

# Method of Accounting

## Cash Basis of Accounting

In cash basis of accounting, all transactions whether of capital or revenue nature are recorded only as and when effected. An entry in the books of account is made only when cash is received or paid except for closing, opening & few adjustment entries. For example, goods and services purchased/ availed are recorded as assets or expenses at the time they are paid while revenues, including grants and donations, are recorded at the time of actual receipt or transfer of funds. Amounts payable, liabilities outstanding or amount receivable are ignored and not accounted for in the books.

## Accrual Basis of Accounting

Under this method, goods and services purchased/availed are recorded as assets or expenses at the time the goods are received and services are availed irrespective of the fact as to whether actual payment by cash/ cheque is effected or not by the organisation. Similarly, revenues including grants are recorded at the time when they are earned or become due irrespective of the fact as to whether the amount has actually been received or not. This is the most acceptable and popular method of accounting though in the NGO sector Cash Basis of Accounting is more widely used.

## Illustration

To understand the difference between Cash and Accrual system of accounting, let us take an illustration : Nimhas after receiving Rs.50,000/- when he purchased the Brochure & Banner worth Rs.30,000/- actually paid only Rs.20,000/- to the supplier and Rs.10,000/- was agreed to be paid later and while travelling the actual expenditure was Rs.4,000/- but Nimhas paid Rs.5,000/- an additional amount of Rs.1,000/- was paid as advance.

When we compare these two Methods of Accounting with the help of the two Trial Balance prepared by Nimhas we find that under Accrual Method there are two additional accounts, Outstanding Expenses Account and Prepaid Expenses Account. In one sense Accrual Method is more scientific and appropriate as it helps us in knowing what we are to pay in future and what we have already paid for the future. But Cash Basis of Accounting is widely followed only due to the simplicity and clarity embedded in its operation.

The cash basis of accounting is widely preferred by the voluntary organisations over accrual basis for reasons of simplicity in its application. Even non-accountants, who have a good grasp of the principle of debit and credit, can fairly perform the job. Many voluntary organisations also view that accrual basis of accounting is useful for profit- making organisations and income generating projects.

Further, most of the funding agencies and provisions of Foreign Contribution (Regulations) Act, 1976 primarily require the actual receipt and disbursement/utilisation/application of funds/grants/ income, thereby approving the cash basis of accounting.

**Entries to be passed on Cash Basis Accounting Method**

<b>Date</b>	<b>Particulars</b>	<b>Ledger Folio No .</b>	<b>Amount</b>	<b>Amount</b>
	Brochure & Banner Account Dr. To Cash Account Cr. (Being Brochure & Banner of Rs.30,000/- purchased, out of which Rs.20,000/- is paid and Rs.10,000/- remains outstanding)		20,000.00	20,000.00
	Travelling Account Dr. To Cash Account Cr. (Being Rs.5,000/- incurred for travelling including Rs.1,000/-as advance payment to be adjusted next year. )		5,000.00	5,000.00

**Trial Balance as per Cash Basis Accounting Method**

<b>Particulars</b>	<b>Debit</b>	<b>Credit</b>
Cash Account	25,000.00	
Brochure Banner Account	20,000.00	
Travelling Account	5,000.00	
Grant Account		50,000.00

