PRINCIPLES OF ACCOUNTS

THE MASTER KEY

Grade 10 – 12 examination concise .

2018 REVISED AND STANDARDIZED ACCORDING TO THE EXAMINATION SPECIFICATIONS.

2018 VERSION

NDOL A DISTRICT PRODUCTION

N.M Kachamba

RESOURCE TEAM

1. Kachamba Norman Team Coordinator, Kanini Secondary School
2. Mwanakasale Prudence – Lubuto Secondary School
3. Clande Bwalya - Kansenshi Secondary School

4. Kasonde Veronica – Kayele Secondary School
5. Fungai Koneki Mpofu – Kaniki Secondary School
6. Kayumba. V.K – Ndeke caritas secondary school

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3. BOOKS OF PRIME ENTRY AND SOURCE DOCUMENTS

32. Subsidiary books are also known as
……..
A. Books of prime entry B. Books of first entry C. Book of Original Entry D. All of the above

33. Which is both a book of prime entry and a ledger?

A Cash Book B General Journal
C Purchases Journal D Sales Journal

34. Every double entry in the journal proper should have summary and this is called a
A. Balance B. detail C. foil D. narration

38. Which of the following documents is used to write up the Petty Cash Book?
A. Receipt B. Invoice C. Petty Cash Voucher D. Cheque

39. Trade discount is recorded in the ……..
    A Cash Book B Cash Account
    C Purchases and Sales Account D Purchases and Sales Journal
40. An original invoice is used for recording in the
    A. Purchases Returns Day Book B. Sales Returns Day Book

    C. Purchases Day Book D. Sales Journal

41. The explanation of the double entries marked in the Journal is called
    A. A Balance B. details c. folios D. a narration

42. The Double entry is completed in the Cash Book for one of the following entries
    A. Drawings B. contra entry C. Sales entry D. Purchases entry
43. A purchases invoice shows 15 Hems costing K60, 000 each, less 20% trade discount and cash discount of 5% if paid within the credit period, the amount of the cheque will be
    A. K180 B. 684 C. K36 K720
44. Which of the following should be entered in the journal?
    (i) Payment for cash purchases
    (ii) Fixtures bought on credit
    (iii) Credit sale of goods
    (iv) Sale of surplus machinery
    A. (i) and (iv) B. (ii) and (iii) C. (iii) and (iv) D. (ii) and (iv)

45. Credit Notes issued by us will be entered in our
    A. Sales Account B. Returns Inwards Account C. Returns outwards D. Returns Inwards Journals
46. Which of the following is the book of original entry?
    A. The Sales (debtors) ledgers B. The purchases Journal

    C…..The general Journal D. The purchases (creditors) ledger

47. Which document does the firm use to record the goods sold on credit?
    A. Debit Notes B. Purchases Invoice C. Sales invoice D. Customers Statement
48. Given a desired cash float of K200. If 146 is spent in the period. How much will be reimbursed at the end of the period?
    A. 200 B. 540 C. K254 D. K 146
49. Invoices received are
    A. First entered In the cash journal
    B. First entered in the purchases journal
    C. First entered in the sales journal
    D. First entered in the general journal
50. The General Journal differs from all the other Subsidiary books. This is because it
    A. Records only assets bought in the business with narrations included
    B. Records transactions of a usual nature chronologically
    C. Records transactions of un usual nature chronologically
51. Record transactions alphabetically an organization's chief cashier gives the petty cashier K50 each week for small expenditures. In turn, the petty cashier asks for re-imbursement of whatever she has spent from the chief cashier. This is a system called
    A. Standing order B. Double entry system C. Floating system D. Imprest system.

52. Cheque book counter foils are used for recording
    A. Cash paid into Bank
    B. Bank credit transfer
    C. Payments received from customers through the bank
    D. Payments made to suppliers through the bank
53. The word **Subsidiary** means
    A. " giving help to the owner of the business"
    B. "giving help to the capital of the business"
    C. "giving additional help to the manager"
    D. "giving the ledger a proper system of accounting"
54. What document summarizes the day to day transactions between the buyer and the seller at the end of the month?
    A. Control Account B. Statement of account C. Bank statement f Account D. Bank

55. A debtor owes his supplier K500 000. What percent of cash discount is he allowed if he sends a cheque for K475, 000 after 14 days?
    A. 95% B. 5% C. 5.2% D. 9.5%

56. Which of the following documents is used to write up the petty cash Book?
    A. Receipt B. Invoice C. Petty cash voucher D. Cheque.

57. We originally sold 25 items at K12000 each, less $33\frac{1}{3}$ percent trade discount. Our customer now returns 4 items to use. What is the amount of Credit Note to be issued?
    A. K48 000 B. K36 000 C. K32 000 D. K16 000.
58. The purpose of sending a Credit Note is to
    A. Inform the buyer about goods payable
    B. Increase the amount owed by the buyer
    C. To inform the buyer the amount he owes the seller
    D. To reduce the amount the buyer owes the seller

59. A Debtor pays K260 000 receiving 5% cash discount. How much did he pay?
    A. K247 000 B. K13 000 C. K273 000 D. K507 000

60. The total of sales Returns journal is posted to the
    A. Credit side of sales Returns Account
    B. Credit side of Side of sales ledger
    C. Purchases ledger
    D. Debit side of purchases returns account

61. A Debit Note received from a supplier for an undercharge
    A. Increases the value of goods sold
    B. Increases the value of the goods
    C. Is credited to the bank Account
    D. Is debited to the bank Account

62. The number which indicates where the corresponding entry is found is known as
    A. Column number B. folio number C. batch number D. patent number

63. A computer costs K500 excluding V.A.T. if VAT is at the rate of 10% percent, the price including V.A.T will be
    A. K530 B. K670 C. K450 D. K550

64. Cash discount is an allowance for
    A. Prompt payment for goods bought
    B. Enabling a trader make profit
    C. Goods bought
    D. Goods bought on credit

4 DOUBLE ENTRY AND THE LEDGER

65. Mr Banda brings his private motor car into business, the entry would be :
    A. Dr, capital Cr cash B. Dr capital, Cr Motor car C. Dr motor car Cr, capital D. Dr Motor Car Cr cash.
66. Which of the following are personal accounts? (i) Building (ii) Wages (iii) Debtors (iv) creditors
    A. (i) and (iv) only
    B. (ii) and (iii) only
    C. (iii) and (iv) only
    D. (ii) and (iv) only
67. "Posting" the transactions in bookkeeping means
    A. Making the first entry of double entry
    B. Entering items in a cash book
    C. Making the second entry of a double entry transaction
    D. Something other than the above
68. Discount received are
    A. Deducted when we receive cash
    B. Given by us when we sell goods on credit
    C. Deduced by us when we pay our accounts
    D. None of the above
69. The proprietor paid a creditor Kalaba from his money outside the firm. The entry to record this would be
    A. Dr Creditors Cr Cash
    B. Dr Capital Cr Kalaba
    C. Dr Kalaba Cr Capital
    D. Dr Capital Cr Bank
70. The ledger is the book ……..
    A. from which the trial balance is extracted
    B. in which transactions are first recorded
    C. of original entry
    D. here errors are first recorded
71. Personal accounts are related to :
    A. Assets and liabilities
    B. Expenses, losses and incomes
    C. Debtors and creditors
    D. Capital and creditors

72. When goods are taken for use by the proprietor, the posting to the ledger is
   A. Dr stock, Cr purchases
   B. Dr proprietor, Cr sales
   C. Dr Drawings, Cr stock
   D. Dr Drawings, Cr purchases

73. Which one of the following is a nominal account?
   A. Rent paid B. Creditors C. Debtors D. Assets
74. Which of the following items would not appear in a purchases ledger Account?
   A. Sales Returns
   B. Purchases
   C. Cash payments made to suppliers
   D. purchases returns

75. Which account usually has a debit balance?
   A. Sales account
   B. Purchase account
   C. Purchase Returns account
   D. Capital account

76. The total of the " Discount allowed '' column cash book is posted to
   A. The debit of the discounts allowed account
   B. The debit of the discounts Received account
   C. The credit of the discounts allowed Account
   D. The credit of the discounts Received account

77. An example of Real Account is …….
   A Drawings Account B Makaya Account
   C Cash Account D Electricity Account
78. The customer's personal accounts are found are found in ……
   A Nominal Ledger B General Ledger
   C Sales Ledger D Purchases Ledger
79. The recording of two aspects of a transaction involves ……
   A Double entry B. Accounting equation
   C. Debit entry D. Credit entry
80. M Mwata was a sales agent for Standard Sales Co. Ltd and was receiving 15% commission on
Monthly sales. In one month he sold goods by cheque worth K15 500. Which entry below was Correct to record commission in M. Mwata's books?

	Account Debited	Account Credited
A	Bank account K2 325	Sales Account K235
B	Sales Account K2 325	Bank Account K2 325
C	Bank Account K2 325	Commission Received K2 325
D	Commission Received K2 325	Bank Account K2 325

81. The double entry is completed in the ……..
   A Sales book B Ledger book
   C Purchases book D General Book
82. In the "date" column of a ledger account you enter the date when the ……
   A Transaction is recorded in the ledger account

B Business started operating
C Transaction took place
D Accounting year started

83. The owner withdraws goods with a selling price of K20 000 from the business for his own use.

The goods cost him K15 000. This should be recorded by:

	DEBIT	CREDIT
A	Purchases Account K20 000.	Drawings Account K20 000
B	Drawings Account K15 000	Purchases Account K15 000
C	Drawings Account K20 000	Purchases Account K20 000
D	Purchases Account K15 000	Drawings Account K15 000

84. The debtors ledger is the book in which ……. are kept

A. Suppliers accounts B. Customers' accounts

C……Capital account D. Drawings account

85. The total of the returns inwards journal is posted to the

A. Debit side of the sales account
B. Credit side of the purchases returns account
C. Debit side of the sales returns account
D. Credit side of the side account

86. The of Accounts is called the

A. The ledger B. subsidiary C. Book of original entry D. Accounting Book

87 . What is the balance on the following account on 31st may 2008?

T. Bwalya's Account.

Dr			Cr		
1.05.08	Balance	205	17.05.08	Cash	300
14.05.08	Sales	360	28.05.08	Sales Returns	50
30.05.08	Sales	180			

A. A credit balance of 395
B. A debit balance of 360
C. A debit balance of 395
D. There is a nil balance on the account

88. Which of the following are correct?

		A/C to debit	A/C to credit
(i)	Bought office furniture for cash	office furniture	Cash
(ii)	A debtor C. Tembo pay us by cheque	Bank	C. Tembo
(iii)	Introduced capital by K. Mule	Capital	Bank
(iv)	Paid a creditor C.Phiri by cash	C. Phiri	cash

A. (i), (ii) and (iii) only B. (ii), (iii) and (iv) only C. (i) (ii) and (iv) only D. (i) and (iv) only

89. Which is the correct entry to record Commission received by cheque?

	A/C to Dr	A/C to Cr
A.	Bank	Sales
B.	Sales	Bank
C.	Bank	Commission Received
D.	None of the above.	

90. A credit balance is an account which occurs when
    A. The two sides of an account are equal
    B. The credit side of an account is greater than the debit side
    C. The debit side of an account is greater than the credit side.
    D. One side of an account has nothing recorded on it.
91. Repairs to the proprietors private house should be
    A. Dr to the drawings account B. Cr to the drawings account C. Dr to the repairs account D. Cr to the repairs account
92. Which of the following are examples of nominal account?
    (i) Star Motors (ii) cash account (iii) postage account (iv)furniture and fittings (v) wages account
    A (ii) and (v) B. (i) (ii) and (v) C. (iii) (vi) D. (ii) (iv) and (v)
93. Show the effect of transaction in which the owner puts an extra K4,000 cash into the business
    A. Debit cash credit owner
    B. Debit business and credit cash
    C. Debit bank and credit capital
    D. Debit cash and credit capital
94. Mande owns a toyshop. He sells a toy to chipo who pays cash. How will mande record this transaction?
    A. Debit cash and credit sale
    B. Debit cash and credit chipo
    C. Debit sale and credit cash
    D. Debit chipo and credit sales
95. Which of the following best describe the accounting equation
    A. Asset +capital=liabilities
    B. Capital –Asset = liabilities
    C. Capital - liabilities =Assets
    D. Assets – liabilities = capital

96. The recording of two aspects of transaction involves..
    A. double entry
    B. accounting equation
    C. debit entry
    D. credit entry

5 THE TRIAL BALANCE

97. Which of the following is the heading for the Trial Balance?
    A. Trial Balance for the year ending 31st December 2001
    B. Trial Balance as at 31st December 2001
    C. Trial Balance for the month ending 31st December 2001

D. Trial Balance as at year ending 31st December 2001

98. The following balances are available in the books of D. Mwanza a trader as at 31st December, 2016

Sales	8000
Drawings	2200
Sales Returns	800
Purchases	5000
Opening stock	1000
Purchases Returns	1500
Insurance	500

Using the information above prepare the Trial Balance to find the totals

A. Dr 7300, Cr 7300 B. Dr 9500, Cr 9500 C. Dr 13800, Cr 13800 D. Dr 3000, Cr 3000

99. A business prepares a Trial Balance so as to
   A. Calculate the profit and Loss account
   B. Show the financial position
   C. Check on the arithmetical accuracy of double entry
   D. Check the cash and bank balances

100. In the trial balance the balance on the provision for Depreciation Account is
   A. Shown as a credit item
   B. Not shown, as it is part of depreciation
   C. Shown as a debit item
   D. Sometimes as a credit, sometimes as a debit.

6 FINAL ACCOUNTS

101. Carriage outwards is charged to the profit and loss account since it is an expense that is concerned with

A. buying of goods B. Selling of goods
C. purchase of fixed assets D. delivery of goods being returns to customers

101. Net profit is calculated in the……..

A. Trading Account B. Profit and Loss Account C. Trial Balance D. balance sheet

102. Freight charges should be charged to
   A. The trading account
   B. The profit and loss account
   C. The balance sheet
   D. The profit and loss appropriation account

103. Import Duty and Freight Charges are expenses to the business. In which section of the final Accounts should they appear? In the ……..

A Profit and Loss Account B Trading Account
C Profit and Loss Appropriation Account D Balance sheet

104 . In which statement is gross profit calculated?

A Balance Sheet B Trial Balance
C Profit and Loss Account D Trading Account

105. A sole proprietorship business is best described as …….
A A manufacturing company
B A business that buys and sells goods at a profit
C A one man business
D A non-profit making organization

105. Which of the following should not be called sales?
A. Office fixtures sold B. Cash Sales
B. Goods Sold on credit D. Sale of an item previously included in purchases

106. Which of the following best describes the meaning of " purchases"
A. Item bought B. Bought goods on credit C. Goods bought for sale D. Goods paid for

107. When preparing final accounts, Revenues should be
A. Debited to the profit and loss account
B. Credited to the Trading Account
C. Debited to the Trading Account
D. Credited to the Trading Account

108. In the absence of drawings and additional capital, capital at the end less capital at start is equal to
A. Net profit B. Gross profit C. Net worth D. Drawings

109. Cost of goods sold is equal to
A. Sales minus purchases
B. Purchases minus closing stock, minus purchases Returns
C. Purchases minus Returns outwards
D. Opening stock, plus purchases minus Returns outwards minus closing stock.

110. The Trading Account of a firm for the year ended 30th June, 2001 shows the following details;

Stock 01.0.2000	K59, 360
Sales	K838, 400
Purchases	K614, 880

What is the gross profit?
A. K833,840 B. K824, 480 C. K268, 960 D. K209, 600

111. Carriage inwards
A. Increases the cost of sales
B. Increases the cost of purchases
C. Increases the expense of the business
D. Increases the gains of the business

112. Cost of goods sold is equal to
A. Sales minus purchases
B. Purchases minus closing stock, minus purchases Returns
C. Purchases minus Returns outwards
D. Opening stock, plus purchases minus Returns outwards minus closing stock.

113. You are given the following:
Cash k80 000, machinery 45 000, Debtors 50 000, creditors k26,000, stock k30,000; Mortgage k42,000, Bank overdraft k18 000, find working capital.
A. K116 000 B. K214 000 C. K133 000 D. K127 000

7 ADJUSTMENT TO FINAL ACCOUNTS

114. When a fixed asset can no longer be used or depreciated in the business due to its obsolete state, it is generally referred to as having a
A. Nominal value B. scrap value C. Book value D. Market value

115. The Omission of a rent receivable owing figure from the profit and Account will
   A. Increase the net profit for the business
   B. Reduce the net profit for the business
   C. Increase the gross for the business
   D. Reduce the gross for the business

116. For which category of fixed assets is the revaluation method of depreciation most appropriate?
   A. Loose tools B. Motor vehicles C. Office equipment D. Plant and Machinery

117. If an accumulated depreciation account is in use then the entries for the year's depreciation would be
   A. Credit, provision for depreciation, Debit profit and loss account
   B. Debit asset Account, Credit profit and loss account
   C. Credit Asset Account, debit provision for Depreciation Account
   D. Credit profit and Loss account, debit provision for Depreciation Account

118. The books of a trader are closed on 31st for December. In the rates Account which shows a total of K220 000 , is included a payment of K96 000 representing rates for the half year 1st October 2002 to 31st March 2003. The amount charged to the profit and loss account will be
   A. K124 000 B. K127 000 C. K316 000 D. K172 000

119. The central sand supply corporation depreciates. Its vehicles using the straight line method and all the trucks are estimated to last 5 years. A truck was bought for K25 000 000 and sold at the end of the third year for
   K13 000 000. We can then say the truck was sold at
   A. A profit of K3 000 000 B. A loss of K3 000 000

   C. A profit of K2 000 00D. A loss of K2 000 000

120. At the beginning of the year provision for bad debts account had balance of K65 500. During the year K35 500 was written off as bad debts. At the end of the year the debtors balance was K 800 000 and a provision for bad debts of 5% was to be maintained. How much was taken to the profit and loss account?
   A. K40 000 Dr B. K40 000 Dr C. K10 000 Cr D. K10 000 Dr

121. The books of trader are closed on 31st December. In the rates account, which shows a total of K220, is included, a payment of K96 representing rates for the half year 1st October 2002 to 31st March 2003. The amount charged to the profit and loss account will be
   A. K124 B. K127 C. K316 D. K172

122. At the beginning of the month the Debtors figure was K360 500, k60 500 was written off as bad debt.
   K200 00 was received from the debtors at the end of the month, and K450 000 was owing from the debtor at the end of the month. How much were credit sales?
   A. K710 500 B. K1070 000 C. K810 000 D. K350 000

123. The creditors balances at the beginning of the month was K328 000, during the month goods worth K735 000 were purchased and cheques amounting to K800 500 were paid. What was the creditors closing balance?
   A. K1063 000 Cr B. K262 500 C. K1128 500 Dr D. K262 500 C of Cr

124. On 1st January 2010, insurance was K48. During the year K72 was paid. On 31st December 2010, insurance paid in advance was K24. Calculate the amount charged to the profit and loss account.
   A. K72 B. K24 C. K96 D. 120

125. A company makes a provision for doubtful debts of 5% on debtors. On 1st January the balance standing on the provision for Doubtful debtors amount to k300, 000. The provision for doubtful debts per 31st December is?

A. Decrease by K5000 B. Increase by K5000

C……Increase by K15 000 D. Decrease by K15 000

126. At the beginning of the year the provision for bad debts account had a balance of k65 500. During the year k35 500 was written off as bad debts. At the end of the year the Debtor balance was k800 000 and a provision for bad debts of 5% was to be maintained. How much was taken to profit and loss Account?

A. K40 000 , debit side
B. K40 000 , credit side
C. K10 000 , credit side
D. K10 000 , debit side

127. If a provision for depreciation account is in use, then the entries for the year's depreciation would be

A. Cr profit and loss account, Dr Provision for depreciation account
B. Dr Asset account, Cr profit and loss account
C. Cr Asset account, Dr provision for depreciation account
D. Cr provision for depreciation, Dr profit and loss account

128. A Trial Balance shows provision for bad debts of K 190 and debtors K 800. It is required maintained the provision at 2.5 percent of Debtors. To do this profit and Loss Accounts should show:

A. A credit of K 20 B. A credit of K 28 C. A credit of K 490 D. A credit of K 394

A decrease in the provision for bad debts will

A. Increase cash/ Bank balance
B. increase net profit for the year
C. decrease net profit for the year
D. decrease the cash/ Bank balance

129. A Motor Van costing K100, 000 is expected to have a working life of five years and a scrap value of K10, 000 at that time. Using the straight line method of depreciation, the annual charge of depreciation will be

A. K20, 000 B. K10, 000 C. K18, 000 D. K2 2000

130. A trader took out an insurance policy 1st March 2007, the annual premium being K724, 000. He closes his books on 31st December of the same year. How much of the amount was paid in advance?

