

BOARD POLICY LETTER

14 NOVEMBER 1970

ISSUE IV

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CANCELS

HCO POLICY LETTER OF 14 NOVEMBER 1970

ISSUE IV

SAME TITLE

Remimeo  
Finance Bureau

Hats

AGF

OES

Treasury Hats

FBO

THE THEORY OF BOOK KEEPING AND ACCOUNTANCY

PART 3

PREPARATION OF INCOME AND

EXPENDITURE ACCOUNT AND BALANCE SHEET

Now let us take a normal series of transactions undertaken by the Organization, record the BOOK KEEPING for these transactions and then prepare the Income and Expenditure Account and Balance Sheet from them.

EXAMPLE 30:

John Smith starts a Franchise on 1 January and the following transactions were made in the three month period to 31 March. It is required that BOOK KEEPING entries be made to record these transactions and that an Income and Expenditure Account and Balance Sheet then be prepared. Full formal BOOK KEEPING, with the use of Personal Accounts, is to be kept whenever practical.

Note: An Income and Expenditure Account and Balance Sheet is usually drawn up for a financial period of one year, but here, for the sake of brevity, I take a smaller period of three months.

The following transactions occurred in the three month period:

Training and Processing Sold - OUTFLOW OF SERVICES

1.	1 Jan	Able is invoiced for a 25 hour intensive at cost	\$300.00
2.	14 Jan	Beal is invoiced for an HSDC at cost	500.00
3.	12 Feb	Cutts is invoiced for 10 hours of Review auditing at cost	200.00

Books and Meters Sold - OUTFLOW OF MEST

4.	17 Jan	10 copies of DMSMH sold for \$5.00 each to Jinks Jinks paid the \$50.00 immediately to cashier	
5.	12 Mar	2 E-Meters sold to Jenkins for \$140.00 each Jenkins paid the \$280.00 immediately to cashier.	

Suppliers Bills Received - INFLOW OF MEST AND SERVICES

6.	11 Jan	Received Rates Bill from East Grinstead Urban District Council for 6 month period to 30 June	200.00
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7.	12 Jan	Received Bill from Pubs Org as follows:	
		100 DMSMH delivered at \$3.00 each	100.00
		10 E-Meters delivered at \$80.00 each	800.00
			1100.00
8.	29 Jan	Received Stationery Bill from Godstone for	80.00
9.	11 Mar	Received Bill for Rent for 3 months period to 31 March from Bigwood & Co.	250.00
10.	17 Mar	Received Electricity Bill from the Electric Co. for supply for the months of January and February	70.00
11.	17 Mar	Received Bill for Simons & Co. for furniture for Franchise delivered and installed on 1 January	500.00
12.	31 Mar	Received Bill for Telephone from the Telephone Co for the period to 31 March	60.00

MONEY Disbursed - OUTFLOW OF MONEY

13.	19 Jan	Paid Rates Bill to East Grinstead Urban District Council	200.00
14.	31 Jan	Paid to Pubs Org on Account	100.00
15.	31 Jan	Paid Wages for staff member Silwell for the month of January	40.00
16.	17 Feb	Paid Rent Bill to Bigwood & Co.	250.00
17.	28 Feb	Paid check for 'cash' for John Smith's own personal expenses	100.00
18.	28 Feb	Paid Wages for staff member Silwell for the month of February	40.00
19.	20 Mar	Paid Electric Bill to the Electricity Co.	70.00
20.	27 Mar	Paid Simons on Account of Furniture	250.00

MONEY Received - INFLOW OF MONEY

21.	1 Jan	Received from Able for intensive	300.00
22.	17 Jan	Received from Jinks for 10 DMSMH	50.00
23.	21 Jan	Received from Beal on Account of HSDC	200.00
24.	31 Jan	Received from John Smith (the owner) to provide capital for the Franchise	1500.00
25.	28 Feb	Received on Account from Beal	200.00
26.	12 Mar	Received from Jenkins for 2 E-Meters	280.00
27.	12 Mar	Received from Cutts for Review Auditing	200.00
28.	29 Mar	Received Advance Payment from Sprake for HSDC to be commenced on 10 April	500.00

Note that in recording the BOOK KEEPING for the above transactions, four main groupings of Accounts or types of Accounts are made. Thus Impersonal Accounts are grouped into one Section; Personal Accounts relating to Suppliers are grouped in another Section; Personal Accounts relating to students and preclears for Sales of SERVICES are in another Section; and finally the Personal Account of John Smith, the owner, is placed in a Section of its own.

