

Rectification of Error

By

GCA Team



Errors - The Concept

- ▶ Errors are unintentional mistakes made by the accountant/book-keeper while recording transactions in the books of accounts.
- ▶ In the process of accounting, a trial balance is prepared which only reflects the arithmetical accuracy but doesnot guarantee the absence of any errors in the books.
- ▶ In such a case if trial balance agrees there may or may not be errors in the books but if trail balance doesnot agree it clearly indicates some kind of error(s) in the books of accounts.

Types of Accounting Errors

Error not affecting trail
balance agreement

Error affecting trail
balance agreement

Errors not affecting trail balance agreement

Errors of commission

Errors of principle

Errors of original entry

Errors of omission

Compensating errors

Complete reversal of entries

Errors affecting trail balance agreement

Suspense
account

Debit Credit Rules (American Version)

Journal Entry Debit / Credit Chart		
Account Type	Debits	Credits
Income	Decrease	Increase
Expense	Increase	Decrease
Equity	Decrease	Increase
Asset	Increase	Decrease
Liability	Decrease	Increase

Debit Credit Rules (British Version)

Rules of Double Entry System

Accounts	Rules
Personal	<ul style="list-style-type: none">• Debit the receiver• Credit the giver
Real	<ul style="list-style-type: none">• Debit what comes in• Credit what goes out
Nominal	<ul style="list-style-type: none">• Debit all expenses and losses• Credit all incomes and gains

Errors not affecting trail balance agreement

Errors of commission

The correct amount is entered but in a wrong personal account

A purchase of goods from Fankaar Limited has been posted to the credit side of Dramabaz Limited account in error, amounting to PKR 500. The correcting entries should be:

Original entry:

- ▶ Dr Purchase 500
- ▶ Cr Fankaar Limited 500

Wrong entry:

- ▶ Dr Purchase 500
- ▶ Cr Dramabaz Limited 500

Rectifying entry:

- ▶ Dr Dramabaz Limited 500
- ▶ Cr Fankaar Limited 500

Errors of Principle

An item is entered in the wrong type of account due to misunderstanding of the nature of the item.

Office equipment purchased for PKR 1,000 in cash has been debited to an office expenses account. The correcting entries should be:

Original entry:

- | | |
|-----------------------|------|
| ▶ Dr Office equipment | 1000 |
| ▶ Cr Cash | 1000 |

Wrong entry:

- | | |
|---------------------|------|
| ▶ Dr Office expense | 1000 |
| ▶ Cr Cash | 1000 |

Rectifying entry:

- | | |
|-----------------------|------|
| ▶ Dr Office equipment | 1000 |
| ▶ Cr Office expense | 1000 |

Errors of Original Entry

Wrong original figure is entered in the journals, and hence posted incorrectly to the accounts.

A payment of PKR 1,200 to a creditor, ABC, has been entered as both a debit and credit as PKR 1,000. The correcting entries should be:

Original entry:

- ▶ Dr ABC 1200
- ▶ Cr Bank 1200

Wrong entry:

- ▶ Dr ABC 1000
- ▶ Cr Cash 1000

Rectifying entry:

- ▶ Dr ABC 200
- ▶ Cr Office expense 200

Errors of Omission

A transaction has been completely omitted from the accounts.

A sale of PKR 400 to Mr. Azeem has been completely omitted from the accounts. The correcting entries should be:

Original entry:

▶ Dr Azeem	400
▶ Cr Sales	400

Wrong entry:

No entry done.

Rectifying entry:

▶ Dr Azeem	400
▶ Cr Sales	400

Compensating Errors

Debit side errors
are equal to
credit side errors.

The purchases account was undercast by PKR 2,200, and the sales account was also undercast by PKR 2,200. The correcting entries should be:

▶ Dr Purchase	2,200
▶ Cr Sales	2,200

Purchases and sales accounts were undercast by \$2,200, now corrected.

Complete Reversal of Entries

The correct amounts
are entered in the
wrong sides of the two
appropriate accounts.

The purchase of goods on credit from Shahid for PKR 60 was entered on the debit side of Shahid account and the credit side of the purchases account. The correcting entries should be:

Original entry:

▶ Dr Purchase	60
▶ Cr Shahid	60

Wrong entry:

▶ Dr Shahid	60
▶ Cr Purchase	60

Rectifying entry:

▶ Dr Purchase (60*2)	120
▶ Cr Shahid (60*2)	120

Errors affecting trail balance agreement

Errors affecting trail balance agreement occurs when:

- ▶ (i) recording transactions in the accounts:
 - ▶ (1) omitting a debit **or** credit entry
 - ▶ (2) posting a wrong amount to one of the accounts
 - ▶ (3) recording an entry on the wrong side
 - ▶ E.g. a debit entry entered as a credit or a credit entry as a debit

- ▶ (ii) Balancing of accounts:
 - Incorrect calculation of a balance
 - ▶ E.g. overcast or undercast
- (iii) Drawing up a trial balance:
 - ▶ (1) omitting a balance from the trial balance
 - ▶ (2) incorrectly posting an amount to the trial balance
 - ▶ (3) incorrectly posting a balance to the wrong side of the trial balance

Suspense Account

When the trial balance does not agree, the amount of the difference is entered in a suspense account.