A. K60, 000 B. K540, 000 C. K180, 000 D. K120, 000

131. A Debtor who owes your company K200 is declared bankrupt. He is able to pay only K4 in every K10 he owes. How much will be written off as a bad debt?

A. K120 B. K100 C. K180 D. K80

132. A firm bought a machine for K320, 000. It is to be depreciation at a rate of 25 percent using the reducing balance method. What would be the remaining book value after two years?

A. K160, 000
B. Value of partly finished goods
C. Value of goods purchased

D. Value of finished goods on hand

133. An increase in provision for Bad debts will
   A. Increase the bank balance
   B. Increase net profit for the year
   C. Decrease net profit for the year
   D. Decrease the cash balance

134. The depreciation which allows same amount to be deducted annually from an asset is called……
   A Straight line method
   B Diminishing balance method
   C Revaluation method
   D Reducing balance method

135. Prepaid rent and salaries at a close of a trading period are listed under ……..
   A Long term liabilities B Fixed assets
   C Current asset D Current liabilities

136. The cost of a machine is K250 000, provision for depreciation is K60 000, depreciation charges For the year are K19 000. In the Balance Sheet, the machine will be shown at a net value of ……..
   A K190 000 B K231 000 C K250 000 D K171 000

137. A machine which originally cost K5 000 is sold for K750. The provision for Depreciation Account relevant to this machine shows a credit balance of K4 350. This means that there is
   A. A loss on sale of K100
   B. A profit on sale of K100
   C. A profit on sale of K750
   D. A profit on sale K4 350

8 LIMITATIONS TO THE TRIAL BALANCE AND SUSPENSE ACCOUNT

138. When a transaction is completely omitted from the books, it is called …….
   A. Error of commission
   B. Error of omission
   C. Error of principle
   D. Transposition error

139. If the trial balance do not agree, the difference must be entered in ……
   A. The profit and loss account
   B. A suspense account
   C. A nominal account
   D. The capital account

140. Which of the following error would be detected by the Trial Balance?
   A. Error of original entry
   B. Error of principle
   C. Error of complete reversal
   D. A single entry transaction

141. The purchase of a motor vehicle has been debited to the motor vehicle expenses account. What type of error has been made?
   A. Commission
   B. Ommission

C. Original entry
D. Principle

142. Which of the following affects the Trial Balance agreement?
    A. Wages account added up incorrectly, being totalled K10,000 more.
    B. Purchases K4,400 from James Manda entered in both accounts as k4,040.
    C. Sales K105 to James entered in Johns account
    D. Cheque payment of K2,130 for motor expenses entered as K2,310 in both accounts.

143. On 20 September 2010, the accounts clerk discovered that sales of K250 had been posted to Mwape's account in error. The goods had been sold to Mwaba on credit. Upon discovering of this error the journal entry was made as shown below:

    Journal entry
    Dr Mwaba K250
    Cr Mwape K250
    (----------)

    Which one is the correct narration for this record?
    A. Being sales overcast
    B. Being error of commission now corrected
    C. Being suspense accounts now corrected
    D. Being error of omission now corrected

144. Errors are corrected through the General Journal. This is because it…….
    A. provides a record to explain the double entries
    B. definitely saves the book-keeper's time and effort
    C. saves the trouble of entering them in the ledger
    D. is much easier to make entries in the general ledger

145. Which of the following errors would not affect the balancing of a Trial Balance?
    A. An amount not posted to E. Banda
    B. An amount omitted entirely from the books
    C. An amount posted to the wrong side of the account
    D. An amount overcast in one account

146. Discount received K2,000 has been posted on the debit side of discount allowed account. The entry to correct the error is ……

A.	Suspense Dr K2,000	Discount received Cr K2,000
B.	Discount allowed Dr K2,000	Discount received Cr K2,000
C.	Suspense Dr K4,000	Discount allowed Cr K2,000 Discount received Cr K2,000
D.	Discount allowed Dr k4,000	Discount received Cr K4,000

147. Which of the following do not affect the Trial Balance agreement?
    (i) Sales K 150 to A. Mwape entered in P. Mwaba's account
    (ii) Cheque payment of K 431 for motor expenses entered only in cash Book
    (iii) Purchases K 404 from C. Chali entered in both accounts as K 440
    (iv) Wages account added up incorrectly being totalled K 100 less
    A. (i) and (iv)
    B. (i) and(iii)
    C. (ii) and(iii)
    D. (iii) and(iv)

148. Compensating errors are……..
    A. Errors where an entry has been omitted

B. Errors which compensate or cancel each other
C. Errors made in the ledger
D. Errors made in the subsidiary books

149. If the purchase of stationery was debited twice in the account, we reserve by
A. Debiting stationery account
B. Crediting stationery account
C. Crediting suspense account
D. Debiting suspense account

150. Which subsidiary book records the correction of errors?
A. Petty cash book
B. Sales journal
C. Cash book
D. General journal

151. The sales figure from the journal was posted as K56 500 to the sales account instead of K65 500. To correct this error.
A. Dr Suspense and Cr Sales with K9 000
B. Dr Sales and Cr Suspense with K9 000
C. Dr Suspense and Cr Sales with K65 500
D. Dr Suspense and Cr Sales with K56 500

152. Errors corrected using the suspense account are the ones that ……
A. prevent the trial balance from balancing
B. are not exposed by the trial balance
C. affect the balance sheet
D. are omitted in the ledger

153. Which of these errors below cannot be revealed by a Trial Balance?
A. Compensating Errors
B. Errors of original Entry
C. Errors of principle
D. All of the above

9 BANK RECONCILIATION STATEMENTS

154. A Bank Reconciliation statement is a statement……..
A. Sent by the bank when the account is overdrawn
B. Drawn up by us to verify our cash Book balance
C. Drawn up by the bank to verify the cash book balance
D. Sent by the bank when we have made an error

155. The bank statement may be used in business as…….
A. A Source document for the subsidiary books
B. A source of information for reconciling the cash and bank records
C. Part of the double entry for deposited money
D. A bank credit records for loans

156. Mr C. Ngoma has a bank overdraft of K250 with Stanchart Bank (Zambia)Ltd. 1st September, he issued cheques to Mr. Mwanza K180 and Ms. Mulomba for K360. He further receives three cheques from the following debtors; MrSoko K150, MrChilekati K70 and MrBwalya K230 within one week. How much overdraft does Mr C Ngoma have at the end of the week
A. K490
B. K250

C. K340
D. K790

157. If you want to make sure that your money will be safe, if cheques sent are lost in the Post, you should
A. Not use the postal service
B. Always pay by cash
C. Always take the money in person
D. Cross your cheques "Account Payee only, not negotiable

158. The bank statement balance may differ from the cash book (bank column) balance because:
(i) One party may have made a mistake
(ii) One party may lack immediate knowledge of action taken by another
(iii) Both have different transactions
(iv) The accountants of the business are very fast in recording
Which of the above statements are true?
A. (i) (ii) and (iii)
B. (i) (iii) and (iv)
C. (ii) (iii) and (iv)
D. (i) and (ii)

159. A Bank reconciliation statement prepared starting with balance as per bank will show
A. Unpresentedcheques added, and uncredited deposits subtracted.
B. Uncredited deposits added, and unpresentedcheques subtracted
C. Bank charges added, and uncreditedcheques subtracted
D. Credit transfers added, and bank charges subtracted.

160. The following information is available for Mwendo enterprises:
Bank balances shown in cash book K650(Dr)
Amounts paid is not yet credited K150
Bank charges not yet entered in cash Book K50
Credit transfer received by the bank not yet entered in cash K300
Unpresented cheques K100
The bank statement balance should be…….
A. K750 B. K450 C. K850 D. K550

161. When Lee makes out a cheque for K50 and sends it to Young then Lee is known as
A. Payee B. Banker C. Drawer D. Creditor

162. Junior Bookkeeper was updating the cash book (Bank Column). On the bank statement he found M. Mahongo (credit transfer) with K1200 entered in the credit column. This had not yet been entered in the cash book. On which side of the cash book (bank column) should it be entered?
A. Credit cash book with K1200
B. Debit cash book with K1200
C. Credit cash book with K2400
D. Debit cash book with K2400

163. A cheque paid by you, but not yet passed through the banking system, is

A. Standing orders
B. A dishonoured Cheque
C. A credit transfer
D. An unpresented cheque

164. A request to the bank to make payments a regular intervals is known as
A. Standing order B. Giro credit C. Bill of exchange D. Paying – in – slip

165. The document for withdrawing money from current Account is the
A. Cheque B. Invoice C. Receipt D. Withdrawal slip

166. Which statement is sent by the bank to its customers to verify the balance at bank at the end of the month?
A. Bank Reconciliation Statement
B. Bank Statement
C. Cash Statement
D. Statement of Account

10 CONTROL ACCOUNTS

167. What is the purpose of the control accounts?
A. To calculate total receipts
B. T o calculate year end debtors and creditors balance
C. To calculate total cash discount
D. To calculate total returns

168. Given opening debtors balance of K11 500, sales K4 800 and receipts from debtors K4 500, the closing debtors' balance total should be
A. K 8 500
B. K14 500
C. K11 500
D. K18500

169. In the sales ledger control account. The bad debts written off should be shown in the account……
A. as a debit
B. as a credit
C. both credit and debit
D. as a balance carried down

170. A trader took out an insurance policy on 1st May 2007, the annual premium being K720. He does his books on 31st December. Calculate the amount paid in advance?
A. K60
B. K240
C. K180
D. K120

171. In which ledger would the debtors control account be kept?
A. Sales ledger
B. General ledger
C. Nominal ledger
D. Purchases ledger

172. Which item would not appear in a Sales Ledger Control Account?
    A. Sales Returns
    B. Interest charged on overdue accounts
    C. Provision for bad debts
    D. Discount Allowed
173. At the beginning of month the total creditors balance was K2700 and the balance at the end was k3560. During the month payments to creditors were K5760. What were the purchases for the month?
    A. K9320
    B. K12020
    C. K6620
    D. K8460

174. In sales ledger control account ,provision for bad debts should be shown in the account
    A. As a debit
    B. As a credit
    C. Balance brought down
    D. Should not be shown
175. Which item appears on the credit side of a purchases ledger control account?
    A. Cheques paid
    B. Discount received
    C. Refund from suppliers
    D. Purchases return
176. The balance brought down in the debtors account was K 9000. At the end of the same accounting period, the firm's debtors were K1500.During the period, a bad debt of K100 was written off and K5000 was received from credit customers. The total of the firms credit sales for the period was:
    A. K3700
    B. K4200
    C. K5400
    D. K5900
177. Entries in control accounts are made from?
    A. Bank statement
    B. Books of original entry
    C. Ledger accounts
    D. Sales invoices
178. At the beginning of the period, a business owed its creditors K15000.During the period, the credit purchases amounted to K87000, and paid K94000 to the creditors. At the end of the period, the firm owed the creditors:
    A. K7000
    B. K8000
    C. K14000
    D. K22000

179. A cheque received by Mulenga from a debtor is later dishonored, how is this taken in Mulenga 's control account?

A. Credit in purchases ledger control account
B. Credit in sales ledger control account
C. Debit in purchase ledger control account
D. Debit in sales ledger control account

180. The total of the purchases control account had been under casted by K100. How could this error be rectified in the concerned firm's journal?

A. Dr suspense A/c K100 Cr purchase A/c K100
B. Dr purchase A/c K200 Cr suspense A/c K200
C. Dr purchase A/c K100 Cr suspense A/c K100
D. Dr creditors A/c K100 Cr purchases A/c K100

181. Calculate the ending debtors from the following balances of sales ledger control account?

Opening balance	K17,100
Sales(Cash)	K7,100
Credit sales	K10,100
Refund to credit customer	K210
Bad debts written	K250
Return inwards	K350
Set off	K2,700

A. K27,200
B. K27,410
C. K23,900
D. K24,110

11 ACCOUNTS OF NON PROFIT MAKING ORGANISATIONS

182. Clubs and societies are registered as non-profit making organizations because

A. The motive of formation is not for profit
B. They only receive income through subscriptions and donations
C. They do not make profit at all
D. They are not involved in selling of anything at all

183. The Kitwe cricket club had equipment worth K1 000, subscriptions in arrears K160, Stock of refreshments K1600; sundry creditors for refreshments K1000. What was the accumulated fund for the club?

A. K1760 B. 170 C. K1750 K17600

184. A social club's receipts and payments account for the year 2010 showed rent paid as K4,000. On 1st January 2010 rent owed by the club was K800. On December 31st 2010 rent owed by the club was K1000. What is the amount charged for rent on the income and Expenditure Account for the year 2010?

A. K4 000 B. K4 200 C. K4 800 D. K 5 000

185. The consolidated fund balance of a club at a specific date can be found by.

A. Balancing off a receipts and payments account.

B. Preparing a statement of affairs
C. Preparing an income and expenditure account
D. Subtracting the surplus for the year from total assets

186. The following balances were taken from the book of Lusaka Golf Club
Subscriptions prepaid for last year K 100
Subscriptions received for next this year K 5 000
Subscriptions prepaid for current year K 150
Subscriptions owed for current year K 200

Find the amount of subscriptions transferred to the income and expenditure account
A. K5 250 B. K5 150 C. K7 150 D. K5 300

187. In a club Balance sheet subscriptions paid in advance are recorded as
A. A current assets B. A current liability C. A fixed assets D. Added to the accumulated fund.

188. A club's income and expenditure statement is similar to
A. Profit and loss B. Appropriation C. cash book D. Balance sheet

189. …… is the summary of the cash book for the period
A. Income and expenditure B. Profit and Loss C. Balance sheet
D. Receipt and payments

190. A club had credit balance of K146 as its subscription account on 1st January 2002. During the year subscriptions of K1300 were received, but K74 of this was in advance for the following year. What is the amount transferred to the income and Expenditure Account?
A. K1 372 B. K1 446 C. K1 154 D. K1 080

191. At the end of the year K6 000 has not yet been paid for the subscriptions by some member of the Recreation Club. This should be ……..

A Shown as a credit balance in Subscription Account
B Shown as an expense in the income and Expenditure
C Added to the accumulated fund
D Shown as a debit balance in the Subscription Account

192. In a club, the profit and loss account is replaced by ……..
A Receipt and payments account
B Subscription account.
C Trading, profit and loss account
D Income and expenditure account

193. Subscriptions prepaid in the previous year will in the Income and Expenditure Account be.....
A Added to new subscriptions
B Subtracted from the new subscriptions
C Included in the expenditure
D let out.

194. Accumulated fund is the term used to mean
A Capital of non- profit making organization
B. Capital of a profit making business
C. Capital for companies
D. Cash in hand

12 CAPITAL AND REVENUE EXPENDITURE AND RECEIPTS

195. Extension to the clubhouse is an example of
   A. Revenue expenditure
   B. Capital expenditure
   C. Current expenditure
   D. Nominal expenditure

196. Capital Expenditure is
   A. The extra capital paid in by the proprietor
   B. Costs of running the business on day to day basis
   C. Money spent on buying fixed assets or adding value to them
   D. Money spent on selling fixed assets

197. Revenue Expenditure is …….
   A Money spent on selling fixed assets
   B Money spent on buying fixed assets or adding value to them
   C The cost of running the business on a day to day
   D The extra capital paid in by the proprietor

198. A motor vehicle purchased for use in the business is……
   a. Revenue expenditure in the profit and loss account
   b. Capital expenditure appearing in the balance sheet
   c. Revenue expenditure added to the purchases in the trading account
   d. Capital receipts added to the capital in the balance sheet

199. Expenditure on assets which last for more than one year and permanently increase profit making capacity of the business is called……..
   a. Capital receipts
   b. Revenue expenditure
   c. Revenue receipts
   d. Capital expenditure

200. ……..appear in the profit and loss account under expenses subtracted from gross profit
   a. Revenue receipts
   b. Revenue expenditure
   c. Capital expenditure
   d. Capital receipts

201. Which receipts/incomes are recorded in the trading, profits and loss account as sales or additional incomes added to the gross profit to get gross income?
   a. Capital receipts/incomes
   b. Capital expenditure
   c. Revenue expenditure
   d. Revenue receipts

202. Which one is capital receipt?

a. Purchase of machinery by cheque
b. Sale of machinery for cash
c. Rent received in cash
d. Stationary bought by cheque

203. Which of the following revenue expenditures is for a Motor vehicle dealer?
(i) Advertising
(ii) Extension of premises
(iii) Purchase of cars for resale
(iv) Purchase of house
a. (i) and (ii)
b. (i)and (iii)
c. (ii) and (iv)
d. (iii) and (iv)

204. What is the effect of treating Capital expenditure as revenue expenditure?
a. To reduce the gross profit
b. To increase the net profit
c. To reduce the fixed assets
d. To increase the fixed assets

SINGLE ENTRY

205. Incomplete records are best described as records which
A. Are kept in single entry bookkeeping system
B. Have been partly destroyed
C. Show only the cash book
D. Are maintained on the double entry system

206. The best method of calculating profit if double entry is not maintained is
A. Decrease in net worth method
B. Increase in net worth method
C. Balance sheet method
D. Profit and loss account method

207. Incomplete Records are best described as records which ……
A are destroyed by fire
B are not kept on single entry
C are not kept on double entry system
D show only debit entry.

208. A trader had an opening capital of K85 000 and closing capital of K107 000. She had drawings of?

K13 000 during the year. What was her net profit?
A K9 000 B K13 000

C K22 000 D 35 000

209. The following are the assets and liabilities of a business:- Cash K850 000, Mortgage loan, K680 000, Creditors K320 000, Motor Vehicle K550 000. What is the amount of capital?

A K850 000 B K400 000
C K680 000 D K320 000

210. A firm's capital at the end of a trading period amounted to K2 100. The net trading profit was K 450. While drawings amount to K 255.What was capital owed at the beginning of the trading period?

A. K1 800 B. K1 875 C. K1 905 D. K1 650

PARTNERSHIP ACCOUNTS

211. Assets can be revalued in a partnership change because
A. The law insist upon it
B. It helps prevent injustice to some partners
C. Inflation affects all values
D. The depreciation charged on them needs to be reversed

212. You are to buy an existing business which has assets valued at buildings 50 000, motor vehicles K15 000, fixtures K5 000, and stock K40 000. You are to pay K140 000 for the business. This means that
A. You are paying K40 000 for goodwill
B. Building are costing k30 00 more than their value
C. You are paying k30 00 for goodwill
D. You have made an arithmetic mistake

213. Mulenga and Jelita are in partnership sharing profits and losses in the ratio 3:2 Net profit for year was k52,000. Mulenga receives a salary of K12 000 . What are the amount to be credited to the Partners current accounts?
A. Mulenga K26 000, Jelita 26 000
B. Mulenga K31 200, Jelita 20 800
C. Mulenga K36 000, Jelita 16 000
D. Mulenga K24 000, Jelita 16 000

214. Interest on capital is recorded on the ……
A. Debit side of the partners current A/C
B. Credit side of the partners current A/C
C. In the balance sheet under current Assets
D. On the credit side of the appropriation A/C

215. Goodwill may be define as
A. The difference between the purchase price of a business and the of assets taken over
B. The value given to the seller of the business
C. The value given to the purchases of the business
D. An agreement between the purchaser and the seller of the business

216. Where there is no partnership agreement profit and losses
A. Must be shared in same proportion as capital
B. Must be shared equally after adjusting for interest on capital
C. Must be shared equally
D. Must be shared after deducting drawings

217. The minimum number of partners in a partnership is

A. 7 B. 2 C. 20 D. 5

218. A double entry for the interest on drawings in the partnership accounts is

A. Credit the interest on Drawings and debit the Current Accounts of partners

B. Credit the Current Accounts of partners and debit the interest on Drawings Account

C. Debit the profit and loss Appropriation and credit the partners' Current account

D. Debit the partners' current Accounts and credit the Profit and Loss Appropriation Account.

219. Profit of partnership amount to K3 280 before the following is taken into account.

(i) Interest on partner's capital K180

(ii) Interest on drawings K20

(iii) Salary of one partner K1 000

(iv) Sharing ratio is 1:1

How much profit remains for division between the partners?

