

# Module 2: Introduction to the Single Entry System

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## 5. Single Entry System of Accounting

### 5.1 Definition and Meaning

The **Single Entry System** is an incomplete, unscientific, and unorganized system of recording financial transactions. Unlike the Double Entry System (which records both the debit and credit aspects of every transaction), a Single Entry System only records one aspect, or sometimes no aspect at all, depending on the convenience of the business owner.

In practice, a Single Entry System is a mixture of:

- **Double Entry:** For cash transactions (e.g., Cash Book).
- **Single Entry:** For personal accounts of Debtors and Creditors.
- **No Entry:** For nominal accounts (expenses and incomes) and real accounts (fixed assets), which are often completely ignored.

**Simple Definition:** Any system of bookkeeping that falls short of a complete Double Entry System is called a Single Entry System.

### 5.2 Objectives of Single Entry System

1. **Simplicity:** To maintain business records without the need for complex accounting knowledge or trained staff.
2. **Cost Reduction:** To save money on accounting software and professional accountants.
3. **Basic Tracking:** To keep track of cash balances, bank balances, and amounts owed by debtors or to creditors.
4. **Tax Assessment (Basic):** To provide a rough estimate of profit or loss for basic tax filing for very small businesses.

### 5.3 Advantages

- **Easy to Maintain:** Does not require specialized accounting knowledge. Anyone who can read and write can maintain it.

- **Economical:** Highly cost-effective; no need for professional accountants or expensive software.
- **Time-Saving:** Recording only essential transactions (cash and personal accounts) takes very little time.
- **Suitable for Small Businesses:** Ideal for sole proprietorships, street vendors, and small retail shops where transactions are limited.

## 5.4 Limitations (Disadvantages)

- **Incomplete Records:** It does not record both aspects of a transaction.
- **No Trial Balance:** Since dual aspects aren't recorded, a Trial Balance cannot be prepared, making it impossible to check arithmetical accuracy.
- **Frauds and Errors:** Highly susceptible to fraud, misappropriation of cash, and errors, as there is no cross-checking mechanism.
- **True Profit/Loss Cannot Be Ascertained:** Without a proper Trading and P&L Account, the exact net profit or loss cannot be calculated.
- **True Financial Position Unknown:** Since real accounts (assets) are not properly maintained, an accurate Balance Sheet cannot be prepared.
- **Unacceptable to Authorities:** Tax authorities and banks generally do not accept Single Entry records for tax assessments or loan approvals.

## 6. Distinction Between Double Entry and Single Entry & Types of Single Entry

### 6.1 Distinction: Double Entry vs. Single Entry

Basis of Difference	Double Entry System	Single Entry System
1. Principle	Records both Debit and Credit aspects of every transaction.	Records only one aspect, both aspects, or no aspect at all.
2. Accounts Maintained	Personal, Real, and Nominal accounts are all maintained.	Only Personal accounts and Cash accounts are maintained. Real and Nominal accounts are ignored.
3. Trial Balance	Can be prepared to check arithmetical accuracy.	Cannot be prepared.
4. Final Accounts	Trading A/c, P&L A/c, and Balance Sheet are prepared.	Statement of Affairs and Statement of Profit/Loss are prepared.

Basis of Difference	Double Entry System	Single Entry System
5. Accuracy & Reliability	Highly reliable, scientific, and acceptable to tax authorities and banks.	Unscientific, incomplete, and generally unacceptable to authorities.
6. Suitability	Suitable for all types of businesses (small, medium, large, companies).	Suitable only for very small sole proprietorships or partnerships.

## 6.2 Types of Single Entry System

1. **Pure Single Entry:** In this type, only Personal Accounts (Debtors and Creditors) are maintained. No cash book or any other subsidiary book is kept. It is extremely rare in practice.
2. **Simple Single Entry:** Here, Personal Accounts and a Cash Book are maintained. Transactions are recorded either in the Cash Book or the Personal Accounts.
3. **Quasi Single Entry:** This is a slightly advanced form where, along with Personal Accounts and a Cash Book, some subsidiary books (like Sales Book, Purchases Book, Bills Receivable Book) are also maintained.

## 7. Determination of Profit or Loss Under Single Entry (Statement of Affairs Method)

Since a Single Entry System does not maintain nominal accounts (expenses and incomes), a traditional Profit & Loss Account cannot be prepared. Instead, profit or loss is calculated using the **Statement of Affairs Method** (also known as the **Net Worth Method** or **Capital Comparison Method**).

