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Manual Accounting - Module 8

Discounts, Accounting Equation and Journal

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Discounts are reductions in the price of goods or services, typically given by sellers to buyers for various reasons. There are mainly two types of discounts in accounting:

1. Trade Discount

- **Definition:** A trade discount is a reduction in the listed price of a product or service, offered by the seller to the buyer, usually based on the quantity purchased or a long-term business relationship.
- **Purpose:** Encourages bulk purchases or rewards loyal customers.
- **Accounting Treatment:** Trade discounts are not recorded separately in the accounting books. The sale is recorded at the net amount after the trade discount has been applied.

2. Cash Discount

- **Definition:** A cash discount is a reduction in the invoice amount offered by the seller to the buyer as an incentive for early payment.
- **Purpose:** Encourages prompt payment, which improves the seller's cash flow.
- **Accounting Treatment:** Cash discounts are recorded separately in the accounting books. They are typically recorded in accounts such as "Discount Allowed" (for the seller) and "Discount Received" (for the buyer).

Cost: Cost can be termed as the amount of resources given up in exchange for some goods and services.

Profit: It is the excess of total revenues over total expenses of a business enterprise of an accounting period.



- Ques 1:** Prepare Accounting Equation from the following:
1. Started business with cash Rs. 75000 and goods Rs. 25000
 2. Paid for rent Rs 2000
 3. Bought goods for cash Rs. 30000 and on credit for Rs. 44000

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4. Goods costing Rs 50000 sold at a profit of 25%, out of which Rs 27500 received in cash.
5. Purchased a Motor-cycle for personal use Rs. 25000

Solution:

To prepare the accounting equation, we need to determine the effects of each transaction on the assets, liabilities, and owner's equity. The accounting equation is:

Assets = Liabilities + Owner's Equity

Let's go through each transaction step by step:

S. No.	Transaction	Assets			- Debtor	Liabilities (₹)	+ Capital (₹)
		Cash (₹)	+ Stock (₹)	+ Debtor			
(i)	Started business with cash ₹75,000 and goods ₹25,000	75,000	25,000			100,000	
		75,000	25,000			100,000	
(ii)	Paid rent ₹2,000	(2000)				(2000)	
		73,000	25,000			98,000	
(iii)	Bought goods – Cash ₹30,000, Credit ₹44,000	(30000)	74,000		44,000		
		43,000	99,000		= 44,000	98,000	
(iv)	Goods costing ₹50,000 sold at 25% profit	27,500	(50000)	35,000		12,500	
		70,500	49,000	35,000	= 44,000	110,500	
(v)	Motor-cycle purchased for personal use ₹25,000	(25000)				(25000)	
		45,500	49,000	35,000	= 44,000	85,500	

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Assignment on Accounting Equation

Ques 1: Set of transactions are given below, apply the accounting equation step by step.

Initial Balances:

Assume we are starting with the following initial balances:

- Cash: Rs. 50,000
- Inventory: Rs. 20,000
- Accounts Receivable: Rs. 10,000
- Equipment: Rs. 30,000
- Liabilities (Creditors): Rs. 15,000
- Owner's Equity: Rs. 95,000

The initial accounting equation is:

Assets = Liabilities + Owner's Equity

$$110,000 = 15,000 + 95,000$$

New Transactions:

1. Purchased goods for cash Rs. 8,000
2. Goods sold to vasu at Rs 1500 (costing Rs 1800)
3. Paid salaries Rs. 4,000
4. Purchased goods from Rahul Rs. 20000, out of which 10% received in immediately.
5. Received Rs. 6,000 from Debtors
6. Owner withdrew Rs. 2,500 for personal use

Ques 2: Prepare Accounting Equation from the following:

1. Started business with cash Rs. 100,000 and equipment Rs. 50,000
2. Paid for office supplies Rs. 5,000
3. Purchased goods for cash Rs. 20,000 and on credit Rs. 35,000
4. Sold goods costing Rs. 30,000 for Rs. 50,000, out of which Rs. 20,000 was received in cash
5. Paid Rs. 15,000 on account to creditors
6. Owner withdrew Rs. 10,000 for personal use

Ques 3: Prepare Accounting Equation from the following:

1. Started business with cash Rs. 80,000 and machinery Rs. 70,000
2. Paid for advertising Rs. 4,000
3. Purchased goods for cash Rs. 40,000 and on credit Rs. 50,000
4. Sold goods costing Rs. 60,000 for Rs. 90,000, out of which Rs. 30,000 was received in cash
5. Paid Rs. 20,000 on account to creditors
6. Owner withdrew Rs. 8,000 for personal use

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- Ques 4: Prepare Accounting Equation from the following:
1. Started business with cash Rs. 90,000 and building Rs. 150,000
 2. Paid for office rent Rs. 6,000
 3. Purchased office supplies for cash Rs. 15,000 and on credit Rs. 10,000
 4. Sold goods costing Rs. 20,000 for Rs. 35,000, out of which Rs. 10,000 was received in cash
 5. Paid Rs. 5,000 on account to creditors
 6. Owner withdrew Rs. 12,000 for personal use

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- Ques 5: Prepare Accounting Equation from the following:
1. Started business with cash Rs. 120,000 and land Rs. 200,000
 2. Paid for utilities Rs. 3,500
 3. Purchased inventory for cash Rs. 30,000 and on credit Rs. 40,000
 4. Sold goods costing Rs. 50,000 for Rs. 80,000, out of which Rs. 25,000 was received in cash
 5. Paid Rs. 18,000 on account to creditors
 6. Owner withdrew Rs. 7,000 for personal use

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Journal Entries of Trade Discount and cash Discount:-

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1. **Trade Discounts:** Trade discount a discount on the retail price of something allowed or agreed between traders or to a retailer by a wholesaler. It is deducted from the list price before journal entry, so they are not recorded separately.

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- **Example:** Purchased goods for cash with a list price of RS. 20,000 at a 10% of trade discount.
- **Calculation:** Trade Discount = $(20,000 \times 10\%) = \text{RS. } 2,000$
- **Net Price:** $\text{RS. } 20,000 - \text{RS. } 2,000 = \text{RS. } 18,000$
- **Journal entry:**

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DATE	PARTICULAR	LF	AMOUNT (DR)	AMOUNT (CR)
	PURCHASEA/C TO CASHA/c	DR	18000	18000

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2. Cash Discount: a discount on the retail price of something allowed or agreed between traders or to a retailer by a wholesaler. It is recorded in the journal at the time of payment to reflect the reduced amount paid or received

- **Example:** A company owes a supplier Rs.10,000 and receives a 20% discount for paying within 10 days. The company pays on the 8th day.
- **Calculation:** Cash Discount Amount: Rs.10,000 x 20% = Rs.2000
- **Net Price:** Rs.10,000 - Rs.2000 = RS.8000

• **Journal Entry:**

DATE	PARTICULAR	LF	AMOUNT (DR)	AMOUNT (CR)
	CREDITORS A/C	DR	10000	
	TO CASH A/c			8000
	TO DISCOUNT RECEIVED A/C			2000

When Trade and Cash both Discounts are applied in entry:-

Trade discounts are deducted from the list price before journal entry, so they are not recorded separately, while cash discounts are recorded in the journal at the time of payment to reflect the reduced amount paid or received.

Example: Purchased goods for cash, list price of ₹50,000, with a 20% trade discount and a 5% cash discount.