A. K2 080 B. K2 100 C. 2 120 D. 2 440

220. What does a Credit Balance on a partner's current account represent to a business?

A. Current Assets B. Current Liability C. Long term Liability D. Part of the capital

221. The agreement between partners is recorded in a document known as

A. Partnership deed

B. Memorandum of association

C. Table of content

D. Prospectus

222. When a partnership agreement states that the capital Accounts should remain fixed. It is best to deal with the share of profits by

A. Dr the Partners current A/C

B. Cr the Partners capital A/C

C. Cr the Partners current A/C

D. Dr the Partners capital A/C

223. What does the word "Residue" mean in relation to profit in a partnership business?

A. The profit that remains after all expenses have been paid in the Profit and Loss Appropriation Account and is available for sharing

B. The profit that remains after all expenses have been paid in the profit and loss Appropriation and is kept aside as a reserve

C. The profit before any expenses have been in the profit and loss Appropriation Account.

D. The profit before any expenses have been paid in the profit and loss Account

224. A partner's salary of K210 000 would be posted to the ……..

A debit side of profit and loss account

B credit side of the profit and loss

C debit side of his current account

D credit of his current account

225. In order to keep the partner's Capital Accounts fixed, changes on variations to the Capital are recorded in the

A. Profit and Loss Appropriation Account

B. Partners, Current Accounts
C. Partners Drawings Accounts
D. Partnership Trading Account

226. When a partnership agreement states that the capital Accounts should remain fixed. It is best to deal with the share of profits by
A. Dr the Partners current A/C
B. Cr the Partners capital A/C
C. Cr the Partners current A/C
D. Dr the Partners capital A/C

227. Where the partnership deed does not exist, the partners are expected to use the……
A. name of the company
B. title names
C. partnership act 1890
D. company certificate

15 MANUFACTURING ACCOUNTS

228. What do you understand b the term "work in progress"
A. Sales less cost of goods sold
B. Value of partly finished
C. Value of goods purchased.
D. Value of finished goods on hand

229. A manufacturing business extracts the following information from its books

Direct materials	K28
Direct Labour	K22
Indirect Expenses	K 8

What is the prime cost of production?

A. K36
B. K42
C. K50
D. K58

230. The cost of manufacturing goods is transferred to…….
A. the profit and loss account
B. the trading account
C. the balance sheet
D. no where

231. Which of the following items would be charged to the profit and loss in a manufacturing concern?
A. Factory Labour
B. Factory overheads
C. warehouse wages
D. Office Rent

232. In the manufacturing business, royalties paid on every item manufactured are regarded as……
A. Direct expense

B. An indirect expense
C. Part of raw material used
D. Factory overhead expense

233. Factor overhead costs are expenses……
A. directly traced to items being manufacturing
B. which cannot be traced to the items being manufactured
C. incurred to sell manufactured goods
D. found in the Trading Account

234. In a manufacturing account the excess of the market value of the goods over the cost of production results in……..
A. an undervalued prime cost
B. a manufacturing profit
C. an overvalued total overhead expenditure
D. a manufacturing loss.

235. For a manufacturing company, depreciation of machinery in the plant should be included in the……
A. prime cost section
B. trading account
C. factory overheads
D. profit and loss account

236. The sum of prime cost plus the indirect manufacturing costs is the …….
A. direct cost
B. production cost
C. overhead expenses
D. direct materials

237. How is the factory cost of production calculated?
A. Direct labour+direct material
B. Direct material+factory overheads
C. Direct material+direct labour+factory overheads
D. Direct material+direct labour+total overheads

238. A manufacturing firms cost were as follows

Raw materials	55,000
Direct labour	86,400
Factory overheads	122,000
Depreciation on plant	6,400
Administration cost	8,800
Selling and distributor	12,000

There was closing work in progress of K12,400. What was the factory cost of production?
A. K257,400
B. K263,400
C. K269,800
D. K278,200

239. A manufacturer has the following costs

240.

Raw materials	K8,000		
Wages: factory workers	K4,000	factory supervisor	K1,000
		office workers	K2,000

Fixed overheads: factoryK4,500 office K4,500

What is the factory cost of production?

A. K12000
B. K16,500
C. K17,500
D. K21,00

241. What item is the factory overhead?

A. carriage on raw materials
B. Cost of raw materials
C. Secretary's salary
D. Wages on machine operators

Priskay manufactures school uniforms. She provided the following information

	K
Material cost	5000
Labour cost	4000
Factory overheads	2000

What is the cost of production?

A. K5000
B. K9000
C. K7000
D. K11,000

242. Which is an Indirect cost

A. Carriage inwards
B. Factory rent
C. Production materials
D. Production wages

243. What will be included in a manufacturing account?

A. Bank charges and commission on sales
B. Depreciation on plant and sales men salaries
C. Direct labour and factory overheads
D. Direct labour and office expenses

16 ACCOUNTING ETHICS

244. When accountant In the firm adhere to professional code of ethics, this would result in clients developing……. The firm as decisions would be made in their best interest.

A. Trust B. Reliability C. Loyalty D. Dependence.

245. Which one of the following is not a danger of non- adherence to Ethics in accounting?

A. Competition B. Fraud C. Integrity B. Embezzlement

246. Which of the following words best describes ethics in accountancy

(i) Fraud
(ii) Integrity
(iii) Corruption
(iv) Discipline
(v) Embezzlement
(vi) Honest

(A) (i) (iii) and (v)
(B) (ii) (iii) and (iv)
(C) (ii) (iv) and (vi)
(D) (I) (V) and (vi)

17 INTERPRETATION OF FINAL ACCOUNTS

247. Given cost of goods sold K16 000 and margin of 20% this sales figure is
A. 20 150 B. K13 600 C. K21 000 D. 20, 000.

248. If the opening stock is K 3 000, closing stock K5 000, Sales K4 000 and Margin 20% their stock turnover is
A. 8 times B. 5 times C. 6 times D. $7\frac{1}{2}$ times

249. If K500 was shown added to purchases instead of being added to a fixed asset.
A. Net profit only would be understated
B. Net profit only would be overstated
C. It would not affect net profit
D. 30th gross profit and loss would be understated

250. If the cost price of goods is k900, 000 and the margin is 25 per cent. Find the selling price
A. K925, 000 B. k1120, 000 C. k300, 000 D. k1200, 000

251. The Mark-Up is the gross profit's relationship with the ……
A Capital B Turnover C Cost of goods D Average stock

252. Total sales of K2800 have been debited to the Sales account. What is the effect of this on the sales account balance?
A. Over stated by K2800
B. Overstated by K5600
C. Understated by K2800
D. Understated by K5600

253. A debit balance in capital account indicates that the firm is
A. Overtrading B. Depreciation C. Insolvent D. Investing

254. Identify the correct statement
A. Profit does not alter capital
B. Profit reduces capital
C. Capital can only come from profit
D. Profit increases capital

255. A business that is short of working capital is said to be
A. Solvent B. Bankrupt C. Insolvent D. overtrading

256. The amount a trader adds to his/her cost price of goods is known as

A. Mark up B. Prime cost C. Cost of goods sold D. Net profit

257. A business maintains a gross profit mark – up of 25% and achieved total sales of K60, 000 for the year. What is the cost of goods sold?

A. K12, 000 B. 15 000 C. K45, 000 D. K48 000

258. C. Phiri's current Assets and Liabilities were as follows:

Stock	62 000
Creditors	35 000
Debtors	43 000
Bank overdraft	25 000
Prepared Expenses	15 000

What is C. Phiri's working capital ratio

A. 2:1 B. 1:2 C. 4:1 D. 0.7: 1

259. Table gives information for a company's financial year

Gross profit	K23 680
Wages	K15 600
Insurance	K1 300

Insurance is prepaid by K60, 000 and wages outstanding are K1500 000. What is the net profit for the year?

A. K5 220 000 B. K53 400 C. K8 220 000 D. K8 340 000

260. A business achieves a gross margin $33\frac{1}{3}$%. The following information available

Opening stock	K5 000
Purchases	K25 000
Closing stock	K6 000

The value of sales for the year is

A. K32 000 B. K36 000 K24 000 D. K30 000

261. The books of a business has the following :

Sales	K90 000
Cost of sales	K50 000
Expenses	K10 000

What is the net profit as a percentage of sales?

A. 20% B. 33.3% C. 44.4% D. 66.6%

262. A trading account showed the following figures, sales K15 000, purchases K10 000, opening stock K4 000, closing stock K6 000. The rate of turnover was

A. 2.4 B. 1.6 C. 3 D. 5

263. A business maintains a gross profit Mark – up of 25% and achieved total sales of K60.000 000 for the year. What is the cost of goods sold?

(A) K12 000,000

(B) K15 000,000

(C) K45,000,000

(D) K48,000,000

264. Trading account of a firm for the year ended 30 June 1999 shows the following details:

Stock (1.7.98)	K 5,936	
Stock (30.6.99)		K 4,544
Sales		K83,840
Purchases		K61.488

(A) K8 8384

(B) K82 448

(C) K26 896

(D) K 20 960

265. Using the details in question above and you gross profit figure, calculate the rate of stock turn

(A) 6 times

(B) 10 times

(C) 15 times

(D) 12 times

PRINCIPLES OF ACCOUNTS

MASTER KEYS

PAPER TWO PART ONE

1 Introduction to accounting

1.1 What is the meaning of Principles of Accounts?

It is process of identifying/recognizing, recording, classifying, summarizing and reporting of business/economic information to stakeholders.

The process of identifying, measuring and communicating economic information to permit informed judgments and decisions by users of that information.

Is the reporting, analyzing and interpretation of recorded information on business transactions?

1.2 Explain the importance of Principles of Accounts

- It is for checks and balances
- To provide information for decision making
- Develop skills in preparing and interpreting economic/business information
- Develop an understanding of accounting concepts, principles, procedures and terminology

Develop skill of numeracy, literacy, communication and enquiry

Encourage attitude of accuracy, orderliness, logical thought and an appreciation of professional ethics

Develop an understanding of the role of accounting in providing an information system for monitoring progress and assessing performance of business.

1.3 Identify career prospects in the Accounting Profession

- Accountant
- Bookkeeper
- Cashier
- Bursar
- Financial Controller
- Assistant Accountant
- Financial Manager
- Finance Minister

1.4 Identify the Accounting Concepts.

- Historical Cost
- Prudence
- Going Concern
- Business entity
- Realization
- Objectivity
- Dual aspect
- Consistency
- Accrual
- Materiality
- Periodical
- Money measurement

1.5 Explain the accounting concepts

1) *Historical Cost –*

It states that assets must be recorded and shown in the books of accounts at the cost price at which they were acquired and not at selling or market value, and that this is the basis for revaluation of the asset.

2) *Prudence*

Requires that a degree of caution/judgement must be exercised in making the estimates required under conditions of uncertainty (e.g. decisions relating to bad debts and allowances for doubtful debts), such that assets and income are not overstated and liabilities and expenses are not understated. To take into account unrealized losses.

3) *Going Concern*

Under this concept it is assumed that the business will continue to operate for a foreseeable future after the end of the reporting period. Business will continue for a long time

4) *Business entity –*

Implies that the affairs of a business are to be treated as being quite separate from the private/personal activities of its owner(s). Assumptions that only transactions that affect the firm and not the owner's private transactions will be recorded.

5) *Objectivity*

the use of a method which arrives at a value that everyone can agree with because it is based upon a factual occurrence.

6) *Dual aspect –*

this states that there are two effects to every economic activity, one represented by the assets of the business and the other by the claims against them. The concept states that these two aspects are always equal to each other. Double entry system means every transaction will be posted on the Dr and Cr side with the same amount

Assets = Capital + Liabilities

7) *Consistency*

Transaction of a similar nature should be recorded in the same way in the same accounting period and in all future accounting periods.

Accrual – Net Profit is the difference between revenues and the expense incurred in generating those revenues i.e. Revenues – Expenses = Net Profit

The effects of transactions and other events are recognized when they occur and they are recorded in the books and reported in the financial statements of the period to which they relate.

Materiality –means an item purchased will be treated as an expense or fixed asset according to the size of the organization and accountants' judgment.

Items of material value are recorded as assets and

2 Business environment and transactions

1.6 2.1 What is a business

is any activity undertaken for the purpose of making a commercial/economic gain or benefit .

2.2 Components of a business

These are features and activities that characterize the operations of business. The following are the main features of a business:

a) Capital/equity/investment
b) Assets
c) Liabilities
d) Expenses
e) Income
f) Transactions.

1.6.1.1 Capital/equity/investment

Capital is often called the owner's equity or net worth. It comprises the funds invested in the business by the owner plus any profits retained for use in the business less any share of profits paid out of the business to the owner.

These are resources/ funds/money that are used to start a business. They are transferred from the owner to the business. the transfer of money from the owner to the business means that the owner has lent money to the business.

Thus capital represents what the business owes the owner/investor.

1.7 Assets

These are resources that are owned by the business and are used to generate revenue or income. They are acquired using the capital invested in the business. They are property or possessions of the business used for production of goods and services. Thus: capital = assets

There are various ways of identifying and classifying assets. The common way is to classify them according to time. Thus we have fixed or non-current and current or circulating assets

Fixed assets are assets which have a long life bought with the intention to use them in the business and not with the intention to simply resell them, e.g. buildings, machinery, fixtures,motor vehicles.

Current assets are assets consisting of cash, goods for resale or items having a short life. For example, the value of stock in hand goes up and down as it is bought and sold.

1.8 Liabilities

Liabilities are resources owed by the business to other people or organizations. Liabilities represent the business obligation to pay somebody for services, goods or cash received from that individual.

Liabilities are settled using assets.

Liabilities are classified into two main classes. Current and long term liabilities.

1.8.1.1.1 Current liabilities

Current liabilities are those liabilities which are expected to be paid within a year. They are settled using current assets.

Examples of current liabilities include: trade creditors, bank overdraft, tax dues, accrued expenses,

Long term liabilities

Long term liabilities are those labilities which repaid over long period or period exceeding one financial year.

Examples of long term liabilities include: capital, bank loan, mortgage, debentures, bonds and securities etc.

Thus the equation:
Assets = Capital + Liabilities
Expressed in terms of capital the equation is:
Capital = Assets - Liabilities.
A statement which a list of assets set against the liabilities is called a balance sheet. sometime referred to as the position statement.
Exercise
Classify the following items into liabilities and assets:

(a) Motor vehicles	(f) Owing to bank
(b) Premises	(g) Cash in hand
(c) Creditors for goods	(h) Loan from D Jones
(d) Stock of goods	(i) Machinery
(e) Debtors.	

2 Transactions and their effects on the balance sheet.

1.9 3.1 define a business transaction:-

A transaction is defined as an exchange of goods or services for money or money equivalent.

1.10 Identify different types of transactions

Cash transaction – A cash transaction is one which there is immediate transfer/payment of cash or cash equivalent for goods or services .
Bank transaction – A transaction in which the exchange of cash for goods or services is done through the bank or using a banking facility such as a cheque or deposit slip.

Credit transaction – A credit transaction is one in which goods supplied or services rendered against a promise given by the receiver of goods or services, to pay at a future date. In this case the supplier of the goods or service is known as a creditor while the receiver is known as a debtor. The promise to pay at a later date is a debt due and payable to the supplier.

Contra Transaction – contra transactions are movement of funds within the enterprise that do not involve inflow or outflow of funds as far as the enterprise is concerned. An example is the banking of cash takings from the office to the bank account of the enterprise or withdrawal of money from the bank account of the enterprise to meet office expenses.

Barter transaction – involves the exchange of goods for goods

1.11 Effects of transaction on the accounting equation

Every transaction affects two items in the accounting equation. Sometimes that may involve the same item being affected twice, once positively (going up/increase) and once negatively (going down/decrease).

Every transaction affects two items in the balance sheet.

TRANSACTION	EFFECT ON ASSET	EFFECT ON LIABILITIES
(1) Owner pays capital into the bank	Increase asset cash at bank	Increase liability – capital or owners equity
(2) Buy goods by cheque	Increase asset stock Decrease asset cash at bank	
(3) Buy goods on credit	Increase asset stock	Increase liability creditor
(4) Sale of goods on credit	Decrease asset stock Increase asset debtor	No effect on liability
(5) Sale of goods for cash (cheque)	Increase asset cash Decrease asset stock	No effect on liability
(6) Pay creditor	Decrease asset	Decrease liability
(7) Debtor pays money owing by cheque	Increase asset cash	No effect on liability
	Decrease asset debtors	
Owner takes money out of the business bank account for own use	Decrease asset	Decrease capital
Owner pays creditor from private money outside the firm	Decrease liability	Increase capital

Exercise

(i) After the preparation of the firm's balance sheet, it was discovered that the following errors had been committed in the books of accounts.
(ii) Furniture bought on credit for k450,000 had been entered in the purchases day book.
(iii) Machinery disposed of for k600,000 had been included in the sales day book
(iv) A cheque for k990,000 from a debtor for goods sold to him at k1000,000 on credit had not been recorded in the books
(v) Goods worthk250,000sold to a customer but not yet delivered had been included in the closing stock
(vi) Motor vans standing at k10,000,000 should have been depreciated at 20%
(vii) The firm should have provided for discount on debtors total of k550,000 at 10%.
(viii) Goods amounting to k150,000 taken by the owner of the business had been included in the sales figure.

Required :

In order to adjust the for each of the errors above , state which items in the balance sheet should be increased or decreased.

Complete the table below:

error	Item to be increased	Items to be decreased
i		
ii		
iii		
iv		
v		
vi		
vii		

Q3.Fill in the missing amounts in the following table.

	Assets	Liabilities	Capital	Answers
A	128,600	84,000	?	Cap=asset – Liab=446000
B	?	56,400	28,400	Asset=cap+Liab=84,800
C	250,400	?	114,800	Liab=Assets – cap=135,600
D	?	111,500	88,500	Assets=capital=200,000
E	216,500	104,300	?	Cap=Asset – Liab=112,200
F	314,100	?	146,300	Liab=Asset – cap=167,800

Q2. F. Mwale had the following assets and Liabilities as @ 1st June, 2006

Premises	20,000
Planted and machinery	14,000
Motor vehicle	10,000
Stock of goods	1,456
Debtors	2,484
Creditors	6,434
Cash in hand	1,200
Bank overdraft	4,608

Required

Calculate his capital as at1st June, 2006.

Workings.

Capital= Assets-Liabilities

=49,140,000 - 11,042,000 = 38,098,00

1.12 Recording business transactions:

A record of business transactions is called an account. A collection of accounts is called a ledger.

1.13 CLASSIFICATION OF ACCOUNTS:

All accounts that form up the ledger can be grouped into three classes;

- Real
- Nominal and
- Personal

1.1.1. Personal accounts:

These are account of individual persons and organizations with whom the business deals. These are credit customers (debtors) and suppliers of goods on credit (creditors) .eg. Mwansa, Zambia sugar, ShopRite, chalikosa

1.1.2. Nominal accounts;

These are accounts that exist in name only i.e. they identify the activities or services performed by or to the business. all expenses such as rent, salaries, carriage, freight charges, purchases, bills including loses such as bad debts, depreciation, and drawings and gains/ income accounts such as sales, rent received, commission received, including capital are nominal accounts.

1.1.3. Real accounts;

These are accounts that keep records of the assets of the business i.e. accounts of all the possessions of the business. They are sometimes called asset accounts. examples include land and buildings account, motor vehicle account etc.

PRACTICE QUESTION

Classify the following accounts as either real, nominal or personal accounts;

i. Premises
ii. Major ltd account
iii. Insurance account
iv. Muyunda's account
v. Bank account
vi. Rent received account
vii. Cash account
viii. Sub divisions of the ledger

1.14 Procedure for recording business transactions.

Processing a business begins with recording the information on a source document. The following table summarizes the common and usual business transactions and the source document prepared in each case.

Transaction	Source document	Account. Debited	Account Credited	Subsidiary book	Ledger class
Cash sales	Duplicate receipt	Cash account	Sales account	Cash book	General
Credit sales	Duplicate invoice	Debtors/ customer	Sales account	Sales journal	Debtors ledger
Cash purchases	Orig.receipt	purchases	Cash account	Cash book	General ledger
Credit purchases	Original invoice	Purchases	Creditors/supplier	Purchases journal	Creditors ledger
Returns in	Credit note	Sales returns	Customers/debtors	Returns in.journal	Debtors ledger
Returns out	Debit note	Suppliers/creditors	Purchases returns	Returns out journal	Creditors ledger
Purchase of fixed asset on cash	receipt	f/Asset account	Cash account	General journal	General ledger
Purchase of fixed asset	Invoice/Journal voucher	f/asset account	Suppliers account		

on credit					
sale of fixed asset cash/cheque	Copy receipt/JV	Cash/bank	Asset disposal	General journal	General ledger
Small daily expenses	Petty cash voucher	Expense account	Petty cash	Petty cash book	General ledger

1.15 Recording transactions in their appropriate ledger accounts.

According to the dual aspect concept, every transaction has twofold effect on the position of the business. It is therefore important that the two accounts are identified, classified and recorded appropriately. The double entry rule applies. The rule states that

For every debit entry there must be a corresponding credit entry.

Note also that this rule applies differently on the three classes of ledger accounts.

