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Trial Balance and Rectification of Errors Notes

Meaning of Trial Balance

A trial balance is a statement showing the balances, or total of debits and credits, of all the accounts in the ledger with a view to verify the arithmetical accuracy of posting into the ledger accounts.

“The statement prepared with the help of ledger balances, at the end of the financial year (or at any other date) to find out whether debt total agrees with credit total is called Trial Balance.” – William Pickles

Objectives of Preparing the Trial Balance

The trial balance is prepared to fulfil the following objectives:

1. To ascertain the arithmetical accuracy of the ledger accounts.
2. To help in locating errors.
3. To help in the preparation of the financial statements.

Preparation of Trial Balance:

1. Totals Method: Under this method, the total amount of debit side of each ledger account is put on the debit side of the trial balance and the total amount of credit side of each ledger account is put on the credit side of a trial balance.
2. Balances Method: Under this method, the trial balance is prepared by showing the balances of all ledger accounts and then totalling up the debit and credit columns of the trial balances to assure their correctness.
3. Totals-cum-balance Method: This method is a combination of the totals method and the balances method. Under this method, four columns for amount are prepared. Two columns for writing the debit and credit totals of various 'accounts and two columns for writing the debit and credit balances of these accounts.

Significance of Agreement of Trial Balance

Normally, a tallied 'Trial Balance' stands that debit and credit entries have been made correctly for each transaction. However, the agreement of 'Trial Balance' only proves, to a certain extent, that the posting is arithmetically correct, but it does not guarantee that there is no error compelled in the accounting records.

Classification of Errors:

1. Errors of Commission: Errors caused due to wrong recording of a transaction, wrong totalling, wrong casting, wrong balancing etc.

2. Errors of Omission: The errors of omission may be committed at the time of recording the transactions in the books of original entry or while posting to the ledger. It is caused due to omission of recording a transaction entirely or partly in the books of accounts.
3. Errors of Principle: Errors arising due to the wrong classification of receipts and payments between revenue and capital receipts and revenue and capital expenditure.
4. Compensating Errors: Two or more errors committed in such a way that nullifies the effect of each other on the debits and credits.

Searching of Errors:

If the trial balance does not tally, it is a clear indication that at least one error has occurred. The error or errors needs to be located and corrected before preparing the financial statements.

Rectification of Errors:

From the point of view of rectification, the errors may be classified into the following two categories:

- (a) Errors that do not affect the trial balance.
- (b) Errors that affect the trial balance.

This distinction is relevant because the errors which do not affect the trial balance usually take place in two accounts in such a manner that it can be easily rectified through a journal entry whereas the errors which affect the trial balance usually affect one account and a journal entry is not possible for rectification unless a suspense account has been opened.

Suspense Account:

Sometimes, in spite of best efforts, all the errors are not located and the trial balance does not tally. In such a situation, to avoid the delay in the preparation of final accounts, the difference in the Trial Balance is placed to a newly opened account known as 'Suspense Account' and the trial balance tallies.

When all the errors are located and rectified the suspense account stands disposed of.
