing purposes, the second and third parts are of no importance, for they do not enter into the system; it is the first and fourth which matter. So long as the amounts which go to the debit of the Departmental Purchase Accounts (or whatever the accounts may be called) equal those which have gone to the credit of individual accounts in the Bought Ledger, the rightness or wrongness of the analysis, as between one department and another, matters (for purely balancing purposes) not at all. In the same way, the correctness of the addition of the first column does not matter, for the total is not used. It would, of course, be almost impossible for this addition to be wrong while that of the analysis columns was right, but the point is that its wrongness, if confined to itself, would not matter; indeed, for balancing purposes, the column need not be added up at all.

The general rule is simple: only items posted into the Ledger count for balancing purposes; how they are made up, whether or not they are wrongly made up, makes no difference. It is, of course, the bookkeeper's business to see that they are right in fact, as well as for bookkeeping purposes; but if he alter one he must remember that, if it is already posted, this entails an alteration in the Ledger, and that, if the matter has anything to do with the totals of analysis columns, an alteration in one *may* involve a corresponding alteration in another.

PETTY CASH BOOK.

The Petty Cash Book, as it may usefully be kept, affords an instance both of an analysed book and of a book which is mainly, but need not be wholly, outside the balancing books. It also affords an instance of a book which may offer peculiar temptations to the making of errors in principle.

Petty cash, as everyone knows, is the cash used to make payments of small individual importance, though their aggregate amount for a year may be considerable. The necessary cash to make the payments is obtained from the main cash, generally in round sums, perhaps of £5 or £10 each. So far as the main set of books is concerned, they need have very little to do with the petty cash. If a cheque for, say, £10 is wanted for petty cash, it is drawn, entered in the main Cash Book as a payment to petty cash, and posted to an account of that name in the Nominal Ledger. Here the matter may end, for though the Petty Cash Book enters this particular cheque and all others as a receipt, and has full particulars of payments just as the main Cash Book has, yet these are outside of the balancing system. But the matter need not end, as regards the main books, with the debit in the Nominal Ledger of a number of sums paid to petty cash, and, generally, should not so end. It should be carrried a little further, because, when the year's accounts are made up, it is unsatisfactory to find in the Profit and Loss Account an item "Petty Cash £200," or whatever the amount may be, for it affords no indication of how the money has been spent. It is therefore usual to analyse the petty cash payments, and this is best done by using a Petty Cash Book ruled with columns for the various known heads of expenditure, such as Postage, Carriage, Travelling, and Sundries, or otherwise, as may be suitable to the business. This analysis is the very thing to which objection was taken on p. 96, as applied to the main Cash Book. The difference is that in that Cash Book the amounts are, or may be, large, whereas in the Petty Cash Book they are small, and therefore of little individual importance. Suppose that at the end of a month the payments, divided as above, had been as follow:—

Total	Postage	Carriage	Travelling	Sundries
£20 17 6	£8 1 9	£3 17 2	£5 2 1	£3 16 6

It is assumed that the Nominal Ledger contains accounts for these various items of expense. Assume also that petty cash has received £25 from the main cash. The Nominal Ledger, therefore, has £25 at the debit of Petty Cash Account, and the balance of the Petty Cash Book itself is £4 2s. 6d. If, then, the total of the payments (£20 17s. 6d.) is posted to the credit of the Petty Cash Account in the Nominal Ledger, its balance will stand at £4 2s. 6d., and if the total of each analysis column goes to its proper account, these accounts will be increased on the debit side by an aggregate of £20 17s. 6d., which is the amount which has gone to the credit of the Petty Cash Account. The net result is that the payments made through the petty cash will have been incorporated in the main books and passed to their proper accounts.

The entry by which Petty Cash Account is credited and the Expense Accounts debited may be made, and often is made, through the Journal. In such a case the Petty Cash Book remains wholly outside of the system, only affecting it as a means of supplying information for a Journal entry. But there is no necessity to make the entry through the Journal, for the totals may quite well be posted to the Ledger direct from the Petty Cash Book itself. If that is done, the book to the extent of the monthly totals (but only to that extent) enters into the balancing system.

What has been said as to the analysing of payments applies also to receipts, if there are receipts other than those from the main cash.

It will be noticed that in the form of Petty Cash Book outlined above, all the *details* are outside of the balancing books. It is therefore not practicable to post any such item to the Ledger. But it is possible to have, as one of the analysis columns, one headed "Ledger Accounts," and to enter in this any payments which it is desired to post to the Ledger. Necessarily the total of the column would not be posted to the debit of any expense account, as it had already been posted in detail. But it is better to keep the Petty Cash Book clear of the Ledgers except as to the totals, and to enter in the main Cash Book every item, however small, which it is desired to post directly into a Ledger.

WHAT ITEMS GO INTO THE INVOICE BOOK.

Speaking generally, an Invoice Book is, as its name implies, for invoices. Most of the purchases made by a business are made from concerns with whom it has a running (usually a monthly) account. Each delivery of goods is accompanied, or quickly followed, by an invoice giving details, and at stated times these invoices are set out in total in what is known as a "statement." An invoice is an advice that certain goods have been sent, a statement is, in effect, a demand for payment of the total of the goods supplied for a specified period. The proper function of the Invoice Book is to record these invoices as they come to hand. Each one is posted to the furnisher's Ledger Account, which, if all is right, agrees with the statement which arrives after the close of each month.

If it is desired to conduct a large business with due regard, on its statistical side, to efficiency and economy, it would be absurd to do so without the aid of an Invoice Book and a Bought Ledger. Nevertheless, these books are not vital ones in the sense in which a Day Book and Sold Ledger are vital. In the nature of the case they only record in writing what is already in documentary form. It would be possible to file all invoices under their respective firms, to compare these with the statements, to debit each payment of a statement direct to a Purchases Account, and to ascertain the liabilities at any time by making a list of the invoices for which statements had not been received and the statements which had not been paid.