1.15.1.1 ***For all real accounts****:*

Dr. what comes in or the increase in value and;

Cr. what goes out or the decrease in value.

1.15.1.2 ***For all person accounts****:*

Dr. the person who receives the value or simply the receiver and

Cr. the person who gives out value or simply the giver.

1.15.1.2.1 For all nominal accounts***;***

Dr. all expenses and loses

Cr. all incomes, gains and liabilities.

Example

Cash Transaction

1/06/17 - Sold goods K2,300 cash

Cash Account

Date	Particulars	F	DR (K)	CR (K)
1/06/17	Sales		2,300	

Sales Account

Date	Particulars	F	DR (K)	CR (K)
1/06/17	Cash			2,300

Bank Transaction

2/06/17 – Bought goods for re-sale at K4,000 by cheque

Bank Account

Date	Particulars	F	DR (K)	CR (K)
2/06/17	Purchases			4,000

Purchases Account

Date	Particulars	F	DR (K)	CR (K)
2/06/17	Bank		4,000	

Credit Transaction

3/06/17 - Bought goods on credit from H. Banda K3,000

Purchases Account

Date	Particulars	F	DR (K)	CR (K)
3/06/17	H. Banda		3,000	

H. Banda

Date	Particulars	F	DR (K)	CR (K)
3/06/17	Purchases			3,000

Contra Transaction

4/06/17 – Withdrew cash from bank, K1,000

Cash Account

Date	Particulars	F	DR (K)	CR (K)
4/06/17	Bank		3,000	

Bank Account

Date	Particulars	F	DR (K)	CR (K)
4/06/17	Cash			3,000

REVISION EXERCISE

I /06/ 2017 Bwalya started business with K20000 cash
3/06/2017 bought goods by cash K5000
4/06/2017 paid rent by cash K1000
10/06/2017 deposited K8000 of the cash into the bank.
12/06/2017 Bought building by cheque K120
20/06/2017 sold goods by cheque K600

2 4 books of prime entry

- What are books of prime entry?
- Identify the types of books of prime entry
- Explain what each book of prime entry is used for
- Identify and explain the source document(s) used to prepare each book

- Enter transactions in each book of prime entry
- Distinguish between a trade discount and a cash discount
- Post each book to the ledger
- Extract a trial balance

Books of prime entry are books where transactions are first recorded. They are sometimes referred to as subsidiary books.

Outline the books of prime entry

i. Examples of these books are:
ii. Cash Book
iii. Petty Cash Book
iv. Purchases Day Book
v. Sales Day Book
vi. Purchases Returns Day Book
vii. Sales Returns Day Book
viii. General Journal or Journal Proper

2.1 4.1 Cash Book

State the subsidiary book and explain the type of transactions which are recorded in each of them.

The cash book is a book of prime entry in which cash transactions are recorded.

Cash transactions are those in which goods are exchanged for cash in the form of notes and coins, or are paid for using the cheque system and the debit cards (ATM Cards). Cash transactions involving the exchange of notes and coins with goods are used to compile the cash account.

Transactions involving Cheques are used to compile the bank account.

2.1.1.1 PREPARING A CASH BOOK

The cashbook is the only book of prime entry that is also part of the ledger.

The cash book is a real account and the application of the double entry is:

- Dr what comes in/inflow/increase and
- Cr what goes out/outflow/decrease

The cash book with only cash and bank accounts is called the two column cash book.

When the discount column is included the cash book is called the three-column cash book.

The discount column has two sections- The discount allowed and received columns.
Cash discount is an allowance given whenever a debt is settled with in a given time.

The allowance given by the business to its customers/debtors to encourage prompt settlement of amounts owed is called allowed.

Discount allowed is a loss to the business as it reduces the value of the asset debtors.

The allowance given to the business by the creditors/suppliers when it pays its debts is called discount received.

Discount received is a gain to the business as reduces the value of the liability creditors.

The debit side of the cash book (bank/cash account) records cash inflows from:

Sales, rent received, commission received, receipts from debtors.

Transfers of cash from the bank to the office- contra entries

Cash withdraws for personal use - drawings

The credit side of the cash book (bank and cash) records

Payments to suppliers, cash purchases, rent and rates, salaries and wages, bills.

Transfers of cash to bank account- contra entries

Cash account of the cash begin with a debit balance and may end with either debit or nil balance.

The debit balance on either cash or bank account of the cash represents cash available in hand. A special case sometimes occurs where the bank account of the cash book shows a credit balance.

This means that the account has been overdrawn. This state is called a bank overdraft. The business has borrowed from the bank.

CONTRA ENTRIES

Where a transaction's double entry is completed within the cash book, it is known as a contra entry.

Examples are:

- Cash paid into the bank from cash till
- Cash withdrawn from the bank for business use.

The letter 'c' is inserted in the folio column to denote that an item is a contra.

Example 1

Record transactions in D. Nyirenda's Cash Book for January, 2004.

01. Bank K6 000 000
16. Sales by cheque K5 500 000
20. Bought goods paying by cheque K1 500 000
22. Bought a motor vehicle paying by cheque K10 000 000
24. Paid for traveling expenses by cash K400 000
27. Withdrew cash from the bank for business use K4 500 000
28. Bought a machine paying by cash K4 000 000
30. Received a cheque for K2 500 000 as a loan from P Lubasi
31. Paid salaries by cheque K2 000 000

D. Nyirenda's Cash Book for January, 2004

DATE			CASH ACCOUNT		BANK ACCOUNT		DISCOUNTS	
2004	DETAILS	FOL	DR	CR	DR	CR	ALL	REC'D
JAN-1	balances sales				6,000,000 5,500,000			

	purchases					1,500,000		
16	motor vehicle					10,000,000		
	Traveling			400,000				
20	expenses		4,500,000					
	Cash/ bank			400,000				
22	Machinery				2,500,000			
	p. lubasi					2,000,000		
24	salaries	c/d				500,000		
	balances							
27								
28								
30								
31								
			4,500,000	4,500,000	14,000,000	14,000,000		
	Balances	b/d			500,000			

QUESTION 2

Enter the following transactions in the three-column cash book of J Pokololo, a general dealer. Balance off the cash book at the end of the month and post the cash book to the ledger.

20x5

May 1 Balances brought down from April:

Cash balance	K926 000
Bank balance	K 6 450 000
Debtors accounts:	
A Maambo	K240 000
B Kolwe	K460 000
Creditors accounts:	
V Mbao	K300 000
C Mwewa	K160 000

3 Cash sales K144 000.

4 Purchased goods by cheque K860 000.

5 A Maambo paid us by cheque K220 000, having deducted K20 000 cash discount.

8 Paid V Mbao's account by cash, deducting 5% cash discount.

10 Paid wages by cash K250 000.

14 Received K430 000 cash from B Kolwe, cash discount K30 000.

16 Deposited cash into the bank K600 000.

20 We paid C Mwewa by cheque, deducting 10% cash discount.

24 Sales by cheque K420 000.

Three-column cash book of J Pokololo

DATE			CASH ACCOUNT		BANK ACCOUNT		DISCOUNTS	
2004	DETAILS	FOL	DR	CR	DR	CR	ALL	REC'D
MAY-1		b/f						
16								
20								
22								
24		c/d						
27								
28								
30								
31								
	Balances	b/d						

NOTE:

1. The opening balances for debtors and creditors should not be entered in the cash book but entered in the respective debtors and creditors accounts in the sales ledger and purchases ledger.
2. The corresponding double entries for the total discounts are entered in the personal accounts of debtors and creditors.
3. All. Stands for discount allowed while Rec. stands for discount received

4.2 The petty cash book

- Petty cash is used to make small payments.
- Petty cash must be kept safely in a lockable cash box.
- Because of its nature, for security reasons petty cash should be in the hands of a responsible officer and that not everybody in an organization is eligible for petty cash.
- Petty cash is operated on an imprest system. This is where the petty cashier is reimbursed what has been spent in order to restore the imprest amount.

Thus:	FLOAT	xx
	Less expenditure	xx
	Balance	xx
	Reimbursement	xx
	FLOAT	xx

All payments out of petty cash must be fully authorized by signing on the voucher.

- If there's no receipt (document) to support the claim, the petty cashier must consult the supervisor.
- Entries made (recorded) in petty cash book originate from a document called petty cash voucher.

- The petty cash book is used as an accumulative book for small expenses of which the totals for the period are transferred to respective expense account in general ledger.

Petty cash expenditure involving Value Added Tax, should be recorded separately in petty cash book with separate amounts in the Value Added Tax column

Analysis Columns

The petty cash book has analysis columns such as:-

Postage - eg. Parcels, letters, stamps.

Stationery - eg. Pens, envelopes, books, pencils.

Office expenses- eg. Coffee, tea, sugar, milk.

Motor Expenses- repairs, fuel.

Travelling- travel, transport expenses, logistics.

Sundry Expenses- beverages, milk, etc.

Cleaning- detergents, disinfectants.

RECORD TRANSACTIONS IN THE PETTY CASH BOOK

QUESTION:

The following is a summary of the petty cash transactions of JK Ltd for May 20x5:

May 1. Received from cashier K300 000 as petty cash float

Payments for the month were as follows:

2.	Postage	K18 000
3.	Travelling	K12 000
4.	Cleaning	K15 000
7.	Petrol for delivery van	K22 000
8.	Travelling	K25 000
9.	Stationery	K17 000
11.	Cleaning	K18 000
14.	Postage	K5 000
15.	Travelling	K8 000
18.	Stationery	K9 000
18.	Cleaning	K23 000
20.	Postage	K13 000
24.	Service of delivery van	K43 000
26.	Petrol	K18 000
27.	Cleaning	K21 000
29.	Postage	K5 000
30.	Petrol	K14 000

You are required to:

Rule up a suitable petty cash book with analysis columns for expenditure on: cleaning, motor expenses, postage, stationery, and traveling.

Enter the month's transactions

Enter the receipt of the amount necessary to restore the imprest and carry down the balance for the commencement of the following month.

Show how the double entry for the expenditure is completed.

4.3 PURCHASES DAY BOOK

Explain the purchases day book

'Purchases' refers to items bought for resale, whether by cash or on credit.

The purchases day book is a book where we record items bought on credit for resale.

The source document for the purchases day book (also known as purchases journal) is the purchase invoice (or original invoice).

Record transactions in the purchases day book

QUESTION:

From the following transactions, you are to prepare the purchases day book, post the book to the ledger and extract a trial balance as at 31 January 20x5:

20x5

Jan. 3 Credit purchases from: B Zimba K580 000; J Phiri K360 000.

18 Bought goods on credit from: C Banda K900 000 less 10% trade discount.

26 Bought goods on credit from: D Soko K600 000 and B Zimba K800 000 less 10% trade discount

Solution

Purchases Day Book

Date	Details	Invoice no	Amount
20x5			K'000
Jan 3	B Zimba	004	580
3	J Phiri	098	860
18	C Banda	014	810
26	D Soko	066	600
26	B Zimba	042	720
31	**Transfer to purchases account**		**3 57**

4.4 THE SALES DAY BOOK

'Sales' in accounting refers to the sale of items previously bought.

The source document for the sales day book (also known as sales journal) is the sales invoice (or duplicate invoice).

Record transactions in the sales day book

QUESTION

B kayumba had the following credit purchase and sales for the month of May 2015:

You are to prepare kayumba's purchases and sales day book only.

May 1 bought good from A.Banda:

5kg of sugar at k20 per kg

3kg of salt at k5 per kg

May 5 sold goods to Hatwaambo:

5kg of rice at k30 per kg

10 bags of potatoes at k20 each

May 10 bought goods on credit from K Mwandu at k20 on credit
May 16 bought goods on credit from p Mwale:
2kgs of rice at k7 per kg
1 bag of potatoes at k25
May 31 Sold goods on credit to B N'gandu
20 kg of caster sugar at a total of k100

B.KAYUMBA'S PURCHASES DAY BOOK FOR THE MONTH OF MAY

DATES	SUPPLIERS NAME	Inv.NO.	Add	Totals
01.05.16	A. Banda			
	5kg sugar @ k20 each		100	
	3Kg salt @k5 each		15	
				115
10.05.16	K. Mwandu			
	1kg sugar @ k20		20	20
16.05.16	P. Mwale			
	2kg rice@k7 each		14	
	1 bag of potatoes @ k25		25	
				39
	debit purchases account in the GL			174

B. KAYUMBA'S SALES DAY BOOK FOR THE MONTH OF MAY 2016

DATES	CUSTOMERS NAME	INV.NO	Add	total
05.05.16	Hatwaambo			
	5kg of rice @ k30 per kg		150	
	10 bags of potatoes @ k20 each		200	
31.05.16	B.N'gandu			350
	20 kg of caster sugar @ k100			100
	credit sales account in the GL			450

C Simwanza, a sole trader specializing in material for Nigerian clothing , has the following purchases and sales for March 20x5:
March 1 Bought from Mulila stores: silk K360 000, cotton K720 000. All less 25% trade discount
8 Sold to A Gondwe: linen items K252 000, woolen items K396 000. no trade discount.
15 Sold to B Hanzala: silk K324 000, linen K1 296 000, cotton items K1 080 000. All less 20% trade discount.
23 Bought from C Kwabe: cotton K792 000, linen K468 000. All less 25% trade discount.
24 Sold to D Shawa: linen items K378 000, cotton K432 000. All less 10% trade discount.
31 Bought from J Mudenda: linen items K2 478 000. Less 33⅓% trade discount.
Required:
a) prepare the purchases and sales journals for C Simwanza from the above
b) post the items to the personal accounts
c) post the totals of the journals to the sales and purchases accounts.

4.5 PURCHASES RETURNS DAY BOOK

Explain the purchases returns day book
A Purchases Returns Day Book is a book in which goods bought for resale but are returned by the buyer to the supplier and are recorded in the purchases day book.

- Reasons for returns
- Customers are oversupplied
- Goods sent are of a wrong color, type or make.
- Goods are damaged in transit to the customer.

Whenever goods are returned to a supplier, the customer sends a debit note to the supplier.
RECORD TRANSACTIONS IN THE PURCHASES RETURNS DAY BOOK
Solution
Purchases returns day book

Date	Details	B/N no	Amount
20x5			K'000
Jan 5	J Phiri	0010	160
20	C Banda	0011	180
28	B Zimba	0012	162
Transfer to purchases returns account			502

4.6 SALES RETURNS DAY BOOK

Explain the sales returns day book
The sales returns day book is a book where we record goods returned to us by our customers.
Whenever goods are returned by a customer, a credit note is sent to the customer.
RECORD TRANSACTIONS IN THE SALES RETURNS DAY BOOK
QUESTION:
B Musonda experienced the following returns inwards during the month of February 20x5:
Feb 6 Returns from C Mate K84 000
18 Returns from Z Buumba K42 000
27 Returns from M Chalwe K60 000
Enter the above transactions in the sales returns day book and post the book to the ledger.
Solution
Sales returns day book

Date	Details	C/N NO.	Amount
20x5			K'000
Feb 6	C Mate	0126	84
18	Z Buumba	0127	42
27	B Zimba	0128	60
28	Transfer to sales returns account		186

You are to enter up the sales, purchases and the returns inwards and returns outwards journals from the following details, then to post the items to the relevant accounts in the sales and purchases ledgers. The total of the journals are then to be transferred to the accounts in the general ledger.

20x5

May 1 Credit sales: T Tamba K504 000; L Dimba K1 332 000; K Banda K1 305 000.

3 Credit purchases: P Phiri K1 296 000; H Hantobolo K225 000; B Sinda K684 000.

7 Credit sales: K Kwabe K801 000; N Malama K702 000; N Lombe K2 313 000.

9 Credit purchases: B Mpafya K216 000; H Hantobolo K522 000;
H Muleta K1 107 000.

11 Goods returned by us to: P Phiri K108 000; B Sinda K198 000.

14 Goods returned to us by: T Tamba K45 000; K Banda K99 000; K Kwabe K126 000.

17 Credit purchases: H Hantobolo K486 000; B Mpafya K585 000; L Ntembe K675 000.

20 Goods returned by us to: B Sinda K126 000.

24 Credit sales: K Mutinta K513 000; K Kwabe K585 000; O Gondwe K1 008 000.

28 Goods returned to us by: N Malama K216 000.

31 Credit sales: N lombe K495 000.

7. JOURNAL PROPER (GENERAL JOURNAL)

The word journal means 'a book containing the record of events as they occur day by day'.

Examples of entries made in the journal proper are:

- Purchase and sale of fixed assets on credit
- Opening entries Correction of errors
- Transfer of items between accounts
- Creation, increase or decrease of provisions and reserves

The journal shows:

- The name(s) of the account(s) to be debited and the amount(s)
- The name(s) of the account(s) to be credited and the amount(s)
- A brief explanation of the transaction called a narrative (narration)

RECORD TRANSACTIONS IN THE JOURNAL PROPER

The layout for the journal is as follows:

Journal proper_

Date	Details	F	Dr	Cr
20x5			K'000	K'000
Jan 1	Name of account to be debited		xxx	
	Name of account to be credited			xxx
	Narrative			

QUESTION:

To illustrate the recording of entries in the journal proper, we shall only look at three groups of entries:

Purchase and sale of fixed assets on credit

Transfers between ledger accounts

Opening entries

a) Purchase and sale of fixed assets on credit

i) On 4th May 20x5, a company bought a machine on credit from Major Ltd for K10 million.

Record the transaction in the journal and post it to the ledger.

Solution.

JOURNAL PROPER

Date	Details	F	Dr	Cr
20x5			K'000	K'000
May 4	Machinery		10 000	
	Major Ltd			10 000

c) Opening entries

These are the entries required to open up a new set of books e.g. when a trader decides to keep his books on a double entry principle. Opening entries are simply entries showing the financial position of a business as at the time a new set of books is to be opened. The excess of assets over liabilities at that date is the capital of the business.

In practice, opening entries may be made only once in the lifetime of the business. However, many book keeping exercises commence by requiring you to do the opening entries.

When opening a new set of books, all assets should have debit opening balances while liabilities and capital should have credit opening balances.

QUESTION:

B Maala has been in business for sometime without keeping proper accounting records. He has now decided to have a full double entry set of books.His assets and liabilities on 1st May 20x5 are as follows:

Assets: Buildings K7 000 000; Motor van K4 500 000; Stock K1 200 000; Debtors: - C Bwalya K6 000 000, O Moono K400 000; Cash at bank K850 000 and Cash in hand K300 000.

Liabilities: Creditors:- W Chansa K750 000, E Kasonde K600 000.

Step 2 Having identified the books, you should now record the transactions in the respective books. For our question, the entries in the books will be as follows:

JOURNAL PROPER

Date	Details	F	Dr	Cr
20x5			K'000	K'000
Jan 1	Buildings		24 000	
	Motor vehicle		16 000	
	Stock		3 000	
	Debtors: - V Lubinda		5 500	
	- M Tembo		3 000	
	Cash at bank		4 200	
	Cash in hand		1 800	
	Creditors: - D Banda			6 000
	- E Kasonde			1 000
	Capital (bal. Fig.)			50 500
			57 500	57 500
	Being assets, liabilities and capital entered to open a new book			
Jan 13	Motor vehicle		14 000	

Toyota (Z) Ltd	14 000	
Purchase of a motor vehicle from Toyota (Z) Ltd on credit		

32 5.THE TRIAL BALANCE - INTRODUCTION

32.1 OBJECTIVES QUESTIONS

- Define a trial balance
- Explain the purpose of a trial balance
- Extract a trial balance from ledger.

32.1.1.1 What is a trial balance?

A trial balance is defined as a list of debit and credit balances extracted from the ledger which when added the totals must be equal.

32.1.1.2 ***Explain the purpose of the trial balance.***

The purpose of a trial balance is:

To check the arithmetic accuracy or errors from the ledger.

To check whether the double entry has been completed.

To check fraud.

By virtue of the principle of double entry book-keeping, the totals of debit and credit balances must agree. Should this not be the case, then there must be an error in the books of account.