- **Step 1:** Calculate the trade discount and net purchase amount.
Trade Discount: 50,000 * 20% = RS.10,000
Net Purchase Amount: RS. 50,000 - RS. 10,000 = RS.40,000
- **Step 2:** Calculate the cash discount and final amount paid.
Cash Discount: 40,000 * 5% = RS. 2,000
Amount Paid: RS. 40,000 - RS. 2,000 = RS.38,000

Journal Entry:

DATE	PARTICULAR	LF	AMOUNT (DR)	AMOUNT (CR)
	CREDITORS A/C	DR	40000	
	TO CASH A/c			38000
	TO DISCOUNT RECEIVED A/C			2000

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Ques 1. Solve the following journal entries:

1. Goods sold ₹50,000 for cash, discount allowed @ 10%.
2. Cash received from Rishabh worth ₹19,500 and discount allowed to him ₹500.
3. Goods purchased from Hardik ₹20,000, at less 10% Trade Discount.
4. Goods sold to Abhinav for ₹10,000 and offered him a Trade Discount of @5%.
5. Goods purchased from Sahil ₹10,000 for cash, at less 10% Trade Discount and 5% cash discount.
6. Goods sold to Kashish for ₹20,000 for cash and offered him a Trade Discount @5% and a cash discount @2.5%.

Solution:

DATE	PARTICULAR	LF	AMOUNT (DR)	AMOUNT (CR)
1	CASH A/C DISCOUNT A/C TO SALES A/C (BEING GOODS SOLD FOR CASH AND DISCOUNT ALLOWED)	DR DR	45000 5000	50000
2	CASH A/C DISCOUNT A/C TO RISHABH'S A/C (BEING CASH RECEIVED AND DISCOUNT ALLOWED TO RISHABH)	DR	19500 500	20000
3	PURCHASE A/C TO HARDIK A/C (PURCHASE GOODS FROM HARDIK AND 10% TRADE DISCOUNT RECEIVED)	DR	18000	18000
4	ABHINAV A/C TO SALES A/C (BEING GOODS SOLD TO ABHINAV AND ALLOWED 5% TRADE DISCOUNT)	DR	9500	9500
5	PURCHASE A/C TO CASH A/C TO DISCOUNT RECEIVED A/C (BEING GOODS PURCHASED AND DISCOUNT RECEIVED)		9000	8550 450
6	CASH A/C DISCOUNT ALLOWED A/C TO SALES A/C (BEING GOODS SOLD FOR CASH AND DISCOUNT ALLOWED)		18525 475	19000

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Assignment on Discount Journal Entries

Ques 1: Solve this following Journal Entries

DATE	
Jan.10	Purchased goods from Ghanshyam of the list price of ₹ 50,000 at 15% trade discount.
13	Returned goods to Ghanshyam of the list price of ₹ 2,000.
15	Paid cash to Ghanshyam ₹ 40,000 in full settlement of his account.
20	Purchased goods from Raghu of the list price of ₹ 60,000 at 10% trade discount.
22	Returned goods to Raghu of the list price of ₹ 5,000.
25	Paid cash to Raghu ₹ 49,000 in full settlement of his account.

Ques 2: Pass Journal entries in the books of Raghunath Bros.

DATE	
Feb.1	Raghunath Bros. started business with cash ₹ 80,000 Goods ₹ 40,000 and furniture ₹ 20,000.
9	Sold goods to Nandal of the list price of ₹ 20,000 at trade discount of 10%.
12	Nandal returned goods of the list price of ₹ 4,000.
20	Received from Nandal ₹ 14,150 in full settlement of his account. Purchased goods from Brij Mohan of the list price of ₹ 10,000 at 15% trade discount.
22	
26	Returned goods to Brij Mohan of the list price of ₹ 1,000

Ques 3: Pass this Journal entries in your book

DATE	
Oct 3	Sold goods to Shruti for ₹ 80,000 at 15% trade discount and 4% cash discount.
9	Sold goods to Seema at Rs. 15000 at 2% cash discount
11	Purchased goods from Richa for ₹ 60,000 at 10% trade discount and 5% cash discount 60% amount paid by cheque immediately

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