The fact that the keeping of an Invoice Book is not vital, however desirable it may be, brings about diversity in the method of keeping it. Departure from the system of reserving it for invoices generally takes one of two forms: (1) Either it is used only for invoices which are in respect of goods bought to sell again, or (2) it is used for purchases where in the nature of the transaction there are no invoices.

As to the first method of using the book, in all businesses there is a clear distinction drawn between articles purchased for re-sale and those purchased as a necessary incident of providing the means of this re-sale. It may not be easy to draw the line, but it is drawn. Purchases for stock are one thing, and purchases for expenses another. And the Invoice Book is not infrequently reserved rigidly for the former class of purchases only. But this is not quite satisfactory, and is certainly not necessary. It is not satisfactory because there may be, and often are, other purchases than stock ones which are the subject of invoices. Such items of expense as repairs to machinery, coal, and horsekeep (to name only a few) often require frequent purchases, involving invoices, monthly statements, and Bought Ledger Accounts, and it is to meet this class of purchase, irrespective of the kind of thing purchased, that the Invoice Book exists. Any objection there may be to mixing together purchases for stock and those for expenses disappears, when it is remembered that the distinction can easily be preserved by means of appropriate analysis columns in the Invoice Book.

The other method of using the book, which falls short of complete satisfactoriness, is to use it too much—to use it for purchases for which there are no invoices. Take the case of accounts for gas supplied. These are generally rendered quarterly, and in the ordinary course one is paid before another is rendered. There is no object in putting this quarterly account through the Invoice Book, for there are no invoices to be gathered together. Not only so, but an Invoice Book entry involves a Bought Ledger Account (*i.e.*, a Personal Account), and it is a waste of time to open such an account. It is not necessary to make any entry in the books for a Gas Account (using this as typical of a class) till it is paid, when the necessary entry of the payment in the Cash Book is posted direct to the proper account in the Nominal Ledger. If Gas Accounts, or similar ones, are put through the Invoice Book, not only is a Personal Bought Ledger Account necessitated, but there is a real difficulty in getting the amount of the account to the proper Nominal Ledger Account, as it can only be done by a very detailed analysis of the Invoice Book.

But, when all is said, so long as an Invoice Book is properly kept in the main, the fact that it contains a little more or less than it ought to do is not a very great matter; and, so far as the balancing of the books is concerned, it is no matter at all. Custom has some weight, and though an established practice which achieves a result may fall short of perfection, it may be better to continue it, so long at least as it is worked through one particular individual, than to upset existing arrangements in order to inaugurate a system more nearly approaching theoretical perfection.

CHAPTER XV.

BRANCH ACCOUNTS.

THE accounts between a Head Office and its branches present certain bookkeeping problems which are somewhat outside the ordinary experience. There are some concerns, such as banks and multiple-shop companies, whose very existence lies in having many branches. Each of these has its own system, suited to its needs. But it is not of these that this section proposes to treat, but rather of the more common case of a business which is carried on at several places. In this connection the word "Branch" has many meanings. There are instances where the branch practically *is* the business, as in the common case of a company which has a registered office and a board of directors in London, but carries on its real business in the Colonies or abroad. On the other hand, there are businesses which, though mostly carried on at one place, yet, for one reason or another, have some sort of a small representation in another place—perhaps only an order office. Then there are concerns which have branches which sell independently but do not buy—that being done for them by the Head Office; and there are other branches which buy, but do not sell. There are others which both buy and sell, just as the Head Office does.

Not only are there all sorts of branches, but there are all sorts of ways of controlling them. In one case no information may be required from the branch but an annual Balance Sheet and Profit and Loss Account, while in another the Head Office will be satisfied with nothing less than duplicates of every entry in the branch books. And between these two extremes are endless variations.

Nothing, therefore, can be attempted here but some indication of general principles—of how the double-entry principle may be brought into use in the case of Branch Accounts, as in the case of accounts of every other kind.

Take first the case of a concern which desires to establish a business abroad—one which shall be entirely independent, doing its own buying and selling. Assume that questions of foreign currency and exchange fluctuations (which form the subject of the next section of this chapter) may be disregarded. Money is sent (say £20,000 in all) to the manager of a new venture (in Vienna, let it be assumed) with which he erects a factory. In the English books this is debited to an account called "Vienna Branch." A set of books would, of course, be started in Vienna, and the accounts opened there for the various items of expenditure, such as

Land and Buildings, Fixed Plant, Loose Plant, &c. If the completion of the erection and equipment of the factory be supposed to coincide with the close of the financial year, the London office has in its books a debit balance "Vienna Factory £20,000," and the Vienna office has a credit balance of a similar amount in its books to an account called "London Office." The Vienna Balance Sheet would be somewhat as follows :—

Liabilities.	£	*Assets.*	£
London Office	20,000	Cash at Bank	300
		Land and Buildings ..	7,500
		Fixed Plant	9,200
		Loose Plant	3,000
	£20,000		£20,000

When the London Balance Sheet came to be prepared the debit of £20,000 could, if desired, be resolved into its constituent parts. Indeed, this could be done in the London books proper by making a Journal entry debiting accounts opened for the various items and crediting (and thus closing) the "Vienna Factory" Account. But this course is not likely to be adopted. It is simpler to keep one account, which shows at any time how much money there is in Vienna, leaving it to the books there kept to show how the amount is made up.