In the normal Scientology (R) Organization, it can be seen that the Personal Accounts with Suppliers are kept as a separate section by the preparation of the MONTHLY Bills Summary by the Department of Disbursements. Similarly, it can be seen that the Personal Accounts relating to students and preclears are kept as a separate section by the Department of Income.

You will note that each of the above example transactions are numbered 1 through to 28 and these numbers are used again when making the BOOK KEEPING entries below in order to help identification of the double entry recording of each transaction.

IMPERSONAL ACCOUNTS

BANK ACCOUNT

21.	1 Jan	Received from Able	300.00	13.	19 Jan	Paid to East Grinstead U.D.C. Rates	200.00
22.	17 Jan	Received from Jinks for books	50.00	14.	31 Jan	Paid to Pubs on Account	100.00
23.	21 Jan	Received from Beal	200.00	15.	31 Jan	Paid Wages to Silwell	40.00
24.	31 Jan	Received from John Smith - Capital	1500.00	16.	17 Feb	Paid Bigwood for Rent	250.00
25.	28 Feb	Received from Beal	200.00	17.	20 Feb	Personal Expenses for John Smith	100.00
26.	12 Mar	Received from Jenkins for E-Meters	280.00	18.	28 Feb	Paid Wages to Silwell	40.00
27.	11 Mar	Received from Cutts	200.00	19.	20 Mar	Paid to Electricity Company	70.00
28.	29 Mar	Received from Sprake	500.00	20.	27 Mar	Paid to Simons on Account	250.00
			<u>3230.00</u>				1050.00
					31 Mar	Balance	2180.00
			<u>3230.00</u>				<u>3230.00</u>
	31 Mar	Balance	2180.00				

PURCHASES OF BOOKS AND METERS ACCOUNT

7.	12 Jan	Books and Meters received from Pubs Org	1100.00	31 Mar	Transfer to Income & Expenditure Account	1100.00
			<u>1100.00</u>			<u>1100.00</u>

WAGES ACCOUNT

15.	31 Jan	Bank Account	40.00	31 Mar	Transfer to Income & Expenditure Account	80.00
18.	28 Feb	Bank Account	40.00			
			<u>80.00</u>			<u>80.00</u>

RATES ACCOUNT

6.	11 Jan	E.G.U.D.C. rates for 6 months to 30 June	200.00	31 Mar	Transfer to Income and Expenditure Account	200.00
			<u>200.00</u>			<u>200.00</u>

RENT ACCOUNT

9.	11 Mar	Pigwood & Co rent for 3 months to 31 Mar	250.00	31 Mar	Transfer to Income & Ex- penditure Account	250.00
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ELECTRICITY ACCOUNT

10.	17 Mar	Electricity Bill for Jan & Feb	70.00	31 Mar	Transfer to Income & Ex- penditure Account	70.00
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TELEPHONE ACCOUNT

12.	31 Mar	Telephone Bill to 27 March	60.00	31 Mar	Transfer to Income & Ex- penditure Account	60.00
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STATIONERY ACCOUNT

8.	29 Jan	Stationery Supplies from Godstone & Co.	80.00	31 Mar	Transfer to Income & Ex- penditure Account	80.00
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FURNITURE ACCOUNT

11.	17 Mar	Furniture Account on 1 Jan from Simons & Co.	500.00
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SALES OF TRAINING AND PROCESSING ACCOUNT

				1.	1 Jan	Intensive Delivered to Able	300.00
31 Mar		Transfer to Income & Expenditure Account	1000.00	2.	14 Jan	HSDC delivered to Beal	500.00
				3.	12 Feb	Review delivered to Cutts	200.00
			1000.00				1000.00