32.2 5.1 PREPARE A TRIAL BALANCE

The first task in preparing a trial balance is to balance all the ledger accounts, and then the balances must be extracted and entered in the trial balance. When extracting the trial balance, the following points should be taken note of:

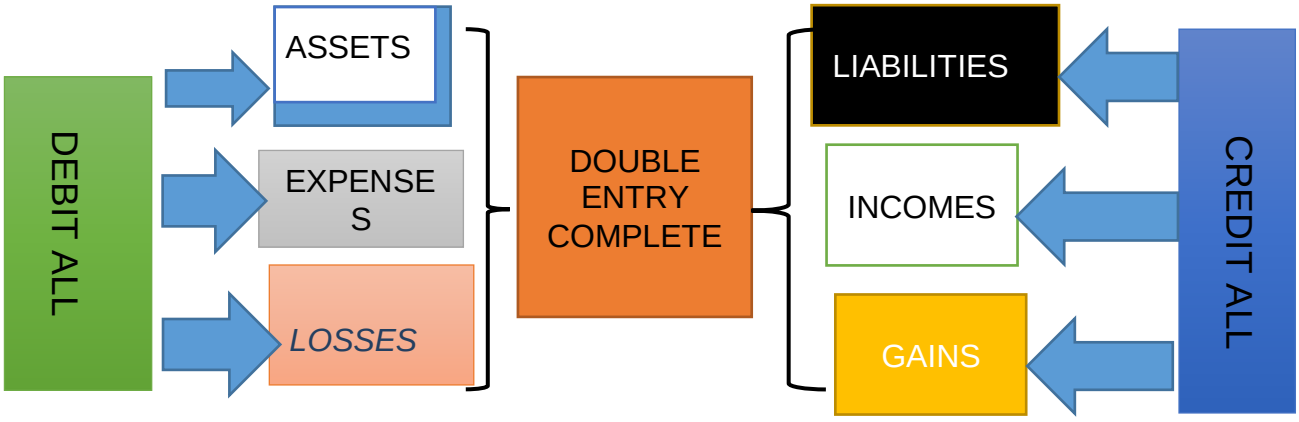
Accounts with debit balances include the following classes of accounts:

Dr. Assets, Expenses & Losses. Hence the acronym DR.A.E.

Accounts with credit balances include the following classes of accounts.

Cr. Incomes, Liabilities & Gains. Hence the acronym = CR.I.L.G

Therefore, trial balance construction is guided by the following model



QUESTION 1

You are required to prepare a Trial Balance and balance it as at 31/03/09

	K
Purchases	61, 420
Sales	127, 245
Stock (inventory)	7, 940
Capital	25, 200
Bank overdraft	2, 490
Cash	140
Discount received	62
Discount allowed	2, 480
Returns inwards	3, 486
Returns outwards	1, 356
Carriage outwards	3, 210
Rent & insurance	8, 870
Allowance for doubtful debts	630
Fixtures and fittings	1, 900
Van	5, 600
Debtors	12, 418
Creditors	11, 400
Drawings	21, 400
Wages & salaries	39, 200
General office expenses	319

Solution

TRAIL BALANCE (as at 31st march, 2009)

Details	**DR K**	**CR K**
Purchases	61, 420	
Sales		127, 245
Stock (inventory)	7,940	
Capital		25, 200
Bank overdraft		2, 490
Cash	140	
Discount received		62
Discount allowed		

Returns inwards	2, 480	
Returns outwards	3, 486	1, 356
Carriage outwards	3, 210	
Rent & insurance	8, 870	
Allowance for doubtful debts		630
Fixtures & fittings	1,900	
Van	5, 600	
Debtors	12, 418	
Creditors		11, 400
Drawings	21, 400	
Wages & salaries	39, 200	
General office expenses	319	
	168, 383	168, 383

QUESTION 2

The following trial balance was drawn by an inexperienced book-keeper on 30 June 2009.

J. MULEYA TRIAL BALANCE For the month ended 30 June 2009

ACCOUNT TITLE	DR	CR
Sales	19 740	
Purchases		11 280
Cash at bank	1140	
Cash in hand		210
Capital (1 July 2008)		9 900
Drawings		2 850
Office furniture	1 440	
Rent	1 020	
Wages and salaries		2 580
Discount allowed	640	
Discount received		360
Debtors	4 970	
Creditors		2 490
Stock (1 July 2008)		2 970
Provision for bad debts (1 July 2008)		270

Delivery vans Vans running expenses Bad debts written off Suspense account	2 400 450 810 300	
	32 910	32 910

The following transactions had been omitted from the records while others had been wrongly recorded:

P. Njakule, a debtor owing K200, had been declared bankrupt but no record had been made in the books.

Vans running expenses, K100, had been recorded in the delivery vans account.

The proprietor, J. Muleya, had taken goods worth K80 for his personal use. No record was made in the books.

An invoice for K300 received from W. Shitisha had been misplaced.

Required:
Draft the correct Trial Balance with correct heading. Show how it would appear after posting the transactions (i) to (i) to the appropriate accounts.

J. MULEYA
REDRAFTED TRIAL BALANCE AS AT 30 JUNE 2009

	DR	CR.
Purchases/sales	11, 500, 000	19, 740, 000
Bank	1,140, 000	
Cash	210, 000	
Capital (01/07/08)		9, 900, 000
Drawings	2, 930, 000	
Office furniture	1, 440, 000	
Rent	1, 020, 000	
Wages and salaries	2, 580, 000	
Discounts	640, 000	360, 000
Debtors /creditors	4, 770, 000	2, 790, 000
Stock (01/07/08)	2, 970, 000	
Provision for bad debts		270, 000
Delivery vans	2, 300, 000	

Vans running expenses	550, 000
Bad debt written off	1,010, 000
33, 060,000	33, 060, 000

NOTES:

- *Debtors – reduced or credited k200*
- *Bad debt increased by k200*
- *Motor Van expenses increased by k100 and delivery van reduced by a k100*
- *Drawings increased by k80 then purchases reduced by k80.*
- *(11280- 80)= k11200*
- *Purchases increased by k300 and creditors increased by k30*

Activity:

The Trial Balance below related to the business of Kandolo as at 31st March, 2015, the end of the month.

	Dr	**Cr**
	K	K
Sales		70 000
Purchases		30 000
Debtors		45 000
Creditors	20 000	
Cash at bank		15 000
Petty cash	5 000	
Sales returns		1 000
Purchases returns	1 500	
Equipment	18 000	
Machinery		28 000
Capital	52 000	
Carriage inwards	1 500	
	98 000	189 000

The above Trial Balance was prepared by an incompetent Book- keeper. You are required to re-draft it correctly with a correct heading.

33 FINAL ACCOUNTS OF SOLE TRADERS

33.1 Objective questions

a) What is meant by the term final accounts
b) Explain the purpose of the trading account
c) Explain the difference between gross profit and net profit
d) Prepare a trading account from the given information
e) Define and Explain how to deal with the following items when preparing a trading account:
   - Opening and closing stocks
   - Returns inwards and outwards
   - Trading expenses

a) Explain the purpose of the profit and loss account.

b) Prepare the profit and loss account from the given information
c) Define a balance sheet
d) Explain the order of permanence and liquidity for showing fixed and current assets in the balance sheet.
e) Prepare the trading, and profit and loss account from information given in a trial balance.
f) Draw up a balance sheet from the information given.

33.2 FINAL ACCOUNTS

Also known as Financial Statements

33.2.1.1 WHAT ARE FINAL ACCOUNTS?

The term final account is used to refer to the stage in the accounting process at which business activities are summarized and reported. Three statements are presented to communicate the performance, profitability and position of the business

- Performance - Trading account,
- Profitability - Profit and loss account
- Financial position - Balance sheet (although a balance sheet is not an account).

NOTE

Trading Account and profit and loss account are also known as INCOME STATEMENTS. It is made up of nominal accounts.

-They are incomes and expenses.

Balance sheet is also known as **position statement**.

-It is made up of assets and liabilities.

TRADING ACCOUNT

33.2.1.2 Explain trading account

- To trade is the buying or selling of goods with the intention of making profit
- A trading account is prepared to calculate the gross profit /loss of the business in a given trading period.

33.2.1.3 Explain the terms used in the trading account

1.1.4. TURNOVER

- Turnover means Net Sales
- It is arrived at by deducting Sales Returns from Sales
- It is the actual value of goods we Sold to our customers

TURNOVER = SALES – SALES RETURNS

1.1.5. OPENING STOCK

- This refers to the value of goods the business has unsold or not yet sold at the beginning of the period.

1.1.6. CLOSING STOCK

- This refers to the value of goods unsold or not yet sold at the end of the trading period.
- To find the closing stock, the business will have to do a Stock Tacking.
- Stock Taking is the physical counting of the goods.

1.1.7. PURCHASES

Purchases are goods bought for resale.

1.1.8. PURCHASES RETURNS

- These are goods bought but have taken them to the seller due to the reasons such as:-
- Damaged in transit, wrong color, wrong size, over supply by the seller.

1.1.9. NET PURCHASES

This is the difference between purchases and purchases returns.

1.1.10. COST OF SALES

- This is the actual cost of goods sold.
- It is the cost of putting goods into a saleable condition.
- The other name is cost of goods sold.
- It is made up of Purchases and other direct expenses like carriage inwards.

33.2.1.4 COST OF SALES = OPENING STOCK – CLOSING STOCK

CARRIAGE

- Carriage refers to the cost of transporting goods from one place to another.

It is divided into two:-

33.2.1.5 CARRIAGE INWARDS

- This is the cost of transporting goods bought into the business.

CARRIAGE OUTWARDS

- This is the cost of transporting goods outside the business to the customers for the sales made.

GROSS PROFIT

- This is profit before deductions of expenses
- Gross profit is the excess of sale over the cost of sales, whereas gross loss is the excess of cost of sales over sales.

QUESTION:

From the following balances, prepare the trading account for W. Koswe for the year ended 30th June 2004:

Sales	K600 000
Sales returns	K50 000
Stock 1st July 2003	K60 000
Purchases	K400 000
Purchases returns	K20 000
Stock 30th June 2004	K70 000.

SOLUTION

W. Koswe

Trading account for the year ended 30th June 2004

	K'000	K'000	K'000
Sales		600	
Less: sales returns		50	
Net sales (or turnover)			550
Less: cost of sales:			
Opening stock		60	
Add: purchases	400		
Less: purchases returns	20		
		380	
Total stock available		440	

Less: closing stock	(70)	
Cost of goods sold		370
Gross profit		180

EXPENSES IN THE TRADING ACCOUNT

DEFINE EXPENSES

Expenses incurred in bringing the goods into the firm/business and those incurred in putting goods into the saleable condition should be charged to the trading account.
Examples of these are:

a) Expenses in buying goods:
   - Carriage inward
   - Customs duty added to purchases.
   - Freight charges

b) Expenses in putting goods into saleable condition:
   - Warehouse wages
   - Warehouse rent added to cost of goods sold.
   - Warehouse light and heat

QUESTION 2
On 31st December 2004, John Banda had the following balances:

Sales K5 000 000

Opening stock K950 000

Purchases K3 000 000

Sales returns K500 000

Purchases returns K450 000

Carriage inwards K250 000

Warehouse wages K300 000

Closing stock K440 000.

You are required to prepare John Banda's Trading Account for the year ended 31st December 2004.

SOLUTION

John Banda
Trading account for the year ended 31st December 2004

	K'000	K'000	K'000
Sales		5 000	
Less: sales returns		500	
Net sales			4 500
Opening stock	950		
Add: Purchases	3 000		
Less: purchases returns	450		
	2 550		
Add: carriage inwards	250		

	2 800	
Total stock available	3 750	
Less: closing stock	(440)	
Cost of goods sold	3 310	
Add: warehouse wages	300	
Cost of sales		3 610
Gross profit		890

33.3 PROFIT AND LOSS ACCOUNT

The profit and loss account is prepared to calculate the net profit/loss in a given trading period. It comprises the gross profit /loss plus any other income other than that from sales, less all other expenses other than the buying expenses incurred by the business. At the end of the accounting period, the net profit or loss is transferred to the capital section in the balance sheet.

Question

Fungai Nkomeki's is an importer of second hand clothes whose trial balance as at 31st,December 2015 is as follows:

Account title	Dr	Cr
Sales		191,600
Purchases	96,680	
Returns outwards		1,920
Stock 1/1/2015	21,560	
Wages	23,000	
Motor vehicles expenses	13,000	
Premises at cost	120,000	
Motor vehicles at cost	40,000	
Provision for depreciation on motor vehicle		30,000
Provision for depreciation on premises		24,000
Rent and rates	15,400	
Light and heat	9,900	
General expenses	12,400	
Discount received		10,600
Provision for bad debts		1,120
Returns inwards	11,600	
Discount allowed	5,400	
8% bank loan repayable 30th,June 2019		60,000
Cash	540	
Bank		3,360
Debtors	37,000	
Creditors		19,500
Drawings	22,620	
Commission received		22,900
Capital		70,000
Insurance	5,900	
	435,000	435,000

Additional information:

1. Stock at 31 December 2015 Was valued at k25,200.

2. 20% of the wages was carriage inwards and 80% selling expenses.

3. depreciation is to be charged on the premises after the sale of one % per annum on cost using the straight line method and 25% per annum on Motor vehicles using reducing balances method.

Depreciation of delivery motor vehicles to be shared 4:1 between selling expenses and carriage inwards.

4. Interest on loan is due on 31 December 2015.

5. Insurance in advance amounted to K900 and electricity due amounted to k260 on 31 December 2015.

6. Provision for doubtful debts is to be maintained at 3% of debtors.

Required:

(a) Prepare trading profit and loss account [income statement] for Fungai Nkomeki for the year 31 December 2015.

(b) Balance sheet as at 31 December 2015.

Solution

Fungai Nkomeki's

Trading Profit and Loss Account for The Year Ended 31 December 2015

PARTICULARS	K	K	K

Sales		191,000	
Less returns inwards			
Net sales or turnover		11,600	180,000
COST OF GOODS SOLD:			
Opening stock			
purchases	96,680	21,560	
Add: wages [20% x 23,000]	4,600		
Depreciation [25% x 10,000 = X1/5]	500		
	101,780		
Less: returns out wards	1,920)		
Net purchases			
Total stock available for sale		99,860	
Less: closing stock		121,420	
Cost of goods sold		(25,200)	
Gross profit			(96,220)
Add : Other Incomes/ Gains			83,780
Discount received			
Commission received		10,600	
Decrease in provision for bad debts [1120-1110]		22,900	
Total additional income		10	
Total profit			33,510
Less: Expenses/ Loses			117,290
Wages [80%X 23,000]			
Motor expenses		18,400	
Rent and rates		13,000	
Light and heat	9,900	15,400	
Add: amount owing	260		
General expenses		10,160	
Depreciation:		12,400	
Premises			
Motor vehicles		1,200	
Interest on loan		2,000	
Discount allowed		4,800	
Total expenses		5,400	
Net profit			(87,760)
			29,530

FUNGAI NKOMEKI'S BALANCE SHEET AS AT 31ST, DECEMBER 2015

FIXED ASSETS	COST	DEP	NBV
Premises	120,000	25,200	94,800
Motor vehicles	40,000	32,500	7,500
Total fixed assets	160,000	57,700	102,300
CURRENT ASSETS			
Stock		25,200	
Debtors	37,000		
Less: provision for bad debts	1,110		
Net debtors		35,890	
Insurance prepaid		900	
Cash		540	
Total current assets		62,530	
LESS CURRENT LIABILITIES			
Creditors	19,500		
Bank overdraft	3,360		
Loan interest due	4,800		
Electricity due	260		
Total current liabilities		(27,920)	
Net assets/working capital			34,610
Total Net asset			136,910
FINANCED BY:			
Capital		70,000	
Add: net profit		29,530	
		99,530	
Less: drawings		(22,620)	
Capital owned			76,910
Add: long term liabilities.			
Bank loan			60,000
			136,910

33.4 Points to remember about the balance sheet.

- A balance sheet is a statement showing the financial position of the business at a given date.
- A balance sheet is also known as a position Statement.
- It consists of the remaining balances for assets, liabilities, capital, drawings and the net profit or loss.
- It shows what a business owns and owes at a particular given date.
- A balance sheet is not part of double entry.

ASSETS

These are resources or things owned by the business.

In the balance sheet, assets are shown under two headings namely:-

NON- CURRENT ASSETS OR FIXED ASSETS

These are resources that:

-Are expected to be used in the business for a long time ie. More than 12 months.

-Were not bought for resale

-Examples include: land and buildings, fixtures and fittings, premises, etc.

CURRENT ASSETS

These are assets that:

- Are likely to change form within 12 months.
- They include goods for resale at a profit.
- Assets in the Balance Sheet are listed starting with the assets that are least likely to turn into cash.
- Prepayments or payments in advance are treated as current assets in the Balance Sheet, ie. Order of permanence.

Balance sheet layout:

There are two methods of laying out assets in the balance sheet; order of permanence and order of liquidity:

(a) Order of permanence: This is when assets are arranged starting with the most difficult item to turn into cash

or the most permanent item (i.e. the item that will be kept the longest), e.g.

Fixed Assets:

Land and building,Fixtures and fittings, Machinery, Motor vehicles

Current Assets:

Stock,Debtors,Bank ,Cash

(b) Order of liquidity: This is where you start with the least permanent item or the easiest items to turn into cash. It is the opposite of the order of permanence, eg.

CURRENT ASSETS:

Cash,Bank,Debtors,Stock

LIABILITIES

These are amounts a Company owes or borrowed from other Organizations or Individuals.

There are two types:

CURRENT LIABILITIES

These are liabilities due for payment in the shortest time, usually within 12 months.

Examples include: Creditors, Bank-overdraft.

Adjustments called Accruals are recorded under current liabilities.

MASTER KEYS PART TWO
GRADE 11 WORK

Adjustments in the Final Accounts

34 Capital expenditure and revenue Expenditure.

1.1 Rationale

Expenditure is the disbursement of funds for acquisition of assets or for services rendered to the business. This topic is designed to help learners appreciate the importance of appropriate classification of business items as a basis of reliability of accounting information. The deductive reasoning approach

is a more suitable method of lesson delivery.

34.1 1.2 objectives

- Define capital and revenue expenditure giving examples
- Show how they are treated in financial statements
- Describe revenue and capital income and their treatment in financial statements.
- Describe why failure to distinguish the above may lead to distortion of financial statements
- explain the effect on the financial statements, and the profits shown there, if revenue
- expenditure is wrongly treated as being capital expenditure, and vice versa.

34.2 1.3 Points to note

34.2.1 Definition

Expenditure is the disbursement of funds from the business for acquisition of assets or for services rendered to the business; or

It is the amount of economic resources given up in obtaining goods and services.

34.2.2 Classification

Expenditure is classified as either capital or revenue expenditure depending on the item for which funds have been disbursed.

- **Capital expenditure**

Capital expenditure is incurred when a business spends money either to *buy fixed assets*, or *add to the* value of an existing fixed asset.

- It is an expenditure to:
  - Get a long-term benefit,
  - Buy fixed assets, or
  - Add to the value of an existing fixed asset

Included in such amounts should be spending on

- *acquiring fixed assets*
- *bringing them into the business*
- *legal costs of buying buildings*
- *carriage inwards on machinery bought*
- *any other cost needed to get a fixed asset ready for use*.

Adding Value

Adding value means spending money on an existing asset in order to improve its performance or increase production capacity. E.g. carrying out renovations on machinery in order to increase production capacity.

- Revenue expenditure
- This is expenditure incurred on the running of the business on a day to day basis as the business is carrying on its trading activities. It is an expenditure for:
    - The acquisition of assets for resale, or For the purpose of earning revenue income

It is also incurred in maintaining the fixed assets.. Examples may include:

- Repairing machinery
- Replacing broken window panes to a building
- Electricity expenses in running machinery
- Petrol costs in running the vehicle
- Purchase of goods for resale

Note

Revenue expenditure is chargeable to the Trading and Profit and Loss Account, while capital expenditure will result in increased figures for fixed assets in the Balance Sheet.

getting the classification wrong affects, the profits reported, the capital account and asset values in the financial statements. It is, therefore, important that this classification is correctly done.

Accounting Treatment

- Capital Expenditure
    - On acquiring assets,

Dr. Asset accounts

Cr. Bank / Cash / Creditors

- At the year end, the balances go to the Balance Sheet
- Revenue Expenditure
- When there are expenses,

Dr. Expenses accounts

Cr. Bank / Cash / Creditors

- At the year end, the balances will be debited to the Profit and Loss Account, or Trading Account.

Expenditure	Benefit	Nature of Expenditure	Accounting Treatment
(a) Buying a house	Long-term benefit ▪ fixed asset acquired	Capital	Dr. Premises Cr. Bank/Cash/ Creditor
(b) Legal cost of buying a house	Long-term benefit ▪ extending beyond current accounting period	Capital	Dr. Premises Cr. Bank/Cash/ Creditor

Expenditure	Benefit	Nature of Expenditure	Accounting Treatment
(d) Renting a house	Short-term benefit ▪ consumed within current accounting period	Revenue	Dr. Rent Cr. Bank/Cash/ Creditor
(e) Management fee	Short-term benefit ▪ consumed within current accounting period	Revenue	Dr. Management fee Cr. Bank/Cash/ Creditor

Expenditure	Benefit	Nature of Expenditure	Accounting Treatment
(e) Installation of partition walls and lighting system in preparing the flat for use as an office	Long-term benefit ▪ to prepare the asset for intended use	Capital	Dr. Premises Cr. Bank/Cash/ Creditor

34.2.3

34.2.4 Capital and revenue income

Income is proceeds coming into the business. Where income is coming from is what would be identified as capital or revenue income.