Now let it be assumed that the Vienna venture grows and prospers, that during the year a further £5,000 is sent out from London, and that the profit earned during the year in Vienna is £3,000. The balance in the London books is £25,000, and this is also the balance of the London Office Account in the Vienna books The Vienna Balance Sheet would now be as follows :—

Liabilities.	£	*Assets.*	£
Sundry Creditors	5,000	Cash	500
London Office	25,000	Debtors	7,000
Profit and Loss Account ..	3,000	Stock	6,420
		Land and Buildings ..	7,500
		Fixed Plant	8,280
		Loose Plant	3,300
	£33,000		£33,000

How is the Profit and Loss Account balance to be disposed of? Like all profit, it is the amount by which the net assets have increased during the year, and this growth belongs to London, just as much as if London had sent out £3,000 to Vienna. It is, therefore, disposed of in the Vienna books by transferring it from the credit of Profit and Loss Account to that of the London Office Account, which will then stand at £28,000. In London the Vienna Factory Account is debited and the general Profit and Loss Account credited with £3,000, so that the former account likewise stands at £28,000. Note that the London Balance Sheet, in its final form, instead of showing one sum of £28,000 as an asset, would probably incorporate the Vienna liabilities of £5,000 and assets of £33,000.

The above illustration is that of a particularly simple case, because the complete independence of the branch in buying and selling is assumed. Broadly, it may be said that the further away the branch the simpler are the bookkeeping problems involved, for of necessity a distant branch must be left to go its own way in the daily affairs of business—the Head Office can control policy, but not details Yet even in a case so completely independent as that assumed above, matters will not go quite smoothly. The London office is pretty certain to have done some buying (say of Plant) for Vienna. When the account is paid in London the amount is debited to Vienna as though it were cash remitted, and Vienna, as the result of an advice, credits London and debits Plant Account. On the other hand, an ordinary trade account for goods supplied by Vienna to an English customer may be paid by that customer in London. In that case London credits Vienna as though Vienna had remitted cash, and Vienna debits London and credits its customer.

Now take the more complicated case of a business in London which has a branch in Manchester, where the arrangement is that the goods bought for Manchester, though delivered there, are yet ordered from, and invoiced to, London. Assume also that all cash taken in Manchester is banked intact for immediate remittance by the Manchester Bank to the credit of the Company's account in London. Under such an arrangement the Bought Ledger is kept in London, but the Sold Ledger is necessarily kept in Manchester (London may have a duplicate of it, but the Manchester one is the original). Let it be assumed, too, that the London office is not a mere registered office, but that a business is actually carried on there.

In such circumstances perhaps no two people would design books in exactly the same way, and therefore the following suggestions, while certainly achieving the wished-for result, are no more than suggestions to show the student how bookkeeping principles may be applied.

Dealing with the London books, the whole affair could be managed through one account, so far as the transactions between the two places are concerned, but these transactions are so numerous that it is much simpler to have several accounts, which at the close of each year are brought together in one account called "Manchester Branch, Capital Account." Assume that the branch is that of a retail business, that it has been equipped and stocked, and that for this purpose £10,000 has been expended, this sum having been sent to Manchester and debited to this Capital Account. The year, therefore, opens with this balance at its debit.

The purchases go through the London books, either by means of an Invoice Book kept specially for Manchester purchases, or, more likely, by means of a special column in the General Invoice

Book. The totals are debited to "Manchester Branch, Purchases Account." Say they are £20,000.

All the cash paid to the Manchester bank for remittance to London is entered in the London Cash Book as received from Manchester, and posted to the credit of a "Manchester Current Account." Say the amount is £18,000.

As Manchester cannot get on without incurring expenses (which are assumed to be paid there), the money is found by remittances to the credit of a Bank Account operated on by the Manchester manager. These go through the London Cash Book, and are debited to a "Manchester Expenses Account." Call the amount £3,000. (Instead of this method being adopted, the Manchester manager might send each week a statement showing the amounts he had to pay, and receive a cheque for the exact amount.)

Turning to the Manchester books, these have, in the Nominal Ledger, a "London Capital Account" with £10,000 at its credit (balanced by, say, £7,000 at the debit of a Stock Account as the value of the stock at the beginning of the year, and £3,000 at the debit of a Fixtures and Fittings Account), a London Purchases Account with £20,000 at its credit, a London Current Account with £18,000 at its debit, and a London Expenses Account with £3,000 at its credit. For the purpose of the sales there is a Day Book and a Sold Ledger, kept as may be found most convenient as to form, but in principle the same as the corresponding books of any other business. There is also a Nominal Ledger (including in this term the Private Ledger, if one is kept). As to the Cash Book, instead of there being one kept in the ordinary way, it will be found convenient to have two—one for receipts from customers, and one for expenses. As all receipts from customers are banked specifically for the credit of London, the quickest and clearest way to deal with them is to enter them in a Cash Book kept for the purpose—to keep the receipts in one column, and to throw the total, up to the point at which they are banked, into an outer column. The mere throwing out of this amount constitutes the record of the payment into bank, though if necessary a column for the date of such payment might be added. Of course, discounts would have their own column as in any ordinary Cash Book. The amounts in the outer column need not be posted individually to the debit of the London Current Account. It is sufficient to post them, say, monthly. The following ruling meets the case. It will be seen that each page contains both the debits and the credits, the second column standing for receipts and the third for payments :—

JANUARY.

Day	Name	Led. Fo.	Discount			Cash Received			Paid to Bank		
			£	s	d	£	s	d	£	s	d
1	T. Cooper		0	10	9	22	1	0			
	B. Smith		0	0	7	14	2	0			
2	F. Armitage		0	8	6	16	1	9			
									52	4	9
	D. Robinson		0	10	7	10	9	0			
	R. Thompson		0	0	3	2	6	0			
									12	15	0

The second Cash Book will deal with the disposal of the amounts received from London for expenses. These amounts constitute the sole entries on the debit side, while the payments are entered and posted to the Nominal Ledger in the ordinary way.

The Profit and Loss Account in the Manchester books, greatly compressed, may run as follows :—

PROFIT AND LOSS ACCOUNT (in the Manchester Books).

	£		£
To Stock at beginning of year	7,000	By Sales	25,000
,, Purchases	20,000	,, Stock at end of year ..	7,500
,, Expenses	2,950		
,, Balance, Profit ..	2,550		
	£32.500		£32,500

The profit is disposed of by being credited to the London Capital Account, which at the end of the year will be as follows :—

LONDON CAPITAL ACCOUNT (in the Manchester Books).