Existence of suspense account indicates the presence of some error in the books of accounts.

Trial Balance as at 31 December 2015

	PKR	PKR
Total balances extracted	90	100
Suspense account	<u>10</u>	—
	<u>100</u>	<u>100</u>

How To Show a Suspense Account on the Balance Sheet

Debit Balance of the Suspense Account

Balance Sheet

Fixed Assets X

Current Assets X

Suspense Account X

X

Credit Balance of the Suspense Account

Balance Sheet

Capital	X
Long-term Liabilities	X
Current Liabilities	X
Suspense Account	<u>X</u>
	<u>X</u>

Correction of Errors

To correct the errors, students should make correcting entries in the ledger accounts first, and hence clear the suspense accounts.

Example

A credit sale of PKR150 to Mr Shahzad has been omitted from his account.

Original entry:

- | | |
|--------------|-----|
| ▶ Dr Shahzad | 150 |
| ▶ Cr Sales | 150 |

Wrong entry:

- | | |
|------------|-----|
| ▶ Dr | |
| ▶ Cr Sales | 150 |

Correct entry:

- | | |
|---------------|-----|
| ▶ Dr Shahzad | 150 |
| ▶ Cr Suspense | 150 |

Example

A sale to Anwar for PKR 230 was correctly entered in the sales book but entered in Anwar account as PKR 320.

Original entry:

- ▶ Dr Anwar 230
- ▶ Cr Sales 230

Wrong entry:

- ▶ Dr Anwar 320
- ▶ Cr Sales 320

Correct entry:

- ▶ Dr Suspense 90
- ▶ Cr Anwar 90

Example

A credit sale of PKR 97 has been credited to Waleed account.

Original entry:

- ▶ Dr Waleed 97
- ▶ Cr Sales 97

Wrong entry:

- ▶ Dr Waleed 97
- ▶ Cr Sales 97

Correct entry:

- ▶ Dr Waleed 97
- ▶ Cr Suspense 97

Example

Sales day book was overcast by PKR 200.

Correct entry:

▶ Dr Sales	200
▶ Cr Suspense	200

Example

Sales day book was undercast by PKR 100.

Correct entry:

▶ Dr Suspense	100
▶ Cr Sales	100

Correction of Errors

- A **single entry** in the suspense account.
- This occurs when errors are made in extracting balances, rather than in the recording phase.

Example

The total of the sales account of PKR 1,500 has been omitted from the trial balance.

Correct entry:

▶ Dr Suspense	1,500
▶ Cr Sales	100

Example

The total of the sales account of PKR 1,500 has been extracted as PKR 1300 in the trial balance.

Correct entry:

▶ Dr Suspense 200

Example

The total of the sales account of PKR 1,500 has been extracted to the debit column of the trial balance.

Correct entry:

► Dr Suspense (1500*2) 3,000

Correction
effect on
Profit/loss &
Balance Sheet

Trading Account Effect

Sale increase	Cr. Sales	Increase in profit
Opening stock increase	Dr. Stock	Decrease in profit
Purchase increase	Dr. Purchases	Increase in profit
Closing stock increase	Dr. Stock	Increase in profit

Profit & Loss Account
Effect

Income increase	Cr. Income	Increase in profit
Expenses increase	Dr. Expenses	Decrease in profit

Example of errors	Action required on the profit	Action required on the balance sheet
Purchases undercast	Subtract	-
Purchases overcast	Add	-
Sales undercast	Add	-
Sales overcast	Subtract	-
Income undercast	Add	-
Income overcast	Subtract	-
Expenses undercast	Subtract	-
Expenses overcast	Add	-

Example of errors	Action required on the profit	Action required on the balance sheet
Opening stock undervalued	Subtract	-
Opening stock overvalued	Add	-
Closing stock undervalued	Add	Increase closing stock
Closing stock overvalued	Subtract	Decrease closing stock

Example of errors	Action required on the profit	Action required on the balance sheet
Prepayments of expenses omitted	Add	Increase prepayments (current assets)
Accruals of expenses omitted	Subtract	Increase accruals (current liabilities)
Fixed/current assets undervalued	-	Increase fixed/current asset
Liabilities understated	-	Increase liabilities

Thank
You!