

Financial Accounting
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Lecture – 45
4.1 Introduction to Trial Balance

In this video, I am going to introduce you to the statement called Trial Balance which is the third step in the process of accounting cycle.

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4.1.1 What is Trial Balance?

- It's a statement of account balances

Handwritten notes on the slide:

- 1. Statement
- 2. Account
- Account types: Liability, Sales A/c, Cash A/c, Purchase A/c, Asset A/c
- Debit (Dr) and Credit (Cr) sides
- Example T-account for Cash:

Trial Balance		Account	
	Dr	Cash	Cr
Cash A/c	100	1 Sale	5 Purchase
		2 Income	7 Expense
			8 Assets

Additional notes: 'On a day on March, 2020', '(Stock) Concept', 'Flow Concept', 'for a period of time', 'by balance sheet', 'Debit Credit'.

The 1st question is, what is trial balance? The answer is: it is a statement of account balances. Let us discuss these two aspects: what is a statement and what do we mean by account balances. Let us understand the contrast between a statement and an account. Till now we have been working with a ledger in which we have posted journal entries in a chronological manner. An account looked like this where we had a debit side and a credit side and let us say this was a cash account. You had transactions where you got cash, any other income on the debit side, and you spent the cash on a number of items, expenses, or any assets that were purchased. These transactions happen over a period of time. Therefore, this account is showing you that on the 1st day of the month you did a sale, on the 2nd day this happened, 5th day, 7th day, 8th day. So, this is a duration of time: during 1 month, or during 1 year, you are looking at what all transpired in a particular account. Therefore, an account is prepared for a duration or for a period of time.

After having prepared this account, you look for what is the balance carried down. This is the balancing figure, the amount left in the cash account, the cash in hand that we have at the end of this financial period. Now, this balance is as on the last day of the financial year or the accounting period for which you are preparing the bank account. This balance is true only on this day. The following day you will spend some more cash. So, the cash is going to go down or you may receive more cash. This one specific balance is true on a given day. However, overall, the account is going to show various transactions happening throughout the period for which the account is being prepared.

Now, let me contrast this with the statement: a statement is prepared on a date, on a day. In a statement, which we are now going to prepare- trial balance, is going to show us account balances. Let us say cash balance, what is the balance in the cash account? It is 100. So, the trial balance is telling you that at the end of the financial year, at the end of the accounting period, the balance left in the account is 100. What is the end of the accounting period? Well, this is as on March 31st, 2020, the last day of the financial year. This 100, this data, is accurate as on this date; on 1st April the data could change. So, that is the difference between a statement and an account, while the account is a flow concept where you are talking about flow of money during an accounting period, this is a stock concept. The stock concept means on a specific date what is it that we have in hand and it could relate to cash, bank or any other account balance. It could be any item of asset, liability, income or expense. So, that is another technical difference between a statement and an account as defined in the accounting language.

Let us answer the second question, what are account balances. Well, you prepared a cash account, purchase account, an asset account; all the accounts had a closing balance by balance carried down or to balance carried down. So, these balances are what we are referring to. At the end of the accounting period what is the balance left in a specific account that when shown in a statement form, we call it trial balance.

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4.1.2 Why Trial Balance?

- Proof of double entry system — Debits = Credits
- All debits have equal credits
- Therefore, all debit balances must be equal to all credit balances
- Arithmetic accuracy of books of accounts
- If Trial balance does not agree, there may be errors in journal entries or ledger posting

The slide also features the logos of the Indian Institute of Technology (IIT) Bombay and NPTEL in the top right corner, and a video feed of a speaker in a white turban and glasses in the bottom right corner.

Let me talk a little bit more about what trial balance is. Trial balance is also thought of as a proof of the double entry system. What is a double entry system? Double entry system basically says all debits have equal credits; all debit amounts are equal to credit amounts. In the trial balance, we are going to report the account balances, as I said, and the account balances here, these could be debit balances and these could be credit balances. So, if you have a sales account- here. If you have any other liability account, this is going to have credit balance, credit balance, debit, debit and debit. The idea is that the balances in all the accounts with credit balance is going to be equal to total balance in all the accounts with debit balances. So, that is when arranged in this statement form, all account balances will show debits equal to credit and when we will prepare the trial balance we will see more about it.


So, this statement is thought of as a proof: if debits are equal to credit, then you have not made an arithmetic mistake at least and you have followed the process of double entry system. To summarize, all debits will have equal credits and arithmetic accuracy is checked, and if there is any difference in the balances of debit and credit, then there must be some mistake which needs to be figured out.


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4.1.3 Format of Trial Balance

Trial Balance As on May 31, 2020

Account	Dr. Amount ✓	Cr. Amount ✓
CASH A/C	100	
Capital A/C		100
.....		
.....		
.....		
.....		
.....		
.....		
	<u>100</u>	<u>100</u>





Let me make it more clear to you with the format of the trial balance. This is the format of this trial balance. So, trial balance is prepared as on a date. So, as on March 31st, 2020, on this date we are going to say cash account; the cash account will have a debit balance and we will write the amount here. Similarly, we could write capital account, any other account and it could have a credit balance of 100. Likewise, you have all the accounts that are going to be listed here and it is important for you to know the concepts of what is a debit balance, what is the credit balance because you have to then show these balances in specific columns. At the end of the statement the total on the debit side has to be equal to total on the credit side. If that is done, that means, we have written the journal entries correctly, we have posted the journal entries in the right accounts, and the statement is correct. The double entry system has been followed. So, we will do some practice problems, some tutorials on this, going forward.

So, let me stop here. This was a quick introduction to the statement called trial balance. I will see you in the next video.