			£				£
Dec. 31	To Current A/c.		18,000	Jan. 1	By Balance	..	10,000
	,, Balance	..	17,550		,, Purchases A/c		20,000
				Dec. 31	,, Expenses A/c		3,000
					,, Profit and Loss A/c. Profit for year	..	2,550
			£35.550				£35,550

This balance of £17,550 necessarily forms an item in the Manchester Balance Sheet. This Balance Sheet is as follows:—

BALANCE SHEET.

Liabilities.	£	*Assets.*	£
London Office	17,550	Cash at Bank	50
		Debtors	7,000
		Stock	7,500
		Fixtures and Fittings ..	3,000
	£17,550		£17,550

The above accounts are given in outline only. They make no provision for depreciation, discount, bad debts, etc. Moreover, the circumstances would never be so simple as in the illustration. For instance, Manchester could not help incurring some liabilities direct, certainly for expenses, and possibly for stock. And the buying in London might not be wholly for stock purposes, as is assumed.

Reverting to the London books, there is in them a Manchester Capital Account. This, when the Manchester accounts have been received, will contain exactly the same items as the corresponding account in the Manchester books, but on the opposite side. The entry for the profit as shown by the Manchester books is obtained by debiting the Manchester Capital Account and crediting the General Profit and Loss Account of the business.

The net result of all these transactions is that two sets of books, kept independently of one another, are brought into harmony; that the whole of the transactions affecting Manchester are correctly recorded—some in London and some in Manchester; and that the true net profit of the Manchester business finds its proper destination in the General Profit and Loss Account of the London books.

The accounts kept may seem complicated, and so, to some extent, they are. But it is necessary to remember that simplification has limits, and that, if transactions are inherently complex, the accounts recording them must also be complex.

The above illustrations are probably sufficiently full to show clearly the principle involved; and this principle, if thoroughly grasped, can be applied to any given circumstances.

FOREIGN CURRENCY.

As it is not practicable to have different currencies in one set of books, it is necessary, where they have to be dealt with, to treat them in one of two ways—either the amounts must, for the purpose of the bookkeeping, be turned into sterling, or a separate set of books must be kept in the particular currency required. (Note that this point is discussed, as every other point touched on has been discussed, primarily from the technical bookkeeping point of view.)

Currency problems in bookkeeping arise in various ways. (1) A business doing a home trade may occasionally execute orders for foreign customers, dealing with them direct. (2) A business may have a regular trade with some foreign country, selling in the currency of that country and receiving payment in it—probably through an account with a foreign bank opened for the purpose. Or (3) a business may have a foreign branch.

In the first case, that of a business which occasionally deals direct with foreign firms, the currency problem hardly arises at all. If the goods are invoiced in sterling there is no problem at that stage, nor is there at a later stage, if, as may happen, the payment is made by a sterling cheque on the London office of a foreign bank. If the remittance comes in foreign currency, the sterling amount produced by cashing it is entered as a receipt in the ordinary way, and the difference (which there is sure to be) is treated as a discount. It may happen, however, that the goods are invoiced in the foreign currency. In such a case this currency amount is entered as a memorandum in the Day Book, and the sterling amount, at a standard rate of exchange, is entered in the cash column.

If a business has a regular foreign trade with some particular country, and particularly if this trade be in sales of relatively small value, it becomes necessary to make special arrangements for doing this trade. Indeed, apart from convenience to the selling business, the customers demand it. A Frenchman who has bought a thousand pounds' worth of machinery from an English firm is doubtless willing, as the transaction is an occasional one, to take some trouble about remitting; but another Frenchman who has bought a few pounds worth of lace from the agent of a Nottingham house must be granted the same facilities for payment as he would have if he bought direct from a French house. Hence the common arrangement by which British houses doing such a trade invoice their goods in the foreign (say, French) currency, and arrange that these goods may be paid for by the customer just as he pays his own countrymen. The cheque, or bill, goes to an account which the exporters have opened with a French bank in France, probably through an agent there, who collects the accounts, advising his principals as to the amounts paid.

Trade conducted thus involves the keeping by the exporting firm of a set of books in French currency. The books required are Day Book, Sold Ledger, and Cash Book. Strictly, there should be a Nominal Ledger also, but, as the Nominal Accounts are very few, they can have a small portion of the Sold Ledger reserved for them. They are kept just as sterling books are kept, and are balanced (without reference to the sterling books) in the ordinary way.

So far there are no special problems. It is as easy to keep books in French currency as in British. Indeed it is easier—centimes are turned into francs more easily than pence into shillings, and shillings into pounds. Such difficulty as there is arises in the incorporation of the French trading figures in the English books.

If it be assumed that the foreign trade begins with the financial year of the exporting firm, the only point at which the two sets of books touch during the year (*i.e.*, until the time for balancing is reached) is likely to be when a sum is withdrawn from the account with the French bank. (This account, being for receipts only, is always in credit, and as the balance grows, cheques are drawn on it, and paid into the firm's ordinary banking account. Or the bank may have instructions to remit when the balance reaches a certain sum.) As regards the French books, this is entered in the Cash Book as a payment to an account called "General Business, Current Account," or some such name. In the English books the amount in sterling produced by the cheque in francs is entered in the Cash Book and posted to the credit of "French Business, Current Account." At the end of the year all the nominal accounts in the French books are written off to a Capital Account —if necessary, they can go through a Profit and Loss Account. The balance of this Capital Account therefore represents the French assets—*i.e.*, book debts and cash in bank. In the English books corresponding entries are made in the Journal, debits in the French books becoming credits in the English ones, and *vice versa*. Also, instead of being in francs they are in sterling at the agreed rate of exchange. The whole procedure is similar to that set forth in the preceding section in connection with the London business having a Manchester branch, for the French books are in effect branch books, though they are kept in the same office as the English ones. The only difference is that what is expressed in one set of books as £1 is expressed in the other as fr. 25.25, or whatever is taken as the value of £1.