SALES OF BOOKS AND METERS ACCOUNT

31 Mar		Transfer to Income & Expenditure Account	330.00	22.	17 Jan	Bank Account - Jinks	50.00
				26.	12 Mar	Bank Account - Jenkins	280.00
			330.00				330.00

PERSONAL ACCOUNT - OWNERJOHN SMITH PERSONAL ACCOUNT

17. 20 Feb	Bank Account		24. 31 Jan	MONEY paid to	
	- MONEY received			the Organ-	
	from the Organ-			ization	1500.00
	ization	100.00			
31 Mar	Balance	1400.00			
		<u>1500.00</u>			<u>1500.00</u>
			31 Mar	Balance	<u>1400.00</u>

PERSONAL ACCOUNTS - SUPPLIERSPUBS ORG ACCOUNT

14. 31 Jan	MONEY received		7. 12 Jan	Books & Meters	
	from the Organ-			delivered to	
	ization	100.00		the Organi-	
31 Mar	Balance	1000.00		zation	1100.00
		<u>1100.00</u>			<u>1100.00</u>
			31 Mar	Balance	<u>1000.00</u>

EAST GRINSTEAD URBAN  
DISTRICT COUNCIL ACCOUNT

13. 19 Jan	MONEY received		6. 11 Jan	Rates SERVICE	
	from the			delivered to the	
	Organization	200.00		Organization for	
		<u>200.00</u>		6 months to	200.00
				30 June	<u>200.00</u>

BIGWOOD & CO. ACCOUNT

16. 17 Feb	MONEY received		9. 11 Mar	Rent SERVICE	
	from the			delivered to the	
	Organization	250.00		Organization for	
		<u>250.00</u>		3 months to	
				31 Mar	250.00
					<u>250.00</u>

ELECTRICITY CO. ACCOUNT

19. 20 Mar	MONEY received		10. 17 Mar	Electricity	
	from the			SERVICE supplied	
	Organization	70.00		to the Organi-	
		<u>70.00</u>		zation for Jan.	
				and Feb.	70.00
					<u>70.00</u>

TELEPHONE CO. ACCOUNT

			11. 31 Mar	Telephone SERVICE	
				supplied to the	
				Organization for	
				the period to	
				31 Mar	60.00
					<u>60.00</u>



GODSTONE & CO. ACCOUNT

8. 29 Jan Stationery delivered to the Organization 80.00

SIMONS & CO.

20. 27 Mar	MONEY received from the Organization	250.00	11. 1 Jan	Furniture supplied to the Organization	500.00
31 Mar	Balance	250.00			
		<u>500.00</u>			<u>500.00</u>
			31 Mar	Balance	250.00

PERSONAL ACCOUNTS - STUDENTS AND PRECLEARS

ABLE'S ACCOUNT

1. 1 Jan	Received SERVICE of 25 hour intensive	300.00	21. 11 Jan	MONEY paid to the Organization	300.00
		<u>300.00</u>			<u>300.00</u>

BEAL ACCOUNT

2. 14 Jan	Received SERVICE of HSDC	500.00	23. 21 Jan	MONEY paid to the Organization	200.00
			25. 28 Feb	ditto	200.00
			31 Mar	Balance	100.00
		<u>500.00</u>			<u>500.00</u>
31 Mar	Balance	100.00			

CUTTS ACCOUNT

3. 12 Feb	Received SERVICE of 10 hours Review	200.00	27. 11 Mar	MONEY paid to the Organization	200.00
		<u>200.00</u>			<u>200.00</u>

SPRAKE ACCOUNT

28. 29 Mar MONEY paid to the Organization 500.00

NOTE: All the above BOOK KEEPING was kept by full formal BOOK KEEPING, i.e. with the use of Personal Accounts except in the case of four items which were recorded by abbreviated BOOK KEEPING.

The first two of these items were:

22. 17 Jan Received MONEY from Jinks for 10 DMSMH 50.00

26. 12 Mar Received MONEY from Jenkins for  
2 E-Meters 280.00

Since the MONEY for these Sales was received immediately then the Personal Accounts of Jinks and Jenkins were ignored and by-passed and no recording was made of the OUTFLOW of the MEST as shown by transaction number '4' and '5' respectively. The entry made therefore was to debit Bank Account with the above receipts of MONEY and credit these sums to Sales of Books and Meters Account. Examples of 25 and 26 also demonstrated the use of abbreviated BOOK KEEPING for this type of transaction.