(a) Capital income

Capital income are proceeds arising from the sale of Fixed assets and long term investments. The profits or losses from the sale of Fixed assets are included in the income statement for the year in which the sale took place.

Example: suppose a machinery is bought for K10,000, and four years later sold for K8,000. The K10,000 would be treated as capital expenditure and K8,000 capital income. The loss K2,000 (10,000 – 8,000) would be shown in income statement.

(b) Revenue income

This is income generated in the normal cause of running the business. Included are:

revenue from ordinary trading (sales)

- interest received
- dividends received
- discount received
- commission received etc.

34.2.5 Treatment of loan interest

If money is borrowed to finance the purchase of a fixed asset, interest will have to be paid on the loan. Loan repayment is capital expenditure while loan interest which is not a cost of acquiring the asset, but is simply a cost of financing its acquisition is revenue expenditure.

PRACTICE questions

a) Explain the difference between capital and revenue expenditure [4marks]

Capital expenditure is incurred on acquisition of new fixed asset or improving the value of an existing fixed asset; while revenue expenditure is incurred on day to day operations of the business which involve mainly current assets.

b) State which of the following are capital and which are revenue expenditure. Give reasons for the classification in each case.

i. Purchase of packing materials from the cartons ltd for the dispatch of goods.

Revenue expenditure; purchase of parking materials is part of the cost of goods sold –Daily operational expense

ii. Payment by cheque for freight costs of goods exported

Revenue expenditure; this forms part of the selling expenses which are daily operating expenses.

iii. Purchase of laser jet printer for use in the office from alpha business equipment.

Capital expenditure – acquisition of new fixed asset

iv. A.Orzel, a partner in the firm, paid for motor vehicle parts for the firm out of her private bank account.

payment by partner is capital expenditure as it represents capital injection into the business where as the expense on motor vehicle parts constitutes revenue expenditure as it does not improve the value the fixed asset[8marks]

Question two.

(a) What is meant by 'capital expenditure', and 'revenue expenditure'?

(b) Some of the following items should be treated as capital and some as revenue. For each of them state which classification applies:

(i) The purchase of machinery for use in the business.

(ii) Carriage paid to bring the machinery in (i) above to the works.

(iii) Complete redecoration of the premises at a cost of £1,500.

(iv) A quarterly account for heating.

(v) The purchase of a soft drinks vending machine for the canteen with a stock of soft drinks.

(vi) Wages paid by a building contractor to his own workmen for the erection of an office in the builder's stockyard.

35 Depreciation of fixed assets.

35.1 Objectives

- Define depreciation and explain why it is provided for
- Identify causes of depreciation
- Calculate and account for depreciation using different methods
- Identify the steps in disposal of fixed asset

35.2 Points to note:

Fixed assets are those assets of material value which are:

- of long life, and
- to be used in the business, and
- not bought with the main purpose of resale.

35.3 Definition

Depreciation is that part of the original cost of a fixed asset that is consumed during its period of use by the business.

- It needs to be charged to profit and loss every year.
- The amount charged in a year to profit and loss for depreciation is based upon an estimate of how much of the overall economic usefulness of a fixed asset has been used up in that accounting period.
- It is an expense for services consumed in the same way as expenses are incurred for items such as wages, rent or electricity.
- Because it is charged as an expense to the profit and loss account, depreciation reduces net profit.

35.4 Causes of depreciation

Physical deterioration, economic factors, time,

35.4.1 Physical deterioration

- Wear and tear.
- Erosion, rust, rot and decay.

35.4.2 Economic factors

Obsolescence. This is the process of becoming out-of-date. For instance, over the years there has been great progress in the development of synthesizers and electronic devices used by leading commercial musicians.

The old equipment will therefore have become obsolete, and much of it will have been taken out of use by such musicians.

Inadequacy. This arises when an asset is no longer used because of the growth and changes in the size of the business.

35.5 Methods of calculating depreciation charges.

The two main methods in use are the straight line method and the reducing balance method.

35.5.1 Straight Line Method

Under this method ,Depreciation is calculated by dividing the depreciable amount of the asset by the expected number of accounting periods of its useful life.

$$\text{Annual depreciation} = \frac{\text{Cost of an asset – residual value}}{\text{Expected useful life of the asset}}$$

$$\frac{\text{Cost (£22,000) - Estimated disposal/residual value (£2,000)}}{\text{Number of expected years of use (4)}}$$

Example

A vehicle cost K500 000 will be in use in the business for 4 years after which it will have residual value of K20 000. Annual depreciation over 4 years will be:

$$\frac{\text{(K500 000 – K20 000)}}{4} = \frac{\text{K480 000}}{4}$$

$$= \underline{\text{K120 000}} \text{ P.A.}$$

35.5.2 The Reducing Balance Method

In this method depreciation is calculated as a fixed percentage of the net book value of the asset, as at the end of previous accounting period.

This method assumes that the business will benefit more from the use of the asset in earlier years than later years.

Example: Reducing Balance Method

Machine was bought at a cost of K150 000. Depreciation is to be charged at the rate of 20% per annum. Calculate depreciation for the first 3 years.

Year 1	20% x 150 000		
		(30 000)	Depreciation
Year 2	20% x 120 000 N.B.V		
		(24 000)	Depreciation
Year 3	20% x 96 000 N.B.V		
		(19 200)	Depreciation
		76 800	

35.6 Depreciation provisions and assets bought or sold

35.6.1 Double entry records for depreciation

The method now used involves maintaining each fixed asset at its cost in the ledger account while

operating another ledger account where the depreciation to date is recorded. This account is known as the 'accumulated provision for depreciation account.

The depreciation is posted directly into the cumulative provision for depreciation account.

The double entry is:

- **Debit** the profit and loss account
- **Credit** the accumulated provision for depreciation account

Example.

Brian Blackpool, a trader with a year-end of 31 December, had the following transactions in his accounts:

He purchased a motor vehicle for £25,000 on 1 January 2004.

Brian purchased a second motor vehicle on 1 January 2005 for £30,000.

He calculates depreciation using the reducing balance method at 20% per annum.

Required:

a) The motor vehicle account.
b) The provision for depreciation account.
c) The profit and loss account extracts and balance sheet extracts for the years 2004, 2005 and 2006.

Solution.

Computation of annual depreciation

MV 1	MV 2	TOTAL
25,000x 20% = 5,000	-	5,000
20,000x 20% = 4,000	30,000 x 20% = 6,000	10,000
16,000 x 20% = 3,200	24,000 x 20% = 4,800	8,000

a) Motor vehicles accounts

Dates	Details	Folio	Debit	Credit
01/01/2004	bank		25,000	
31/12/2004	Balance	c/d		25,000
			25,000	**25,000**
01/01/2005	Balance	b/d	25,000	
	bank		30,000	
31/01/2005	Balance	c/d		55,000
			55,000	**55,000**
01/01/2006	Balance	b/d	55,000	
	Balance	c/d		55,000
			55,000	**55,000**
	Balance	b/d	55,000	

Provision for depreciation

Dates	Details	Folio	Debit	Credit
31/12/04	Profit/loss acct			5,000
	balance	c/d	5,000	
			5,000	**5,000**
01/01/05	balance	b/d		5,000
31/12/05	Profit/loss account			10,000
	balance	c/d	15,000	
			15,000	**15,000**
01/01/06	Balance	b/d		15,000
31/12/06	Profit and loss			8,000
31/12/06	Balance	c/d	23,000	
			23,000	**23,000**
01/01/07				23,000

Profit and loss account (extract)

Less expenses

31/12/04	Provision for depreciation	5,000
31/12/05	Provision for depreciation	10,000
31/12/06	Provision for depreciation	8,000

Balance sheet (extract)

		Cost	Dep'n to date	NBV
31/12/04	Motor vehicle	25,000	5,000	20,000
31/12/05	Motor vehicles	55,000	15,000	40,000
31/12/06	Motor vehicles	55,000	23,000	32,000

PRACTICE QUESTION TWO

B. Fungai bought four (4) machines on credit from Kayumba equipment limited on 1 January 2010 for k20,000 each. She charged 20% depreciation per year by reducing balance method. The policy is to charge full year's depreciation in the year of purchase but not charge any depreciation in the year of sale. Two of the machines were sold for k13,000 each by cash on 1 October 2012. On the same date two replacement machines costing k24,000 each were bought for cash. Fungi's financial year ends on December 31st,2012.

Required:

Prepare the provision for depreciation account for the years 2010,2011 and 2012.[7]

Solution

DATES	details	folio	Dr.	Cr.
2010	Profit and loss account			16,000
Dec.31.	Balance	c/d	16,000	
			16,000	16,000
2011				
Jan. 1	Balance	b/d		16,000
Dec.31	Profit and loss account			12,800
Dec.31	Balance	c/d	28,800	
			28,800	28,800
2012				
Jan.1	Balance	b/d		28,800
Oct.1	Machinery disposal		14,400	
Dec.31	Profit and loss account			14,720
Dec.31	balance	c/d	29,120	
			43,520	43,520
2013				
Jan. 1	Balance	b/d		29,120

Calculations for depreciation

2010 4 x 20,000 = 80,000 x 20% = 16,000

2011 80,000 – 16,000 = 64,000 X 20% = 12,800

2012 2 new machinery 24,000 x 2 = 48,000 x 20% = 9,600

2 old machinery 12,800 x 2 = 25,6000 x 20% = 5,120

Total provision for depreciation to profit and loss account. 14,720.

35.7 The disposal of an asset

When a fixed asset is sold or disposed, it is necessary to bring together:

- The original cost of the asset.
- Depreciation provided over the life of the asset.
- Sale proceeds.

This can be achieved using the following accounts:

- Fixed asset account
- Provision for depreciation account
- Disposals account

On 1 January 2007, Brian Blackpool sold the motor vehicle he purchased on 1 January 2004 for £11,000.

Required

Show the accounting entries for the disposal of the asset, together with the extracts for the profit and loss account and balance sheet extracts for the year ending 31 December 2007.

If we start with the balance b/d in the previous double entry accounts for:

- motor vehicles
- provision for depreciation

we can now show the accounting entries for the disposal of the asset.

Motor vehicle account

Date	Details	Folio	Dr.	Cr.
	Balance	b/d	55,000	

Provision for depreciation account

Date	Details	Folio	Dr.	Cr.
	Balance	b/d		23,000

Double entry transactions for disposal of an asset

1) Transfer the cost price of the asset sold to the disposal account
   - Debit disposals account
   - Credit fixed asset account
2) Transfer the depreciation already charged to the disposal account
   - Debit provisions for depreciation account
   - Credit disposals account
3) For sale proceeds
   - Debit cash book
   - Credit disposals account
4) Transfer balance on disposals account to the profit and loss account

If the difference is on the debit side of the disposal account, it is a profit on sale

- Credit profit and loss account
- Debit disposals account

If the difference is on the credit side of the disposal account, it is a loss on sale

- Debit profit and loss account
- Credit disposals account

<u>Profit and loss account (extract</u>

<u>Less expenses</u>

Loss on disposal 1,800

Problems involved in accounting for depreciation.

- Selection of appropriate method
- Estimating the useful life of the asset
- Determination of the cost of a fixed asset (correctly dealing with delivery installation and legal fees etc.)

Concepts

Accruals – matching what has been used of an asset to that period of time.

Prudence – not overstating the profit in the profit and loss account or the value of assets in the balance sheet.

Consistency – Using the same method and percentage year on year.

Summary of accounting treatment for disposal of fixed assets.

Dr. Disposal Cr. Fixed Asset	Cost price of the asset sold
Dr. Provision for Depreciation Cr. Disposal	Depreciation already charged on the assets concerned
Dr. Cash / Vendee Cr. Disposal	Proceeds received / receivable on the disposal
In case of loss on the disposal (Debit side greater than credit side)	
Dr. Profit and Loss Cr. Disposal	With any loss on the disposal
In case of profit on the disposal (Credit side greater than debit side)	
Dr. Disposal Cr. Profit and Loss	With any profit on the disposal

More Practice Questions

A company purchased machine for $2,500 each on 1 Jan. Year 1.

It is the company's policy to provide for depreciation on its machinery at a rate of 20%, with a full year's depreciation made in the year in which a machine is purchased, but none in the year of sale. One machine was traded in and a new machine for $4,000 was purchased on 1 Feb. Year 2. The trade-in value of the old machine was $1,000.

Machinery

Year 1		$	Year 1		$
Jan 1	Bank	2,500	Dec 31	Bal. c/d	2,500

Provision for dep.-Machinery

Year 1		$	Year 1		$
Dec 31	Bal. c/d	500	Dec 31	P/L (2500*20%)	500

Machinery

Year 2		$	Year 2		$
Jan 1	Bal. b/d	2,500	Feb 1	Disposal	2,500
Feb1	Disposal: trade-in-allowance	1,000	Dec 31	Bal. c/d	4,000
Feb1	Bank	3,000			
		6,500			6,500

Provision for dep.-Machinery

Year 1		$	Year 1		$
Dec 31	Bal. c/d	500	Dec 31	P/L	500
Year 2			Year 2		
Feb 1	Disposal	500	Jan 1	Bal b/d	500

Disposal

Year 2		$	Year 2		$
Feb 1	Machinery	2,500	Feb1	Dep.	500
			Feb 1	Machinery: trade-in-allowance	1,000
		2,500			2,500

Practice Question.

Mulenga maintained his motor vehicle account at cost price and a provision for depreciation of motor vehicle account.

On January 2014, the motor vehicle account had a cost value of k120,000 while the provision for depreciation account had a balance of k24,000.

His policy was to depreciate the motor vehicle at 20% of cost per annum, charge full years' depreciation in the year of purchase and no charge of depreciation in the year of disposal.

On 31 march 2015 Mulenga acquired another vehicle from TATA motors ltd at K40,000. ON 30 September 2016, Mulenga sold one vehicle which had cost him K35,000 in 2014, at K19,000, to zionele traders on credit.

Required;
Open the provision for depreciation of motor vehicles account for three years -2014 -2016.

Solution.

Provision for Depreciation of Motor Vehicle Account

Date	***Details***	***folio***	***Dr***	***Cr***
2014				
January 1	Balance			24,000
December. 31	Profit and loss account			24,000
December. 31	balance		48,000	
			48,000	48,000
2015				
January 1	Balance			48,000
December. 31	Profit and loss account			32,000
December. 31	balance		80,000	
			80,000	80,000
2016				
January 1	Balance	b/f		80,000
September 31	Disposal account		14,000	
December. 31	Profit and loss account			25,000
December. 31	Balance		91,000	
			105,000	105,000
Jan 2017	balance			91,000

36 Bad debts, provisions for doubtful Debts

36.1 Objectives

- explain and show how bad debts are written off
- explain why provisions for doubtful debts are made
- make the necessary entries to record a provision for doubtful debts in the books
- calculate and make provisions for discounts on debtors

36.2 Definition

36.2.1 Bad debts

- When a business sells to a customer on credit it takes a business risk that the customer might not pay the amount owed.
- What the customer fails to pay is what is known as a bad debt.
- A business might have to write off the debt as a bad debt.
- Bad debts are an expense and will reduce the profit of the business.
- A business may decide that the debtor cannot pay or the cost of chasing the debt is not cost effective. The debt will then be written out of the ledger.

36.2.2 Accounting entries

Debit - bad debts account

Credit - personal account of the debtor

John Green

Bal b\d	6,000	Bad debts	6,000

Bad debts account

Dr.		Cr.	
John Green	6,000	Profit and loss a\c	6,000

BAD DEBTS RECOVERED

A debt previously written off may be recovered in full or partially.
Steps in recovery:

(a) The debt must first be reinstated to facilitate the recording of cash coming in.

DR. – the receivable (Debtor) account
CR. – Bad debts recovered account.

(b) When payment is received:

DR. – Cash or Bank account
CR. – Receivables (Debtors) account } with amount received

36.2.3 Provisions for doubtful debts

When creating a provision, the concept of **prudence** is applied. The profit of the business will not be **overstated**. Debtors will be shown at a **true and fair value** in the balance sheet.

When drawing up the financial statements, the following are the objectives:

- to charge as an expense in the profit and loss account for that year an amount representing debts that will never be paid;
- to show in the balance sheet a debtors figure as close as possible to the true value of debtors at the balance sheet date.

The accounting entries needed for the provision for doubtful debts are:

Year in which provision is first made:

- Debit the profit and loss account with the amount of the provision (i.e. deduct it from gross profit as an expense).
- Credit the Provision for Doubtful Debts Account.With the **full amount** of the provision

Total debtors £500,000 ,5% provision

Provision for doubtful debts account

Bal c\d	25,000	Profit and loss	25,000
	25,000		25,000
		Bal b\d	25,000

Debtors must be shown in the balance sheet at the net figure.

Balance sheet extract

Current assets

Debtors		500,000
Less provision for doubtful debts	25,000	475,000

The **prudence concept** has been applied and the debtors' figure is not overstated.

The accounting entries to increase the provision

The accountant may decide that the provision is not enough and must be increased:

Debit - profit and loss account

Credit - provision for doubtful debts account

only with the **amount of the increase**

If the total debtors have increased to £800,000 and the business maintains a 5% provision on debtors:

Provision for doubtful debts account

Bal c\d	40,000	Bal b/d	25,000
		Profit and Loss	15,000
	40,000		40,000
		Bal b/d	40,000

Current assets	
Debtors	800,000
Less Provision for doubtful debts	40,000
	760,000

36.2.4 points to note:

- That debts the business is unable to collect are called bad debts.
- That bad debts are credited to the customer's account (to cancel them) and debited to a bad debts account.
- That provisions for doubtful debts are needed, otherwise the value of the debtors on the balance sheet will be showing too high a value, and could mislead anyone looking at the balance sheet. Also, this allows for more accurate calculation of profits or losses.
- That the provision for doubtful debts is calculated after bad debts have been deducted from the debtor balances.
- That the amount of the provision for doubtful debts is based on the best estimate that can be made taking all the facts into account.
- That an increase in the provision for doubtful debts will create a debit entry in the profit and loss account.
- That a reduction in the provision for doubtful debts will create a credit entry in the profit and loss account.
- That the provision for doubtful debts is shown as a deduction from the debtors in the balance

sheet.

- That provisions for cash discount are made in the same way as provisions for doubtful debts.

Practice question

On 1 January 2008. There was a balance of k500 in allowance for doubtful debts accounts, and it was decided to maintain the provision at 5% of the debtors each year end.

The debtors on 31 December each year were:

2008 K 12000

2009 K8000

2010 K 9000

REQUIRED:

Show the necessary entries for the three years ended 31 December 2008 to 31 December 210 inclusive of the allowance for doubtful allowance for doubtful account. [8]

Solution

Date.	Details	folio	Dr	Dr
2008				
Jan.	Balance	b/f		500
Dec	Profit and loss			100
Dec	balance		600	
			600	600
2009				
Jan.	Balance	b/f		600
Dec	Profit and loss		200	
Dec	balance		400	
			600	600
2010				
Jan.	Balance			400
Dec	Profit and loss			50
Dec	balance		450	
			450	450
	Balance	b/d		450

36.3 Prepayments and accruals

36.4 Objectives.

- To prepare expense account and interpret balance brought down as an accrual or prepayment.
- To adjust expenses for accruals and prepayments in income statement
- To prepare income account with adjustment for amounts owing and prepaid
- To show accruals and prepayments appropriately in balance sheet.

36.5 ACCRUALS

The accruals concept states that income and expenses should be included in the income statement of the period in which they are earned or incurred and not paid or received.

A business rents a shop for K1,200 per annum (K100 per month). If at year end, the business has only paid K1000, a full year's charge of K1,200 will be expensed in income statement. The K200 though not paid will be included because it relates to the same period.

Accruals or accrued expenses are expenses which are charged against the profits of a particular period, even though they have not been paid, because they were incurred in that period.

N.B. Accruals can be owing by the business or to the business.

Example 1

Dates	Details.	folio	Dr.	Cr.
	Bank		1000	
	Profit and loss account			1200
	Balance c/d		200	
			1200	1200
	Balance b/d			200

the rent expense account with balance brought down on credit is a liability (amount owing).

But the amount to charge in income statement will be K1200 including K200 not paid because it relates to the same period.

In balance the sheet K200, will be shown under current liabilities as accrued expenses.

Example 2: Owing by the business

Genuine Motor Spares, is a dealer in motor spares. The financial year for the business ends on 28 February each year. His telephone was installed on 1 April 20x6 and receives his telephone account quarterly at the end of each quarter. He pays it promptly as soon as it is received. On the basis of the following data, calculate the telephone expense to be charged to the income statement for the year ended 28 February 20x7.