The result of these entries is that the debit balance of the French Capital Account in the English books stands at the value in sterling of the number of francs at the credit of the Capital Account in the French books. This debit balance in the English books, therefore, represents the French assets, which would (or could) be set out specifically in the Balance Sheet of the business.

The third instance of dealing with foreign currency in accounts is that of a business having a foreign branch—one which is free to manage its own affairs, as in the illustration of the business in Vienna given in the preceding section of this chapter. In such a case the complications affecting the balancing books *need* only be trifling, though they may be considerable.

When a business establishes a foreign branch the assets abroad are subject to the ordinary diminution of value by wear and tear and the like, to which the English assets are subject. But, in addition, they are subject to the fluctuations of the rate of exchange. The extreme case of Indian currency illustrates the point. Once, the rupee was worth two shillings; now it is worth about one shilling and fourpence—*i.e.*, it has lost about a third of its one-time value. Assume a company which, when the rupee was worth two shillings, raised in this country a capital of £100,000 which it remitted to India where it was invested in trade. Such a concern may be very prosperous, but it is obvious that when the rupee is depreciated by one-third, what cost the company £100,000 is worth only about £67,000. A company formed at such a time with a capital of £67,000 could acquire assets in India equal in value to those which had cost the older concern half as much again. If it were desired by this older concern to write off what is, of course, a real loss, the consequences might be serious; but as a matter of bookkeeping it is the simplest thing to do, for all that is required is to depreciate the Indian Capital Account in the London books by one-third. A single Journal entry suffices.

Such a heavy loss on exchange does not arise where the foreign country has a gold standard. The fluctuations in exchange are within narrow limits, and for the purpose of periodical Balance Sheets it may be decided to disregard them, assuming one normal rate. In such a case, if no cash ever passed between the Head Office and the branch, there would never be any difficulty. But there are certain to be such transactions during the year, and they must be made at the rate of exchange of the day, which is all but certain not to be the normal rate which the business has assumed for its own purposes. Thus, to refer again to the Vienna illustration. The London office may have decided that £1 is to be considered as equal, for the purposes of their Balance Sheet, to fl.24.10. But, if Vienna remits money to London, and has to pay fl.24.12 for every £1 which it purchases, there is a loss on the transaction, and London must debit its Exchange Account (an account which goes to the Profit and Loss Account) with this loss, crediting the "Vienna Branch Account." In this way the Vienna Branch Account always agrees with the

London Office Account in the Vienna books, at the normal rate of exchange.

This is the only way in which it is absolutely necessary for the English books to take cognisance of currency fluctuations. But, if the London office decided at each stocktaking to take the Vienna assets at the rate of exchange of the day, it would be necessary to make a further entry, similar in character to the writing down of the Indian assets in the case referred to above.

As with Branch Accounts, so with Foreign Currency. Any intelligent student of bookkeeping, armed with a general idea of how the thing can be done, can deal with any transactions if he bring to his work an ability to set the problem clearly before himself, and to resolve it into its constituent parts.

CHAPTER XVI.

SECTIONAL BALANCING.

A SET of books is primarily designed to balance as a whole. But where the transactions are very numerous there is an obvious advantage in adopting some method by which portions of the books can be balanced by themselves. If no such system be adopted, an error can only be found by the process of checking—and, if necessary, re-checking—all the books; but, if the error can be shown to exist in a particular section of the books, only that section need be examined.

Such a division into sections it is always possible, and sometimes easy, to make. Let it be assumed that it is desired to be able to test the accuracy of the Sold Ledgers apart from the other books. The total which has gone to the debit of customers in this Ledger is easy to find, for it is either the total of the Day Book or this total with certain small adjustments. The reason why the Sold Ledger debits may not exactly correspond to the Day Book entries is that some Day Book items may have gone to a Bought Ledger Account and some Invoice Book items to a Sold Ledger Account. If so, they must be noted;

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but, where sectional balancing is in vogue, there is generally a rigid rule confining the Day Book to the Sold Ledger and the Invoice Book to the Bought Ledger. The Returned Sales Book follows, of course, the lines of the Day Book.

The other great factor in the Sold Ledger is the cash, with the corresponding discount. Where it is the practice to keep the receipts in a separate Cash Book division is easy, for this book can be reserved for Sold Ledger accounts, all other receipts going into the main Cash Book. But where there is only one Cash Book it is necessary to extract from the debit side all the items which go to the Sold Ledger, and this is best done by an analysis column. There must be a similar column on the credit side of the Cash Book to catch the few payments which have gone to the Sold Ledger. These arrangements probably result in picking up all the items comprising the Sold Ledger except any there may be in the Journal, and these must be noted. Care must be taken to make any transfer between the Sold and other Ledgers by means of a Journal entry, so as to preserve a record of it.

The following is a ruling of a Cash Book (of a business where only one Cash Book is kept), so arranged as to provide for an analysis of the entries passing through it, and for balancing the Ledgers separately :—

DEBIT SIDE.

Date	Details	Ledger Folio	Discount	Cash	Bank	Bought Ledger	Sold Ledger	Nominal and Private Ledgers	Contras
			£ s d	£ s d	£ s d	£ s d	£ s d	£ s d	£ s d
Feb. 1	W. Statham	..	4 5	8 12 9	..	..	8 17 2		
	J. Topham	..	6 7	12 16 2	..	..	13 2 9		
	W. Longson	..	9 0	17 12 2	..	..	18 1 2		
	Cash	..	..	..	30 0 0	..	..	..	30 0 0
3	R. Scott	..	3 4	6 12 0	..	..	6 15 4		
	J. Greenwood	..	5 1	9 17 7	..	..	10 2 8		
	Cash Sales	..	..	15 0	..	..	..	15 0	

CREDIT SIDE.