### 7.1 The Core Logic (Capital Comparison Method)

The fundamental logic of this method is comparing the Capital at the beginning of the year with the Capital at the end of the year.

- If **Closing Capital** > **Opening Capital** = Profit
- If **Closing Capital** < **Opening Capital** = Loss

However, the closing capital is affected by two other factors:

1. **Drawings:** Amount withdrawn by the owner reduces capital. Therefore, it must be *added back* to closing capital to find the true profit.
2. **Additional Capital:** Fresh capital introduced during the year increases capital. Therefore, it must be *deducted* from closing capital to find the true profit.

## 7.2 The Statement of Affairs

A **Statement of Affairs** is similar to a Balance Sheet. It is prepared to find out the Capital on a specific date.

**Formula:** Capital = Total Assets - Total Liabilities

To find profit, you usually need to prepare **two** Statements of Affairs:

1. **Opening Statement of Affairs:** Prepared using assets and liabilities at the *beginning* of the year to find the **Opening Capital**.
2. **Closing Statement of Affairs:** Prepared using assets and liabilities at the *end* of the year to find the **Closing Capital**.

### FORMAT OF STATEMENT OF AFFAIRS (AS ON DATE...)

Liabilities	Amount (₹)	Assets	Amount (₹)
Sundry Creditors	xxx	Cash in Hand	xxx
Bills Payable	xxx	Cash at Bank	xxx
Outstanding Expenses	xxx	Sundry Debtors	xxx
Bank Overdraft	xxx	Stock in Trade	xxx
<b>Capital (Balancing Figure)</b>	<b>XXX</b>	Fixed Assets (Machinery, Furniture)	xxx
		Prepaid Expenses	xxx
<b>Total</b>	<b>XXXX</b>	<b>Total</b>	<b>XXXX</b>

## 7.3 Format of Statement of Profit or Loss

Particulars	Amount (₹)
<b>Capital at the end of the year (Closing Capital)</b>	<b>XXX</b>
Add: Drawings made during the year	XXX
	<b>XXX</b>

Particulars	Amount (₹)
Less: Additional Capital introduced during the year	(XXX)
<b>Adjusted Closing Capital</b>	<b>XXX</b>
Less: Capital at the beginning of the year (Opening Capital)	(XXX)
<b>Profit or Loss before Adjustments</b>	<b>XXX</b>
Less: Adjustments (e.g., Depreciation, Bad Debts, Provision for Doubtful Debts, Interest on Capital, Outstanding Expenses)	(XXX)
Add: Adjustments (e.g., Prepaid Expenses, Accrued Income, Interest on Drawings)	XXX
<b>Net Profit / Net Loss for the year</b>	<b>XXXX</b>



### Exam Tip:

*Adjustments (like depreciation or provision for bad debts) are usually made only to the Closing Assets when preparing the Closing Statement of Affairs, or they are deducted at the end in the Statement of Profit/Loss. Do not adjust Opening Assets.*

## 7.4 Practical Problem: Statement of Affairs Method

### Question:

Mr. Kumar keeps his books under the Single Entry System. His financial position on 1st April 2022 and 31st March 2023 was as follows:

Particulars	1st April 2022 (₹)	31st March 2023 (₹)
Cash in Hand	5,000	8,000
Cash at Bank	15,000	20,000
Sundry Debtors	40,000	50,000
Stock	30,000	45,000

Particulars	1st April 2022 (₹)	31st March 2023 (₹)
Furniture	20,000	20,000
Machinery	60,000	60,000
Sundry Creditors	25,000	35,000

During the year, he introduced additional capital of ₹20,000 and withdrew ₹1,500 per month for personal use.

**Adjustments:**

- Depreciate Machinery by 10% and Furniture by 5%.
- Create a provision for doubtful debts at 5% on Sundry Debtors.

Calculate his profit or loss for the year ended 31st March 2023.

**Solution:**

**Step 1: Prepare Opening Statement of Affairs (to find Opening Capital)**

**STATEMENT OF AFFAIRS AS ON 1ST APRIL 2022**

Liabilities	Amount (₹)	Assets	Amount (₹)
Sundry Creditors	25,000	Cash in Hand	5,000
		Cash at Bank	15,000
<b>Opening Capital (Balancing Figure)</b>	<b>1,45,000</b>	Sundry Debtors	40,000
		Stock	30,000
		Furniture	20,000
		Machinery	60,000
<b>Total</b>	<b>1,70,000</b>	<b>Total</b>	<b>1,70,000</b>

**Step 2: Prepare Closing Statement of Affairs (to find Closing Capital)**

(Note: We will apply the adjustments directly to the assets here)