The following payments were made.

Dates.	K
30.6.20x6	23.50
30.9.20x6	27.20
31.12.20x6	33.40
31.3.20x7	36.00

solution

Telephone account

Dates	Details.	folio	Dr.	Cr.
30.6.2006	bank		2,350	
30.9.2006	bank		2,720	
31.12.2006	bank		3,340	
	Profit and loss			10,810
	Balance	c/d	2,400	
			10,810	10,810
	Balance	b/d		2,400

36.5.1 Amounts accrued to the business

While the business may owe others for expenses, the business may also be owed for other amounts apart from trade among others:

- Rent receivables
- Commission receivable
- Unsettled claims for insurance etc.

Using the matching or accruals concepts, all income whether received or not as long as it relates to the accounting period under review, should be included as income in income statement for that period. Since amounts are not yet received, they should be shown in balance sheet under current assets as other receivables.

Example 1.

T.K. Furnishers Ltd sublets part of the buildings at an annual rent of K1200 000 (K100 000 per month). During the year ended 31 December 20X8, T.K. discovers that the tenant had only paid K1 000 000. Show rent receivable account and statement to be shown in income statement and interpret the balance brought down.

Solution:

Rent receivable account

Date	Details	folio	Dr	Cr
Dec.31	bank			1000,000
	Income statement		1,200,000	
	Balance	c/d		200,000
			1,200,000	1,200,000
	Balance	b/d	200,000	

A business maintains one account for rent and rates.
During the year ended 31 December 20X5, the following information was made available for rent and rates.
At 1 January 20X5, there was K250 000 rates which had been paid in advance in 20X4, and K500 000 rent was owing on the same date.
The following payments were made during 20X5, rent K4 000 000 and rates K3 6000 000.
On 31 December 20X5, rent of K200 000 is owing and rates of K150 000 are paid in advance.
Required:
Prepare the rent and rates account (combined and appropriately bring down the balance).

Rent and rates account

	Details	folio	Dr	Cr
	Balances	b/f	250,000	500,000
	Bank (rent)		4,000,000	
	Bank (rates)		3,600,000	
	Balances	c/d	200,000	150,000
	Profit and loss			7,400,000
			8,050,000	8,050,000
	Balances	b/d	150,000	200,000

Note:
In balance sheet: Rent is current liability (K200 000) Rates is current asset (150 000).

The trial balance and limitation.

37 Objectives

- Identify different types of errors and how to correct them
- Distinguish between errors affecting trial balance and those not
- Adjust profit figure after correcting errors
- Show correctly suspense account in balance sheet before errors are corrected
- correct all errors which do not affect trial balance totals being equal

38 Definition

A trial balance is a list of debit and credit balances taken from the ledger.

the trial balance is constructed on the principle of double entry which states that:

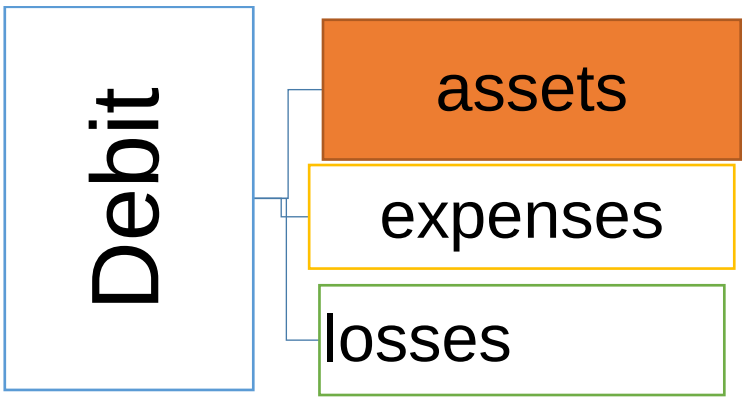
- every debit entry needs a corresponding credit entry
- every credit entry needs a corresponding debit entry

When this principle is correctly applied, the debit and credit totals of the trial balance are equal.

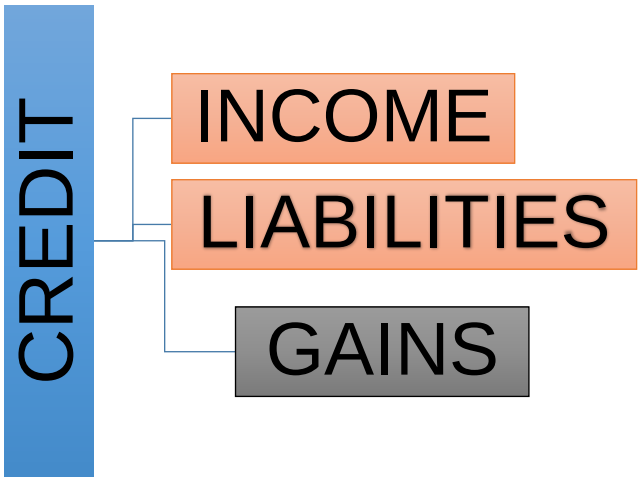
38.1 Summary of ledger account classes and nature of balances:

The acronyms
- DR. EA L
- CR.ILG

DR.EAL



CR.ILG



trial balance blue print

Account titles	CLASSIFICATION	Nature of balance
Land and buildings	Asset	Dr
Premises	Asset	Dr
Equipment	Asset	Dr
Fixtures and fittings	Asset	Dr
Capital	liability	Cr
Drawings	loss	Dr
Bank loan	liability	Cr
Bank overdraft	liability	Cr
Debtors	Asset	Dr
Stock	Asset	Dr
Cash at bank	asset	Dr
Discount received	Gain	Cr
Provision for bad debts	gain	Cr
Rent	Expense	Dr
Salaries	Expense	Dr
Purchases	Expense	Dr
Carriage in	Expense	Dr
Returns in	Loss	Dr
Total		

Practice question two

Thomas Smith, a retail trader, has very limited accounting knowledge. In the absence of his accounting technician, he extracted the following trial balance as at 31 March 20X8 from his business's accounting records:

	£	£
Stock in trade at	1 April 20X7	10,700

Stock in trade at 31 March 20X8	7,800	
Discounts allowed		310
Discounts received	450	
Provision for doubtful debts		960
Purchases	94,000	
Purchases returns		1,400
Sales	132,100	
Sales returns	1,100	
Freehold property: at cost		70,000
Provision for depreciation	3,500	
Motor vehicles: at cost	15,000	
Provision for depreciation	4,500	
Capital – Thomas Smith	84,600	
Balance at bank		7,100
Trade debtors	11,300	
Trade creditors	7,600	
Establishment and administrative expenditure		16,600
Drawings		9,000
	£239,010	£239,010

Required:

(a) Prepare a corrected trial balance as at 31 March 20X8.

After the preparation of the above trial balance, but before the completion of the final accounts for the year ended 31 March 20X8,

39 Trial balance construction.

The following information is extracted from the books of B Stepson, a sole trader, whose financial year ends on 31 October 2015.

	K
Capital 1 January 20X5	204,235
Opening inventory	46,000
Purchases	234,000
Sales	288,000
Light & heat	2,000
Advertising	3,000
Insurance	5,000
Bad debts	150
Rent	13,000
General	13,850
Drawings	8,000
Receivables	48,000
Payables	35,000
Bank overdraft	50,000
Returns inwards	1,000
Returns outwards	350
Carriage inwards	780
Carriage outwards	475
Machinery	132,000
Discounts allowed	880
Discount received	550

Required:
Construct Stephen's trial balance as at 31 October 2015

solution

B. Stephson
Corrected Trial balance as at 31 December,2015

	Dr.	Cr.
	K	K
Capital 1 January 20X5		204,235
Opening inventory	46,000	
Purchases	234,000	
Sales		288,000
Light & heat	2,000	
Advertising	3,000	
Insurance	5,000	
Bad debts	150	
Rent	13,000	
General	13,850	
Drawings	8,000	
Receivables	48,000	
Payables	35,000	
Bank overdraft		50,000
Returns inwards	1,000	
Returns outwards		350
Carriage inwards	780	
Carriage outwards	475	
Machinery	132,000	
Discounts allowed	880	
Discount received		550
	543,135	543,135

40 errors not disclosed by the trial balance.

1. *Errors of omission* – where a transaction is completely omitted from the books. If we sold £90 goods to J Brewer, but did not enter it in either the sales or Brewer's personal account, the trial balance would still 'balance'.
2. *Errors of commi*ssion – this type of error occurs when the correct amount is entered but in the wrong person's account, e.g. where a sale of £11 to C Green is entered in the account of K Green. It will be noted that the correct class of account was used, both the accounts concerned being personal accounts.
3. *Errors of principle* – where an item is entered in the wrong class of account, e.g. if purchase of a fixed asset, such as a van, is debited to an expenses account, such as motor expenses account.

4. Compensating errors – where errors cancel each other out. If the sales account was added up to be £10 too much and the purchases account was also added up to be £10 too much, then these two errors would cancel out in the trial balance. This is because the totals of both the debit side and the credit side of the trial balance will be £10 too much.
5. *Errors of original entry* – where the original figure is incorrect, yet double entry is still observed using this incorrect figure. An instance of this could be where there were sales of £150 goods but an error is made in calculating the sales invoice. If it were calculated as £130, and £130 were credited as sales and £130 were debited to the personal account of the customer, the trial balance would still balance.
6. *Complete reversal of entries* – where the correct accounts are used but each item is shown on the wrong side of the account. Suppose we had paid a cheque to D Williams for £200, the double entry of which is Cr Bank £200, Dr D Williams £200. In error it is entered as Cr D Williams £200, Dr Bank £200. The trial balance totals will still agree.
7. *Transposition errors* – where the wrong sequence of the individual characters within a number was entered. For example, £142 entered instead of £124. This is quite a common error and is very difficult to spot when the error has occurred in both the debit and the credit entries, as the trial balance would still balance. (It is more common for this error to occur on one side of the double entry only.)

41 Correction of errors – suspense account

41.1.1 Rationale

The suspense account is taught and examined for two main reasons:

- To test the candidates' knowledge and understanding of how suspense accounts can be used to correct errors found in the trial balance
- To test the students' appreciation of the reason why a trial balance is extracted for the compilation of the final accounts of a business.

This topic calls for hands-on activity, thus the demonstration coupled with practice method is recommended method of lesson delivery.

41.1.2 Objectives

- Explain why a suspense account may be used
- Create a suspense account in order to balance the trial balance
- Correct errors using a suspense account
- Recalculate profits after errors have been corrected
- Explain why using a suspense account is generally inappropriate

When totals in trial balance are not equal, a temporal account called the suspense account is opened.

41.1.3 Suspense account

The suspense account is opened for the difference in the trial balance when the cause for the difference is not clear. However, it is not encouraged to all the time open suspense account when trial balance totals disagree, except under certain circumstances e.g. where it is suspected that the difference may be as a result of many errors which might take some time to discover.

Also where the bookkeeper does not know where to post one side of a transaction e.g. a cash payment is credited to cash, but the bookkeeper does not know what the payment was for and so will not know which account to debit.

Exhibit 33.1

Trial Balance as at 31 December 2011

	Dr	*Cr*
	£	£
Totals after all the accounts have been listed	100,000	99,960
Suspense		40
	100,000	100,000

41.2 Steps in correcting errors

1. Identify the accounts affected
2. Identify the account class of the affected accounts
3. Identify the nature of balance the account ends with.
4. Perform the journal correcting entry to rectify the error.
5. The following table may be of help in carrying out this process.

Error types	Action on accounts ending with Dr.balances asset, expenses/loss	Action on accounts with Cr.balances(income, liabilities and gains)
a) overcast	Cr.the account to remove the excess	Dr.the account to remove the excess
b) Under cast	Dr the account to increase the balance	Cr.the account to increase the balance.
c) Omissions from entry	Dr the account with the amount omitted	Credit the account with the amounts omitted
d) Transpositions resulting in understatement	Dr the account affected with the difference	Cr the account affected with the difference

e) **Transpositions resulting in overstatement**	Cr the account affected with the difference	Dr the account affected with the difference

practice questions to do

December each year. At 31 December 20X5 a trial balance was extracted which revealed a deficit of K1421 on the debit side. This was resolved by opening a suspense account, and financial statements where prepared and showed a profit of K12,600.

In January 20X6 investigation revealed that:

(i) A page of sales day book totaling K576 had not been posted to sales account.

(ii) An accrual of rates K371 had not been taken into account

(iii) A repayment part of the loan from the bank K300 had been entered on the loan interest account

(iv) The petty cash balance had been included as K57 instead of K75.

(v) A bad debt of K120 had been entered in the customer's account but not in the expense account.

(vi) Drawings K200 had been entered in the sundry expenses account

(vii) An invoice for car repairs K380 had been entered in the wages account.

(viii) The rent received account balance of K600 had been entered on the wrong side of the trial balance and income statement.

(ix) Advertising account with a balance of K2,759 had been omitted altogether.

(x) Closing inventory had omitted some items valued at cost K2,000.

(xi) Discount allowed of K150 had been credited to discounts received.

Required:

(a) Show by means of journal to correct the above errors (narratives are not required).

(b) Clear suspense account balance after the correction of errors and

(c) Prepare a statement showing the corrected amount of the profit.

Solution:

(a) The Journal entries

		Dr	Cr
(i)	Suspense account	576	
	Sales account		576
	Profit and loss account		371
(ii)	Rates account	371	
(iii)	Bank loan account	300	

	Interest account		300
(iv)	Petty cash account	18	
	Suspense account		18
(v)	Bad debts account	120	
	Suspense account		120

(vi)	Drawings account	200	
	Sundry expenses account		200
(vii)	Car repairs account	380	
	Wages account		380
(viii)	Suspense account (rent)	1,200	
	Rent		1,200
	Advertising	2759	
(ix)	Suspense account (advertising)		2,759
(x)	Closing Inventory/stock account	2,000	
	Income Statement		2,000
(xi)	Discount allowed account	150	
	Discount received account	150	
	Suspense account		300

42 Practice

Account title	Dr	Cr
Capital		45,000
Debtors and creditors	32,900	5,000
Returns in and out	2,500	2,710
Purchases and sales	25,000	30,485
Discounts	6,800	5,630
Drawings	8,220	
Wages and salaries	7,000	
Equipment	8,000	
Total	90,420	88,825

The following errors were discovered by Sandy, the internal auditor, on 31 December 2014:

i) The Purchases account had been under cast by £4,500.

ii) Cash sales of £24,205 had not been entered into the Sales account.

iii) A credit note of £3,450 was entered in P White's customer account but no entry was made in the relevant returns account.

iv) The Sales account was overcast by £3,900.

v) £4,590 of goods was taken out of the business for I Johnson's personal use. This was recorded in the Drawings account but there were no other entries.

vi) An invoice for J Sullivan was discovered behind the computer. No accounting entries had

been made for the £1,650.

vii) £2,700 in respect of debtor J Smith was debited in error to the account of J Smyth Ltd.

viii) A discount allowed of £4,275 was credited in error to the Discount Received account.

ix) A bad debt of £6,800 had been entered into the customer's account only.

TASK

a) What is the purpose of a trial balance? (2 marks)

b) Correct the above errors and prepare the resulting suspense account. (18 marks)

Note: journal entries are not required.

Control accounts

42.1 Objectives

- explain that control accounts are an independent check on the sales and purchases ledgers
- explain that control accounts may be used to provide totals of debtors and creditors, locate errors and act as a deterrent against fraud
- identify and use the books of prime entry as sources of information for the control account entries
- enter the following items into the relevant control account: credit sales and purchases, receipts and payments, discounts, returns, bad debts, dishonoured cheques, interest on overdue accounts, contra
- entries, refunds, opening and closing balances (debit and credit within each account)

Definitions and Explanations.

Control accounts are so called because they control a section of the ledger which they represent.

By control it means that the balance on a control account should equal the total of balances of the ledger it is controlling.

Thus a sales ledger control account controls the sales ledger

A purchases ledger controls the purchases ledger

42.2 Purpose of control accounts

The control accounts help us to locate errors.

The control accounts provide a summary. The total balances of the debtors and creditors can be derived quickly and easily.

- If there is a difference on a trial balance, the control account will show whether or not any of the difference is in the sales or purchases ledger accounts.

- If the control accounts agree with the balances on the sales and purchases ledgers, then the difference must lie in the nominal general ledger.

42.3 Sources of information for control accounts–Sales ledger control account

- Opening receivables or debtors balance – List of receivables balances drawn up at end of previous period
- Credit sales got from sales day book
- Returns inwards obtained from returns inwards book
- Cheques/cash received. Total of receipts from cashbook
- Discounts on receivables. This is the total of discounts from discounts allowed column in the cashbook
- Closing receivables. This a total of receivables balances drawn at the end of the period.

43 Format for sales/debtors ledger control accounts

DR.	Cr
DEC 1. Balances b/f	Balance b/f
31. sales	Returns inwards
31. bank	Cash/bank
31. bills receivable	Bills receivable
31. interest received	Set – offs/transfers
31. bad debts recovered	Refunds and rebates
31 .balance c/f	Discount allowed
	Bad debts
	Balance c/f

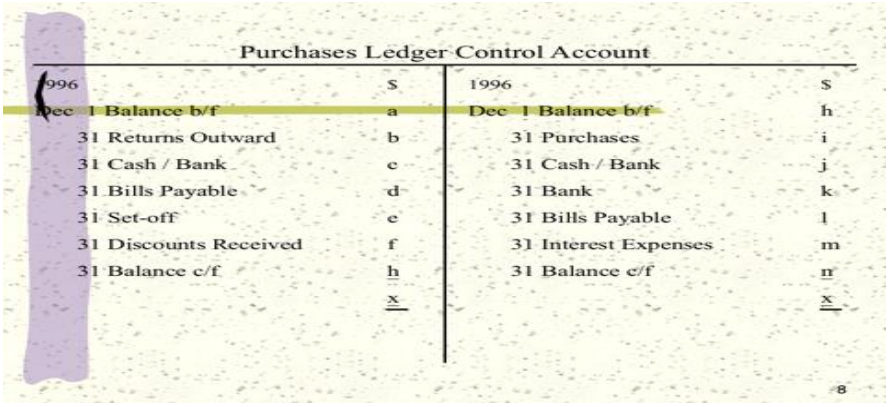
43.1 Sources of information: Sales ledger control accounts

- Opening receivables or debtors balance – List of receivables balances drawn up at end of previous period
- Credit sales got from sales day book
- Returns inwards obtained from returns inwards book
- Cheques/cash received. Total of receipts from cashbook
- Discounts on receivables. This is the total of discounts from discounts allowed column in the cashbook
- Closing receivables. This a total of receivables balances drawn at the end of the period.

44 Sources of information: purchases ledger control account

- Opening creditors – List of creditors' balances drawn up at the end of the previous period.
- Credit purchases – Total from purchases journal
- Purchases returns – Total from purchases returns journal

- Cheques/cash paid to creditors – Cash book
- Discounts received – Cash book
- Closing creditors – List of creditors' balances drawn up at the end of the period



Purchases Ledger Control Account

1996		$	1996		$
Dec 1	Balance b/f	a	Dec 1	Balance b/f	h
31	Returns Outward	b	31	Purchases	i
31	Cash / Bank	c	31	Cash / Bank	j
31	Bills Payable	d	31	Bank	k
31	Set-off	e	31	Bills Payable	l
31	Discounts Received	f	31	Interest Expenses	m
31	Balance c/f	h	31	Balance c/f	n
		x			x

Format for Purchases ledger control account

44.1 Set offs/transfers/contras

These arise from contra entry transactions. This is where a firm is both a customer and supplier to the same person. Eg X Ltd sold goods to Engine Zimba, K20,000. Engine also supplied the firm with goods worth K28,000. The K20,000 owed by Zimba to X Ltd will set off against the K28,000 owed to him. This makes the two transactions cancel out, with the net effect of K8,000 remaining as the amount owing to Zimba.

Contra items(set-off) are shown on the credit side of the sales ledger control account and will appear on the debit side of the purchases ledger control account

Practical examination question

The following information was extracted from the books of Lewell Ltd. On 1 March 1996:

Purchases ledger control account	28,500
Sales ledger control account	67,300
During the month:	
Cash sales	12,000
Credit sales	20,000
Cash purchases	8,800
Credit purchases	14,000
Discounts received from suppliers	5,400
Discounts allowed to customers	4,200
Returns Inwards	900
Cash received from customers	25,000

Cash payment to suppliers	30,000
Returns Outwards	700
Bad debts written off	100
Bills receivable from customers	11,000
Dishonored Cheques returned to customers	500
Balances in sales ledger set off against credit Balances in purchases ledger	2,600

Solution

Sales/Debtors Ledger Control Account

Details		**Dr**	**Cr**
Balance	b/f	67,300	
Sales		20,000	
Bank		500	
Discount allowed			4,200
Returns in wards			900
Bad debts			100
Cash			25,000
Bills receivable			11,000
Set-off			2,600
Balance	c/d		44,000
		87,800	87,800
		44,000	

Purchases/creditors ledger control account

Details

Balance	b/f		28,500
Purchases			14,000
Discount received		5,400	
Returns out wards		700	

Set-off		2,600	
Cash		30,000	
Balance	c/f	3,800	
		42,500	42,500
Balance	c/d		3.800

Practice question 2

KAMWI had the following balances on his trade receivables and trade payables on 1 December 2006. Customers owed K40 250 and he owed suppliers 26 423. Credit balances in the trade receivables ledger amounted to K3 845 and debit balances in the trade payables ledger amounted to K1 985.