Date	Details	Ledger Folio	Discount	Cash	Bank	Bought Ledger	Sold Ledger	Nominal and Private Ledgers	Contras
			£ s d	£ s d	£ s d	£ s d	£ s d	£ s d	£ s d
Feb. 1	J. Hulse	..	1 2 6	..	43 19 6	45 2 0			
	Hancock, Wakefield & Co.	..	13 7	..	26 9 7	27 3 2			
	G. Stanton	..	9 5	..	18 6 7	18 16 0			
	Wages	..	..	113 2 6	..	..	..	113 2 6	
	Petty Cash	..	..	6 17 6	..	..	..	6 17 6	
	Bank	..	..	30 0 0	..	..	..	..	30 0 0
	A.B. Drawing Account	..	..	..	10 0 0	..	..	10 0 0	

It will be noticed that, for the purpose of this analysis, the cash and discount are treated as one. In this particular form every entry in the book is placed in an analysis column, and this is the safest plan to adopt. But as on the debit side the bulk of the items go to the Sold Ledger, it is possible to omit the column for that Ledger, and to arrive at the total by deduction—by taking from the total of the Discount, Cash, and Bank columns the total sums which have gone to the Bought and Nominal and Private Ledgers, and the contras. Similarly, on the credit side, the Bought Ledger column may be omitted and the total arrived at in a similar way.

The constituent parts of the Sold Ledger being thus built up, the balance so obtained should agree with the aggregate of the individual Sold Ledger balances, or rather, a figure is obtained with which those balances should agree. The statement bringing out this figure is generally recorded in permanent form in the Nominal Ledger. But it is not a true Ledger Account, it is only a memorandum producing a result which may be exceedingly useful, but is not an integral part of the bookkeeping.

The Bought and Nominal Ledgers can, of course, be similarly treated.

Every practising accountant finds it his business on occasion to produce a Profit and Loss

Account from books which have been kept without any intelligible system and have never been balanced. If there is no Nominal Ledger, he must make one in some form, if it is only in columns on loose sheets of foolscap. This work, and the checking which is a necessary part of the task as a whole, virtually turns the books into double-entry ones, and can be very easily arranged to make the Ledgers balance sectionally.

The possibility of applying checking to sectional balancing is very well worked out in a book published in 1897 by Mr. (now Sir John) Craggs, called "Heavy Trial Balances Made Easy." The method, with some slight modifications, has been used by the writer in his office for many years with most satisfactory results.

The subject of sectional balancing is much too large to be treated exhaustively here, but it is desirable to refer to it because of its relation to the principle underlying modern bookkeeping.

COMPANY AND PARTNERSHIP BOOKKEEPING.

So far as pure business operations are concerned, there is nothing in the bookkeeping of a limited company or a partnership to differentiate it from any other kind of bookkeeping. It is only when those accounts which are usually kept in the Private Ledger are reached that the difference shows itself. The word "capital," which to an individual trader means the surplus of assets over liabilities at any time, has a very specialised meaning in the case of a company; and this is also true, though in a less degree, of the word in connection with a partnership. This entails the keeping of some additional Ledger Accounts. But the general principles of debit and credit, real and nominal, are not altered in any way. A dissertation on the distinctive features of Company and Partnership Accounts is really a dissertation on a branch of company and partnership law, and lies outside the scope of this work.

DEPARTMENTAL ACCOUNTS.

Departmental Accounts might be thought at first sight to have some resemblance to Branch Accounts, but the resemblance is only superficial. The problem of Branch Accounts is to keep two sets of books, in different places, in correspondence with each other, while Departmental Accounts are accounts kept substantially in the ordinary way, but with a particular subdivision of the nominal accounts. All keeping of nominal accounts, involving, say, the separation of wages from purchases, is a kind of departmentalising, and a division into departments is a mere extension of this principle. There are, therefore, no special features to be noticed, viewing the matter as a problem in bookkeeping.

Division into departments varies in different concerns. In some, it does not go beyond purchases and sales. In others, the division is carried through every item of expense. In the former case the division is probably based on indisputable facts, but in the other it is certainly, to some extent, based on estimate. If it lies with a bookkeeper to make the division he should distinguish between the two cases. But this is rather a question of the wording of the Profit and Loss Account than of the keeping of the accounts which lead up to it.

COST ACCOUNTS.

The subject of Cost Accounts is one large enough to have a literature of its own. Nor does it need to be dwelt upon here; for though the costing books must be dependent upon the commercial ones, the latter can go their way whatever the costing system, or even if—as often is the case—there is no costing system worthy of the name. Cost books may be so kept, and, indeed, ought to be so kept, as to have a balancing system of their own, and they may be kept either in terms of money or of material, or of both. In such cases, the ordinary rules of bookkeeping apply to them as independent units. But the commercial books are the ultimate test. If the Profit and Loss Account shows a manufacturer that (fluctuations in stock being taken into account) he has spent in material in any year £20,000, then he *has* spent that amount among his various jobs, and if the individual items of cost which his cost books or cards may show do not amount to that sum, they are wrong. Similarly, if a percentage is added to the prime cost of each job which purports to cover the general expenses, this percentage cannot do more than agree with the actual expenses, as shown by the Profit and Loss Account; if it does not do so, it is the percentage, not the Profit and Loss Account, which is wrong. A business is run for profit, and profit is the balance of the Profit and Loss Account. This balance is, as a matter of bookkeeping, entirely unaffected by the existence, or non-existence, of Cost Accounts. Of course, the existence of a proper system of costing may be necessary to that economical production which is a condition of profit earning, but that is another matter.

SUSPENSE ACCOUNTS.