The other two items dealt with by abbreviated BOOK KEEPING were:

15. 31 Jan Paid MONEY to Silwell for Wages 40.00  
18. 28 Feb ditto 40.00

Since these wages were paid immediately, then the only entry made was to credit Bank Account and debit Wages Account. The Personal Account of Silwell was ignored. Again, this type of transaction was demonstrated in Example 27.

Note: You will observe that certain of the Impersonal Accounts have been closed off with an entry marked "Transfer to Income and Expenditure Account". Now this entry should be ignored at this stage because it is made later in the sequence than we are currently at. You should therefore look at the above BOOK KEEPING at this stage as though the above entries had not been made and, later in this example, the correct time and sequence for the above entries are indicated.

Now having completed the double entry BOOK KEEPING for each of the transactions we simply list down all the balances on each Account to show as either a debit or a credit balance. This listing is sometimes called a Trial Balance since it proves the arithmetical accuracy of the BOOK KEEPING.

The proof of this accuracy is that the list of debit balances equals the list of credit balances and as long as the double entry has been correctly recorded for each transaction, then we must balance.

It also should be observed what is meant by either a 'debit balance' or a 'credit balance' on an Account. A 'debit balance' on an Account simply means that the sum of the debit entries on that Account exceeds the sums of the credit entries. The Bank Account in this example shows debit entries of \$3230.00 and credit entries of \$1050.00 and this gives a debit balance of \$2180.00. You will observe the method of striking the balance on the Account and the fact that the debit balance does appear finally on the debit side.

A 'credit balance' is the reverse and occurs when the sum of the credit entries exceeds the sums of the debit entries. Pubs Org Account in this example shows credit entries of \$1100.00 and debit entries of \$100.00 to give a credit balance of \$1000.00. Again you will note the method of striking the balance and the fact that the credit balance does appear finally on the credit side.

	<u>TRIAL BALANCE</u>	<u>Debit</u>	<u>Credit</u>
IMPERSONAL ACCOUNTS -	Purchases of Books & Meters	1100.00	
	Wages	80.00	
	Rates	200.00	
	Rent	250.00	
	Electricity	70.00	
	Telephone	60.00	
	Stationery	80.00	
	Sales of Training & Processing		1000.00
	Sales of Books & Meters		330.00
<hr/>			
	Furniture	500.00	
	Bank Account	2180.00	
PERSONAL ACCOUNTS - SUPPLIERS			
	Pubs Org	1000.00	
	Telephone Co.	60.00	
	Godstone	80.00	
	Simons & Co.	250.00	
			1390.00
PERSONAL ACCOUNTS - STUDENTS AND PRECLEARS			
	Beal	100.00	
	Sprake		500.00
PERSONAL ACCOUNT OWNER	John Smith		1400.00
		<hr/>	<hr/>
		4620.00	4620.00

#### OBSERVATIONS ON THE TRIAL BALANCE

1. If you follow through all the Accounts above you will observe that we have simply listed down onto the Trial Balance all debit balances and all credit balances shown on the various Accounts. Again it must be stressed that those entries marked "Transfer to Income and Expenditure Account" must be ignored at this stage since they occur later in the sequence of actions.

You will observe that the debit balances listed do equal the credit balances and so the arithmetical accuracy of the BOOK KEEPING is proven.

2. If you look at the debit balances on the Trial Balance you will observe that a debit balance should equal either:

- a. The cost of MEST or SERVICES used up in the period
- or
- b. An Asset.

If you look at those debit items above the line drawn, you will observe that these should represent the cost of MEST or SERVICES used up in the Period. And if you look at those debit balances below the line, you will observe that these are Assets, i.e. Furniture, Bank Account, Debt due from Beal.

3. If you look at the credit side of the Trail Balance, you will observe that a credit balance equals either:

- a. The value earned in the Period
- or
- b. A liability.