**STATEMENT OF AFFAIRS AS ON 31ST MARCH 2023**

Liabilities	Amount (₹)	Assets	Amount (₹)
Sundry Creditors	35,000	Cash in Hand	8,000
		Cash at Bank	20,000
<b>Closing Capital (Balancing Figure)</b>	<b>1,52,000</b>	Sundry Debtors (50k - 5% prov: 2,500)	47,500
		Stock	45,000
		Furniture (20k - 5% dep: 1,000)	19,000
		Machinery (60k - 10% dep: 6,000)	54,000
<b>Total</b>	<b>1,87,000</b>	<b>Total</b>	<b>1,87,000</b>

### Step 3: Prepare Statement of Profit or Loss

#### STATEMENT OF PROFIT OR LOSS FOR THE YEAR ENDED 31ST MARCH 2023

Particulars	Amount (₹)
<b>Closing Capital</b> (as per Step 2)	<b>1,52,000</b>
<i>Add:</i> Drawings (₹1,500 x 12 months)	18,000
	<b>1,70,000</b>
<i>Less:</i> Additional Capital Introduced	(20,000)
<b>Adjusted Closing Capital</b>	<b>1,50,000</b>
<i>Less:</i> Opening Capital (as per Step 1)	(1,45,000)
<b>Net Profit for the year</b>	<b>5,000</b>

(Alternative Method: You can calculate Closing Capital without adjustments first, find the "Profit before Adjustments", and then deduct the Depreciation and Provision in the Statement of Profit or Loss. Both methods yield the exact same Net Profit).

## | 8. Distinctions and Conversion Method

### 8.1 Distinction Between Balance Sheet and Statement of Affairs

Basis of Difference	Balance Sheet	Statement of Affairs
1. Accounting System	Prepared under the Double Entry System.	Prepared under the Single Entry System.
2. Basis of Preparation	Prepared exclusively from ledger account balances extracted into a Trial Balance.	Prepared from incomplete records, physical counts, estimates, and external documents (like bank statements).
3. Reliability	Highly reliable and accurate.	Less reliable as it is based on estimates and incomplete data.
4. Missing Figures	Since both aspects are recorded, there are no "missing" balancing figures like Capital. Capital is taken from the ledger.	The primary purpose is often to find the missing <b>Capital</b> as the balancing figure.
5. Objective	To show the true and fair financial position of the business.	To estimate the capital balance on a particular date.

### 8.2 Distinction Between Profit & Loss Account and Statement of Profit & Loss

Basis of Difference	Profit & Loss Account	Statement of Profit & Loss
1. Accounting System	Prepared under the Double Entry System.	Prepared under the Single Entry System.
2. Components	Prepared by matching actual Revenues (sales, indirect incomes) against actual Expenses (purchases, indirect expenses).	Prepared by comparing Opening Capital with Closing Capital, adjusting for drawings and new capital.
3. Accuracy	Highly accurate as it uses complete nominal account balances.	An estimate of profit, as it relies on estimated capital figures.
4. Gross Profit	Calculates Gross Profit (via Trading A/c) before Net Profit.	Cannot calculate Gross Profit; it only provides an estimated Net Profit.

## 8.3 The Conversion Method (Overview)

The **Conversion Method** is the process of converting incomplete Single Entry records into a complete Double Entry set of accounts to prepare a proper Trading Account, Profit & Loss Account, and Balance Sheet.

This is a much more complex method than the Statement of Affairs method. It requires finding missing figures by opening various ledger accounts.

### Key Steps in Conversion Method:

1. **Prepare Opening Statement of Affairs:** To find Opening Capital.
2. **Prepare a Total Debtors Account:** To find missing figures related to credit sales, cash received from debtors, or closing debtors balance.
3. **Prepare a Total Creditors Account:** To find missing figures related to credit purchases, cash paid to creditors, or closing creditors balance.
4. **Prepare a Cash/Bank Book:** To find missing cash sales, cash purchases, opening/closing cash balances, or drawings.
5. **Prepare Bills Receivable / Bills Payable Accounts:** If required, to find missing acceptances or dishonored bills.
6. **Final Accounts:** Once all missing figures (Sales, Purchases, Cash balances) are calculated, prepare the Trading A/c, P&L A/c, and Balance Sheet normally.

### Exam Focus:

*For university exams, the Statement of Affairs (Capital Comparison) method is highly tested for practical problems. The Conversion method problems are usually longer and test your ability to construct Total Debtors and Total Creditors accounts to find missing Sales and Purchases.*

End of Module 2 • Subject: Financial Accounting