In the majority of cases the destination of the entries in the Day Book, Cash Book, &c., is quite well known. But from time to time there arise cases where, for one reason or another, the destination is not certain. For instance, a firm may make a payment of, say, £100, in order to obtain an option on a patent right. If the option is exercised, this payment is treated as a part of the cost of obtaining the right, while, if it is not so exercised, the amount is written-off to Profit and Loss Account as a loss. The amount might be left unposted in the Cash Book till its destination was known, but this is a dangerous practice, as it might be overlooked, and so cause trouble. Therefore it is posted to the debit of a Suspense Account. The Suspense Account is a temporary resting place for such items as the above, and the fact that there is any item in it is in effect a notice that there is an entry in the books which requires to be looked into. Consequently the Suspense Account balance, if there happens to be one, requires special attention at each stocktaking.

Sometimes the Suspense Account is used for the special purpose of obtaining a temporary resting place in the Ledger for amounts accrued at stocktaking. This use has already been briefly referred to on p. 69 in connection with the making of the entries which immediately precede the preparation of a Balance Sheet. The process involving the use of the Suspense Account is not a necessary one, but, as it is not uncommon, it is well to refer to it.

In the analysed Trial Balance set forth on p. 74, there is a note of certain amounts accrued in respect of expenses—amounts relating to accounts wherein no personal Bought Ledger Accounts are kept. Those, in the illustration there given, were dealt with by being brought down as credit balances in their respective nominal accounts, which is a method at once easy and clear. But if it was desired to put them into a Suspense Account, the following Journal entry would have to be made:—

		£ s d	£ s d
1911			
Dec. 31	SUNDRIES. *Dr.*		
	To SUSPENSE Account		137 17 7
	For amounts due or accrued at date.		
	Customers' Discount	74 6 4	
	Salaries	6 15 3	
	Rent, Rates, Taxes and Insurance	12 18 9	
	Carriage	22 17 3	
	Legal and Professional Costs	21 0 0	

(The word "sundries" used above has no mystic significance. It is employed where a Journal entry deals with more than one account on a side, and is really short for "Sundry Accounts set forth below.")

The posting of this entry has the effect of making the nominal accounts show their proper debits for the year, and also of showing the proper liability in respect of them through the Suspense Account, which is a "real" account.

This particular kind of Suspense Account, however, is only opened to be closed, and this closing is done by reversing the entry on 1st January as follows:—

			£	s	d	£	s	d
1912								
Jan. 1.	SUSPENSE ACCOUNT.	*Dr.*	137	17	7			
	To SUNDRIES. *For amounts due or accrued at 31st December 1911 written back.*							
	Customers' Discount					74	6	4
	Salaries					6	15	3
	Rent, Rates, Taxes and Insurance					12	18	9
	Carriage					22	17	3
	Legal and Professional Costs					21	0	0

The nominal accounts, therefore, begin the new year with a credit balance in each case, this balance representing the liability at 1st January, which forms a proper deduction from subsequent payments, for these payments include this liability.

The above illustration deals with liabilities, but the same process, with the sides reversed, may be applied to assets.

STOCK ACCOUNTS.

This section does not deal with the keeping of Stock Accounts as a part of a system of Costing, but with the more technical question of the keeping of the Stock Account in the commercial books, and the method of treating this account at a stocktaking.

The following is the method (a common one) adopted in the illustration given in Chapters XII and XIII. The year begins with (*inter alia*) a Stock Account which has at its debit the value of the stock on 1st January—£2,175 12s. 6d. This account is unaltered during the year, but on 31st December it is closed by the transfer of the amount to the debit of the Profit and Loss Account. At the same time an entry is made crediting the Profit and Loss Account and debiting the Stock Account with the value of the new stock—£2,227 9s. 5d. It will be seen that the stock has increased during the year by £51 16s. 11d., and that the net result of the two entries is to credit Profit and Loss Account and debit Stock Account with that sum. The only advantage of making the two entries for the larger amounts instead of one entry for the difference, is that they show the whole transaction quite clearly, which is always a good thing to do.

There is this peculiarity about the Stock Account, that while all the other accounts may be said to move during the year as the business moves, the Stock Account remains fixed at an amount which is certainly not the value of the stock at any other time than the moment at which it is taken. It was not the older custom (and on the Continent it is not the modern custom) to have separate accounts for Stock, Purchases, and Sales. One account, called "Goods Account," took them all. This account began in any year with the Stock at the beginning, the Purchases during the year were debited to it, and the Sales credited. At the end of the year the account showed a balance, which would have been the amount of the stock had everything bought been sold at the same price, but which, under normal circumstances, was smaller than the actual stock, by reason of the profit made on each sale. The account was therefore debited with the amount required to bring the balance up to the ascertained value of the stock, and the amount so debited was credited to the Profit and Loss Account. The then balance of the Goods Account (being the value of the stock) was brought down to form the commencement of the account for the next year.

If the books illustrated in Chapters XII and XIII had been kept in such a fashion, the Profit and Loss Account on page 89 would have begun with the balance of the Goods Account, which would have been the Gross Profit of £3,085 8s. 11d.

A Stock Account on these lines is theoretically correct, but it has practical disadvantages, being of little value for statistical purposes. As actually kept, it would not show the Purchases and Sales each in one sum. Assuming that the Invoice Book and Day Book were ruled off monthly, both Purchases and Sales would appear in twelve monthly totals—indeed in twenty-four, for there would be twelve entries of Purchases on the debit side, and twelve entries for returned Purchases on the credit side, and the sales would be similarly split up. It is therefore convenient to keep separate accounts for Stock, Purchases, and Sales, and to bring them together in the Profit and Loss Account, which, however, may be divided into two parts, the first part being the Goods Account summarised as above, and now generally known as the "Trading Account." For the particular business illustrated, the Goods Account is the Trading Account referred to on page 89.

Another practical objection to a Goods Account is that in many businesses, including all manufacturing ones, it is not easy to say what are "Purchases" in the strict sense of the word. It is generally most useful to analyse fully all purchases, of whatever sort, by means of separate Ledger Accounts, and at stocktaking to make such a grouping of them as is convenient and useful. In the illustration given it will be noticed that the carriage of goods bought has been treated as a portion of the cost of goods bought, which it properly is.