If you look at the items above the line drawn on the Trial Balance, you will observe that these represent the value earned by the Organization. And if you look at the items below the line, you will observe that these are Liabilities.

4. All the debit and credit balances shown above the line go into and compose the Income and Expenditure Account since this shows the value earned by the Organization against the cost of MEST and SERVICES used up by the Organization in the Period. The resulting balance on the Income and Expenditure Account represents either Profit or Loss and is carried to the Balance Sheet.

5. All the items shown below the line drawn compose the Balance Sheet since the Balance Sheet is simply a list of Assets and Liabilities. To these is added the balance from the Income and Expenditure Account and this, as noted above, represents either an Asset or Liability according to whether it is a Loss or a Profit.

6. The next thing to realize is that the Income and Expenditure Account and Balance Sheet are one complete report. You cannot complete one without the other and it must be appreciated that the Balance Sheet is not a separate document all on its own.

It is the Income and Expenditure Account and Balance Sheet which give the complete financial report for the Period and together they represent all the BOOK KEEPING and Accounts.

7. The actions now necessary are:

- a. Take all the items above the line and place into the Income and Expenditure Account as shown below.
- b. Strike the balance on the Income and Expenditure Account and bring into the Balance Sheet as either Profit or Loss.
- c. Take all the items below the line and bring into the Balance Sheet.
- d. Obviously your Balance Sheet must now balance since the Trial Balance balanced in the first instant.

All we have done is to take those items above the line and summarize their result in the Income and Expenditure Account. This result (representing either profit or loss) is then carried down to join those items below the line on the Balance Sheet. Quite obviously, this must balance.

Now let us prepare the Income and Expenditure Account and Balance Sheet in accordance with the above.

JOHN SMITH - FRANCHISE

Income and Expenditure Account for the three months to 31 March

= Purchases of Books		Sales of Training &	
& Meters	1100.00	Processing	1000.00
Wages	80.00	Sales of Books &	
Rates	200.00	Meters	330.00

Rent	250.00		
Electricity	70.00		
Telephone	60.00		
Stationery	80.00		
		Loss for the Period carried to Balance Sheet	510.00
	<u>1840.00</u>		<u>1840.00</u>

BALANCE SHEET AS AT 31st MARCH

<u>Assets</u>		<u>Liabilities</u>	
Furniture	500.00	John Smith - Capital Account	1400.00
Balance at Bank	2180.00	Amounts due to Suppliers	1390.00
Debt due to the Organization	100.00	Advance Payment	500.00
Income & Expenditure Account - Loss for the Period	510.00		
	<u>3290.00</u>		<u>3290.00</u>

Observations on the Income and Expenditure Account and Balance Sheet:

1. The Income and Expenditure Account is composed of Accounts which are terminatedly handled for the Period concerned, i.e. as representing either the value earned by the Organization or the value of MEST or SERVICES used up in the Period.

Thus the final BOOK KEEPING ENTRY on each of the Accounts placed into the Income and Expenditure Account is one marked "Transfer to Income Expenditure Account". The effect of this entry is merely to transfer the balance on each of the Accounts concerned to one large summarizing Account - the Income and Expenditure Account. This final BOOK KEEPING entry has the effect of permanently closing off each of the Accounts concerned as far as that Period is concerned.

The entry "Transfer to Income and Expenditure Account" has been shown above on all the Impersonal Accounts so transferred to the Income and Expenditure Account.

But it should now be appreciated that the time at which this entry is made is when preparing the Income and Expenditure Account. Thus the Trial Balance is extracted first to prove the arithmetical accuracy of the BOOK KEEPING and then on preparation of the Income and Expenditure Account the relevant Accounts are closed off with the entry "Transfer to Income and Expenditure Account".

2. The Balance Sheet is composed of all the other Accounts representing either Assets or Liabilities. These Accounts are not terminatedly handled at the Balance Sheet date and so remain as "Balances". Hence the term "Balance" Sheet - it is simply a sheet of paper listing down all those Accounts not terminatedly handled and therefore still showing a "Balance".

3. The Income and Expenditure Account shows a debit balance or Loss for the Period of \$510.00 and this is carried to the debit side of the Balance Sheet as representing an Asset.