This separation of accounts involves the isolation of the Stock Account. But though it stands unaltered throughout the year, it must be read in conjunction with the accounts of the Purchases and Sales. The movements in these two accounts are in fact stock movements, as is clearly seen when the Profit and Loss Account is drawn out, and all the accounts relating to the year's working are brought together.

CHAPTER XVII.

CONCLUSION.

THE foregoing chapters are an attempt to set forth clearly the principles which are implied in all good modern bookkeeping, and the application of these principles in some cases which are apt to be met with in every set of books. Throughout, an endeavour has been made to adhere strictly to the technical side of bookkeeping, because it is that, and that only, with which the book professes to deal. A competent counting-house staff must be able to do much more than keep books properly. It is, for instance, at least as important that the entries in the Journals should be correct as that they should be correctly posted into the Ledger. A single Day Book entry may imply a great deal of work on the part of the staff before it is correctly obtained; yet, to the bookkeeper, as such, it is merely one amount to be correctly included in the Day Book addition and correctly posted. This is especially true in large manufacturing concerns, where a contract may be for thousands of pounds, and may involve the most elaborate costing details and calculations. Yet, to the bookkeeper, it all boils down to a single item. Indeed, the keeping of the books proper—of those books which, taken together, form the balancing set—is often (perhaps usually) a comparatively small part of the counting-house work. It is, however, a part which can be dealt with by itself—hence this book. And it may not be amiss to add that where books are thoroughly well kept, and regularly balanced, one may expect to find—and usually does find—that the rest of the office work is well done. If one is satisfied that a certain man is exceedingly particular about the cut of his coat, one may assume that he is not wearing baggy trousers!

Good bookkeeping, then, is an outward and visible sign of system in a counting-house, and for that reason alone is valuable. But it has also a direct value in preventing losses caused by mistakes and fraud. Mistakes may, and do, occur through carelessness; but even where great care is taken there is certain to be some mistake made in the course of a long year's work. The proof is simple, and is to be found by asking any keeper of a considerable set of books whether his Trial Balance comes out rightly at the first attempt. How careful soever he may be, it will be found that in nine, and probably in ten, years out of ten he has had a difference which he has been obliged to search for. It is true that the difference, when found, may prove to be of such a nature as not to involve the firm in any pecuniary loss; but that is a mere chance, and makes a mistake none the less a mistake.

Not only does good bookkeeping minimise mistakes due to carelessness; it is a valuable agent in the prevention of fraud. There are people who maintain that if a man wants to be dishonest, dishonest he will be, whatever system of bookkeeping be employed. It would be equally true to say that, if a man wants to break into a house, locks and bolts will not stop him. But the people who say so presumably lock their doors and fasten their windows o'nights. True it is that, if a man is determined at all costs to steal, he will not stick at trifles—it is a condition of being prepared to steal at all costs that you are *not* stopped by trifles. But the fact is that the number of such desperate fellows is very limited. Between them on the one hand, and the incorruptibly honest on the other, stand a great number of people who would be dishonest in certain circumstances, but are kept honest because these circumstances do not arise. There is many a man who could not be trusted with uncounted money who could be depended on not to break into a safe. In like manner there are people who could not be trusted to receive money, if they knew that they could keep it for their own purposes by making a simply entry most unlikely to be detected, who would deal honestly with it if they knew that any irregular dealing would certainly be detected at, or soon after, the next stocktaking.

Double-entry bookkeeping, rigidly carried out, does not directly prevent fraud, but, by making continued immunity from detection almost impossible, it makes fraud too dangerous for the average man to attempt. It acts very much as the general system of law and police acts in daily life. It is a very easy thing for one person to injure seriously, or even to kill another, and the reason that it is not done more frequently than is actually the case is not its physical impossiblity, but the reasonable certainty of detection and punishment. Thus, in a counting-house, especially in one belonging to a business in which the staff are well treated, the true security in the honesty of the staff—over and above the most important one of the innate honesty of its members—lies in the knowledge that any departure from honesty implies speedy detection, and that detection implies dismissal without a "character." It is this security which is supplied by system in an office, culminating in well-kept books periodically balanced.

Carelessness and fraud, however, are the exception in any ordinary business, and it is not in connection with them that the principal advantage of good bookkeeping is to be found. The counting-house is an integral part of the machine engaged in turning out the wares supplied by a concern—or the profit earned by it, according to the point of view taken. It is essential to the smooth working of the machine as a whole that full and accurate statistical information shall be available when wanted. What purchases have been made, and from whom; what payments have been made in respect of them; what goods have been sold and to whom; what amounts are owing by customers; what expenses have been incurred; what profit the business is earning—this information, and much more, is essential to efficient management, and is obtainable only if the counting-house is considered as being as much a profit-earning department of a business as any other. And this it truly is, for any department which cannot be done without is a profit-earning one, even though, taken by itself, it brings in no specific return. When the counting-house is well staffed and well equipped, the information which it contains is quickly forthcoming, so that the utmost use can be made of it. It seems almost unnecessary to insist on the advantage of good bookkeeping and office management, yet there are many people who spend time and money unsparingly in keeping the mechanical part of their business up to date who are content to let their counting-house look after itself and go on its way employing methods long superseded. The details of office management are many and varied, and do not come within the province of this work. But the most important detail of all is that the financial books, which are the records on which a business takes its stand against the world, should be well and accurately kept. They will not be so kept, unless the person responsible for them apprehends the principle on which all good book-keeping is based—that principle which is known to the commercial world as "Double Entry."

R. L. Stevenson was no man of business, but he hit upon a truth, valuable in business as in other departments of life, when he wrote—

> "You also scan your life's horizon
> For all that you can clap your eyes on."

For even if one's horizon be bounded by the walls of an office, yet it is well to scan it carefully, and to note all that is to be seen within its limits. That way lies success.

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(*See* **Vade Mecum**, p. 40.)

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