It is an Asset because it means that the owner, John Smith, owes this amount to the Organization.

However, since the Organization already owes John Smith \$1400.00 on his Capital Account, then the usual showing of this Loss is to deduct it from this sum owing to Smith.

Thus the Balance Sheet would record it as follows:

John Smith -- Capital Account	1400.00	
Less Loss for the Period	<u>510.00</u>	890.00

Thus the Loss of \$510.00 disappears from the Assets side of the Balance Sheet and, on the Liabilities side, the debt due to Smith is reduced to \$890.00 as shown above. Obviously we still balance since all that has been done is to reduce the Asset side and the Liability side of the Balance Sheet by \$510.00 each.

4. On the Asset side of the Balance Sheet, you will note that the debt due by Beal of \$100.00 is shown as "Debt due to the Organization". This could also have been described as "Sundry Debtor" or else "Account Receivable".

5. On the Liabilities side of the Balance Sheet the amounts due to Suppliers are collectively shown in the total of \$1390.00. Such amounts due to Suppliers could also have been described as "Sundry Creditors" or else "Accounts Payable".

6. The Liability due to Sprake of \$500.00 for his advance payment is described as this, i.e. "Advance Payment".

#### A NOTE ON BANK ACCOUNTS

In example 30 above, the Bank Account maintained by the Organization shows a debit balance of \$2180.00. This is an Asset and means that the Organization has that much MONEY in the Bank.

Now the fact that a debit balance on the Organization's Bank Account, as above, means that the Organization owns that much MONEY sometimes causes confusion.

This confusion arises because when the Bank, with whom the Organization deals, presents its Statement of the Bank Account, it will show a credit balance of \$2180.00 - not a debit balance. In other words, the Bank in presenting its Statement shows the complete reverse of the situation as shown by the Organization's BOOK KEEPING.

Now this is perfectly correct and is understandable if you realize that the Bank is presenting its own BOOK KEEPING records; these are different BOOK KEEPING records to those kept by the Organization.

And when the Bank holds \$2180.00 of the Organization's MONEY then, factually, it owes this MONEY to the Organization.



Therefore the credit balance of \$2180.00, as shown by the Bank Statement, reflects the liability of the Bank to the Organization.

If you work out the BOOK KEEPING records that the Bank would keep, you will see how this arises. You will see that when the Organization banks MONEY that the Bank must, in its BOOK KEEPING, credit the Account of the Organization because it owes the Organization this much MONEY. From the Bank's point of view, the Account maintained by it for the Organization is a Personal Account of an Outside Person, and it must credit that Account with all MONIES that the Organization banks.

And, reversely, the Bank will debit the Account of the Organization for all checks disbursed by the Organization.

In summation therefore, if you realize that the Bank Statement presented by the Bank represents its BOOK KEEPING record of the Personal Account that it keeps for the Organization then the matter becomes clear. Therefore the Bank Statement prepared by the Bank is always the complete reverse to that maintained in the Organization's BOOK KEEPING.

And when the Bank Manager tells you that the Organization is "in credit" to the amount of \$2180.00, then he is telling you that the Bank owes that much MONEY to the Organization.

Of course the complete reverse would apply if the Organization Bank Account were overdrawn. If we were to assume that in Example 30 that the Organization had disbursed \$3230.00 and received \$1050.00, then the Organization's records would show a credit balance on its Bank Account of \$2180.00. This credit balance would mean that the Organization had a liability of this amount since it owed this sum to the Bank.

The Bank, in presenting its Bank Statement, would show a debit balance of \$2180.00. Again, this is perfectly correct, since the Bank is presenting its BOOK KEEPING records and the debit balance on the Bank Statement means that the Bank has an asset of this amount because the Organization owes this amount to it. Therefore, when the Bank manager tells the Organization that it has a 'debit balance' on its Bank Account, he means that the Organization owes this amount of MONEY to it.

Derek Field  
Accountant WW  
for Herbie Parkhouse  
D/Guardian Finance WW  
for Jane Kember  
The Guardian WW  
for Mary Sue Hubbard  
The Controller

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