During the month his daybooks showed the following totals:

Purchases	408 563
Sales	854 239
Returns inwards	44 271
Returns outwards	32 662
Payments to suppliers	300 912
Receipts from customers	675 843
Discounts received	9 027
Discounts allowed	20 275
Amounts written off to bad debts	13 173
Transfers between the receivables ledger and the payables Ledgers	7 457
Rebates on customer invoices	3 244
Refunds of cash from suppliers	5 877

On 31 December 2006 amounts owed to customers were K2 119. Suppliers who owed him amounts at start of the year had paid K1 525.

REQUIRED

Prepare a trade receivables/debtors/sales ledger control account and a trade payables control account, showing the balances to carry forward to the following month.

KAMWI'S TRADE DEBTORS' LEDGER
CONTROL ACCOUNT

Details	folio	Dr.	Cr.
Balances	b/d	40 250	3845
Sales		854,239	
Returns in wards			44,271
Bank			675,843
Discounts all.			20,275
Bad debts written off			13,173

Trade creditors transferred			7,457
Rebates on customer invoices			3,244
balances	b/f	2,119	128,400
		896,508	896508
Balances	b/d	128,400	2,119

KAMWI'S TRADE CREDITORS LEDGER CONTROL ACCOUNT

Details	folio	Dr.	Cr.
Balances	b/f	1985	26,423
Purchases			408,563
Purchases returns		32,662	
Bank		300,912	
Trade debtors		7,457	
Discounts rec.		9,027	
Balances	c/d	83,403	460
		435,446	435,446
		. . 460	83,403

45

46 The bank reconciliation statements.

46.1 Objectives:

- Interpret the cash book entries and bank statement entries.
- state the meaning and need of Bank Reconciliation Statement;
- explain the reasons for difference between the balances of Cash Book
- and bank statement;
- update the cash book
- prepare the Bank Reconciliation Statement.

46.2 Definitions

The bank Account (or The Analysed Cash Book) is the *account holders own record* of money received and spent.
The Bank Statement is the *banks record* of money received and spent by the account holder. This is viewed from the banks perspective.

The Bank Reconciliation Statement is then prepared to *reconcile (or fix) the two records* and check for any errors that have occurred.

46.3 The purpose of the bank reconciliation statement

It should be prepared regularly as part of the internal control system of the business to check:

a) the accuracy of the cash book
b) the accuracy of the bank statement
c) that undue delay is not occurring between payments, receipts and their clearance by the bank
d) to discover payments made and items received by the bank not entered in the cash book

46.4 Interpretation of the cash book bank account.

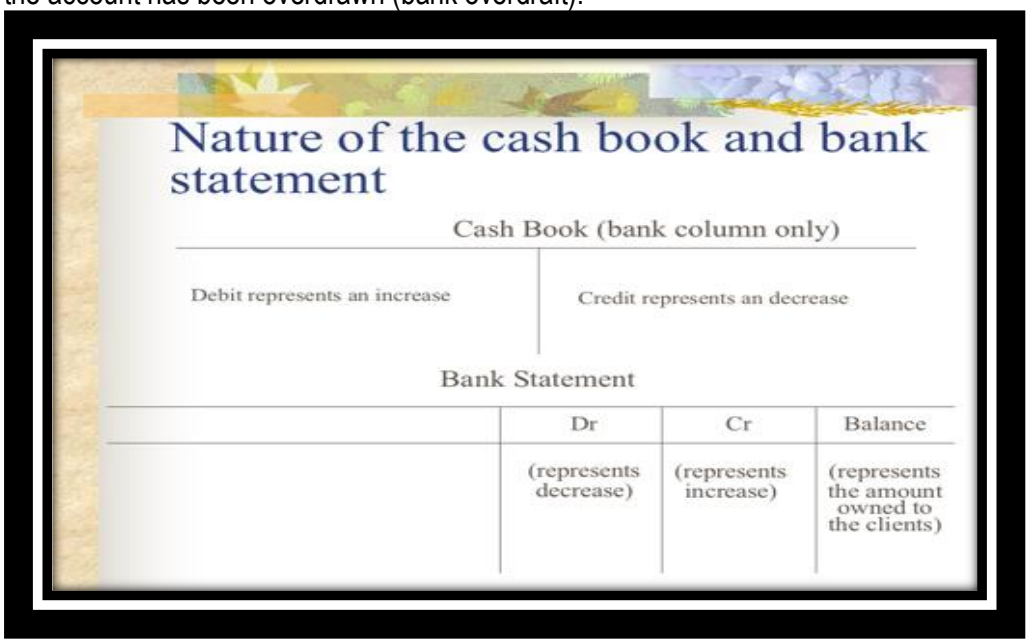
- It keeps records of the business' cash transactions.
- It is a real account which operates on the principle of:

Dr. what comes in/increase and Cr. what goes out/decrease.

- A debit balance shows/indicates the cash available in the account;
- while a credit balance indicates an overdrawn account or bank overdraft.
- An overdraft is short term financial assistance that is given to current account holders.
- It is shown as a current liability in the business' balance sheet.

46.5 Interpretation of the bank statement.

- It keeps the records of the cash deposited and withdrawn by the business from the banks point of view.
- It is the business' personal account in the banks ledger which operates on the principle of : Dr =the receiver and Cr = the giver.
- Hence all cash withdrawn by the business is debited to show that the business received; and all cash deposited into the account is credited to show what the business gives to the bank.
- All deposits represent what the bank owes the business.
- Thus a credit balance shows the cash available in the bank while a debit balance shows that the account has been overdrawn (bank overdraft).



46.6 Reasons for differences between the cash book balance and the bank statement balance

46.6.1 Uncredited items

These are deposits paid into the bank but do not appear on the statement as these items occurred too close to the cut-off date of the bank statement. They will appear on the next statement.
Banking made shown in the cash book but not on the bank statement

46.6.2 Unpresented Cheques

These are Cheques issued by the firm that have not yet been presented to its bank for payment.

46.6.3 Standing orders

These are instructions from the firm to the bank to make regular payments of a fixed amounts on predetermined dates to a specified person.

46.6.4 Direct debits

These are payments made directly through the firm's bank.

46.6.5 Bank charges

These are charges made by the bank to the company for banking services used.

46.6.6 Dishonored Cheques

Cheques deposited but subsequently returned by the bank due to the failure of the drawer to pay.

46.6.7 Credit transfers / direct credits

This is money received from the business' customers directly through the banking system.

46.6.8 Interest allowed by the bank

This is interest earned /received on deposits or fixed deposit account.

46.7 Drawing up a bank reconciliation statement

Three steps:

1. Check the bank statement and the cash book to identify the items which have been omitted.
2. Update the cash book with any omissions and errors made by the firm itself.
   - Credit transfers (debit cash book)
   - Bank interest (debit cash book)
   - Standing orders / direct debits (credit cash book)
   - Bank charges (credit cash book)
   - Dishonored Cheques (credit cash book)
3. Prepare the bank reconciliation statement

Bank Reconciliation Statement as at XXXX

	$	$
Corrected balance in hand as per Cash Book		x
Add Unpresented cheques	x	
Wrong credits by the bank	x	x
		x
Less Bank deposits not yet entered on Bank Statement	x	
Wrong debits by the bank	x	x
		x

Question:

Cash book(Bank column)

1996		$	1996		$
Dec 1	Bal b/f	2800	Dec 8	K Wong	1600
3	W Lee	1000	20	C Kwok	700
10	T Cheung	2000	29	M Tang	100
30	S Sin	1400	31	Bal c/f	4800
		7200			7200

Uncredited items

Unpresented cheque

Bank Statement

1996		Dr $	Cr $	Balance
Dec 1	Balance			2800
3	Cheque deposit		1000	3800
8	Cheque 76343	1600		2200
10	Cheque deposit		2000	4200
11	Dishonoured cheque	2000		2200
11	Service charges (Bank charges)	30		2170
12	Autopay-rent (Direct debit)	250		1920
20	Cheque 76344	700		1220
31	Bank interest		50	1270
31	Credit transfer-commission received		300	1570
31	Balance			1570

Answer:

Cash Book (Bank Column)

1996	$	1996	$
Dec 31 Balance b/f	4,800	Dec 31 T. Cheung – Dishonoured cheque	2,000
31 Commission Rec.	300	31 Bank charges	30
31 Bank Interest	50	31 Rent	250
		31 Balance c/f	2870
	5,150		5,150

•Identify the items which have been omitted in the cash book

To reconcile the bank statement with the Unadjusted cash book

Two steps:

- Check the bank statement and the cash book to identify the items which have been omitted.
- Prepare the bank reconciliation statement.

Begin with the unadjusted cash book balance and end with the bank statement balance

Bank Reconciliation Statement as at XXXX

		$	$
Corrected balance in hand as per Cash Book			x
Add Credit transfers	Amount received on bank statement	x	
Bank interest	But not on bank statement	x	
Unpresented cheques	Timing difference	x	
Wrong credits by the bank	Bank error	x	x
			x
Less Standing orders / direct debits		x	
Bank charges		x	
Dishonoured cheques		x	
Bank deposits not yet entered on Bank Statement		x	
Wrong debits by the bank		x	x
Balance in hand as per Bank Statement			x

Bank Reconciliation Statement as at 31 Dec 1996

		$
Corrected balance in hand as per Cash Book		2870
Add	Unpresented cheques	100
		2970
Less	Bank deposits not yet entered on Bank Statement	1400
Balance in hand as per Bank Statement		1570

•Only adjusted caused by timing difference

46.8 Post-dated cheque

It is a cheque which has not yet matured within the current accounting period.

46.8.1 Accounting treatment

The cheque should be held by the cashier and no entry should be made until the cheque becomes mature. If a post-dated cheque has been entered in the cash book, make correcting entries.

46.9 Bank overdrafts

The adjustment needed to reconcile a bank overdraft according to the firm's books (shown by a credit balance in the Cash Book) with that shown in the bank's records are the same as those needed when the account is not overdrawn.

Bank Reconciliation Statement as at 31 December 20X8

	£	
Overdraft as per cash book	(380)	
Add Unpresented cheque	63	
	(317)	
Less Bank lodgment not on bank statement	(106)	
Overdraft per bank statement		(423)

Practice question

On 31 December 2017 the bank column of Norman's cash book showed a debit balance of K1,500. The monthly bank statement written up to 31 December 2017 showed a credit balance of K2,950.

On checking the cash book with the bank statement it was discovered that the following transactions had not been entered in the cash book:

Dividends of K240 had been paid directly to the bank.
A credit transfer – Customs and Excise VAT refund of K260 – had been collected by the bank.
Bank charges K30.
A direct debit of K70 for the ACCA subscription had been paid by the bank.
A standing order of K200 for Norman's loan repayment had been paid by the bank.
Norman's deposit account balance of K1,400 was transferred into his bank current account.

A further check revealed the following items:

Two Cheques drawn in favor of T Chola K250 and F Hamududu K290 had been entered in the cash book but had not been presented for payment.
Cash and Cheques amounting to K690 had been paid into the bank on 31 December 2017 but were not credited by the bank until 2 January 2018.

REQUIRED:

a) Starting with the debit balance of K1,500, bring the cash book (bank columns) up to date and then balance the bank account.
b) Prepare a bank reconciliation statement as at 31 December 2017.

SOLUTION

Norman's Updated cash book.

DATES	DETAILS	DR	CR
Dec.31	Balance b/f	1,500	
	Dividends	240	
	HM Revenue and customs	260	
	Bank charges		30
	ACCA subscription		70
	Loan repayment		200
	Deposit account balance transfer	1,400	

	Balance c/d	3,400	3,100 3,400
	Up dated balance	3,100	

Norman's bank reconciliation statement
as at 31st, December 2017

Balance as per bank statement			*2,950*
updated cash book balance		*3,100*	
Add: unpresented Cheques:			
T. Chola	*250*		
F. Hamududu	*290*		
		540	
		3,640	
less : unrecorded/uncredited deposits			*(690)*
reconciled cash book balance			*2,590*

47 accounting for Clubs and societies

47.1 Objectives.

- Describe non-profit organizations and explain their main object
- Distinguish between receipts and payments accounts and income and expenditure accounts
- Prepare accounts for the following – receipts and payments, revenue generating activities, e.g. Refreshments, and subscriptions
- Define and calculate the accumulated fund
- Prepare income and expenditure accounts and statements of financial position
- Make the other adjustments as detailed as appropriate.

47.2 Not-For-Profit Organizations

The main purpose of such organizations is to provide social amenities to its members such as games of tennis, soccer, etc.
They can also be charities to help people. They exist not to make profits, thus the name not for profit making organizations.
They may be engaged in profit making activities, but profits arising from such is not shared by members but ploughed back in the organization to improve on services to members.

TERMS USED IN COMPARISON WITH TRADING ORGANISATIONS

Terms associate with npo	*commercial business*
Accumulated fund	Capital
Receipts and payments account	Cash book
Income and expenditure account	Profit and loss account
Surplus of income over expenditure	Net profit
Deficit of expenditure over income	Net loss

RECEIPTS AND PAYMENTS ACCOUNT

- A summary of all cash and bank transactions throughout the year.
- The receipts and payments account is in essence the cash book.
- It is a summary of cash receipts and cash payments.
- Smaller clubs and charities with no other assets (apart from cash) and no liabilities will use the receipts and payments account as a financial statement.
- No balance sheet is produced.

Procedure:

- Start with the opening cash balance.
- ***Add*** all cash received during the year regardless of whether it is capital, revenue or period for which it is received (i.e. whether it is received in advance or areas).
- ***Subtract*** cash payments during the year regardless of whether it is capital, revenue or period for which it is paid (i.e. whether it is paid in advance or accrued)

Example: receipts and payments account

ARMSTRONG Body Building Club

Receipts and payments account for the year ended
31 December 20X4

Receipts	K	Payments	K
Balance b/f	200	Bar purchases	160
Subscriptions	6,450	Rental	720
Bar Sales	240	Care takers wages	1,800
Donations	150	Printing & postage	22
		Heat & light	60
		Repairs	15
		Balance c/d	4,263
	7,040		7,040

Balance b/d 4,263

N.B. The receipts side is same as debit and payments side credit of the cash book.

Advantages and disadvantages of receipts and payments account:

Advantages

(a) Very easy to prepare

(b) Very easy to understand especially cash position

(c) It is used as a basis for the preparation of the income and expenditure account

Disadvantages

(a) Only accounts for cash. There could be other assets in use.

(b) Does not account for any amounts paid in advance or owing.

(c) Does not distinguish between capital and revenue expenditure

(d) Does not account for depreciation of non-current assets.

Income and Expenditure Account

- Income and expenditure account is the same as income statement for trading organizations.
- The principals of matching or accruals concepts are applied to income and expenditure accounts in the same way as for income statement in trading organizations.
- List and total up all **revenue income** applying to the **year in question** only.
- This means adjustments must be made for accruals and prepayments
- When total income exceeds expenditure the club makes a **Surplus**
- When total expenditure exceeds income the club makes a **Deficit**

XXXX Sport Club

Income and Expenditure account for the year ended XXXX

	$	$
Income		
Income received		X
Subscriptions – Annual subscriptions		X
- Life membership fees		X
- Joining fees/Entrance fees		X
Profit on fund raising activities		
(Related Proceeds – Related Expenditure)		X
Profit on disposal		X
Donations/Subsidies received		X
		X
Expenditure		
Expenses incurred	X	

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	$	$
Subscriptions/bad debt written off	X	
Loss on fund raising activities		
(Expenditure- proceed)	X	
Loss on disposal	X	
Depreciation	X	
Bar loss (from bar trading a/c)	X	X
Surplus/ (deficit)		X

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TRADING ACTIVITIES WITHIN THE NOT-FOR- PROFIT ORGANISATION

The main source of income for non-trading organizations is subscriptions from members. However, they may engage in profit ventures like owning a bar.

In such a case a separate bar income statement will be prepared to determine profit or loss arising from it, and transferred to income and expenditure account.

For other profit ventures such as dinner dance or fete income and expenses are netted and the resultant profit or loss also transferred to income and expenditure account.

Accumulated fund

In a trading organization it is known as capital. In most cases it may not be given. It should be calculated by identifying assets and liabilities given at a particular time . Thus.

Accumulated fund = Assets – Liabilities

Example: accumulated fund

The North East Rotary Club had the following assets and liabilities as at 1 January 20X1, the beginning of the year.

Cash and Bank balances K210, Equipment at valuation K975, Subscriptions in arrears K65, Subscriptions in advance K10, Owing to suppliers of competition prizes K58 and Inventory of competition prizes K38.

Required:

Calculate the accumulated fund as at 1 January 20X1, to be included in balance sheet.

Solution:

	K	K
Assets:		
Cash and bank balance	210	
Subscriptions in arrears	65	
Equipment	975	
Inventory of competition prizes	38	
Total assets		1288
Liabilities:		
Subscriptions in advance	10	
Owing to suppliers	58	
Total liabilities		68
Accumulated fund at 1 January 20X1		1220

Subscriptions

This may be the main source of income for not profit making organizations.

Subscription is an agreed amount each member must pay at regular intervals e.g. monthly or annually. Members will enjoy facilities of the organization at no cost, while nonmembers will have to pay high fees to use same facilities and sometimes may be denied access even if they have money.

Subscriptions account

A subscription account is always maintained to show the amount collected, amount not collected and amounts paid in advance.

N.B. Members who have not paid the subscriptions and their membership has not lapsed are considered as receivables because they have not paid the institution and yet they have been enjoying the services. This is called ***subscriptions in arrears***.

Subscriptions in arrears should be included as part of income (subscriptions) in the year they are not paid and shown as current asset in the balance sheet.

Remember the matching or accruals concept. When they are paid the following year, they should not be included into subscriptions for that year and are no longer assets.

Practice question

at the beginning of the year ,1 January 2016, Matero social club had the following assets and liabilities:

ITEM	K
equipment at cost	1,000,000
furniture at cost	1,500,000
cash at hand	200,000
cash at bank	450,000

stock of refreshments	250,000
subscriptions in advance	50,000
subscriptions in areas	60,000
credit suppliers of refreshments	120,000
sundry expenses owing	50,000

As at 31 December, the end of the year, the club presented the receipts and payments as follows:

RECEIPTS	K	PAYMENTS	K
Opening balances:		New equipment	400,000
Cash at hand	200,000	Rent and rates	500,000
Cash at bank	450,000	Stationery	200,000
Subscriptions	1,200,000	Wages –office assistant	450,000
Sale of raffle tickets	580,000	Creditors for refreshments	650,000
Sale refreshments	900,000	Sundry expenses	120,000
		Raffle tickets and expenses	200,000
		Balances:	
		Cash at hand	210,000
		Cash at bank	600,000
	3,330,000		3,330,000

The treasurer had the following additional information at the end of the year 31 December 2016:

1. Stock of unsold refreshments was k390,000
2. Subscriptions in advance k100,000
3. Rent paid in advance k120,000
4. The club policy was to depreciate:
    a. Equipment at 20% on cost
    b. Furniture at 10% on cost.

You are required to:

a) Calculate the club's accumulated fund at 1 January 2016.
b) Prepare the club refreshment trading account
c) Prepare the income and expenditure account for the year ending 31 December 2016.
d) The balance sheet as at 31 December 2016.

Solution.

Matero social club
Accumulated fund = assets – liabilities

assets		
Equipment	**1,000,000**	
Furniture	**1,500,000**	
Cash	**200,000**	
Bank	**450,000**	
Stock of refreshments	**250,000**	
Subscriptions in areas	**60,000**	
Total assets		**3,460,000**
Less liabilities:		
Subscriptions in advance	**50,000**	
Credit supplies refreshments	**120,000**	
Sundry expenses owing	**50,000**	
Total liabilities		**(220,000)**
Accumulated fund		**3,240,000**

Matero social club
Refreshment Trading account
for the year ended 31December 2016

Details	**k**	**K**	**k**
Sales of refreshments			**900,000**
Opening stock		**250,000**	
Purchases of refreshments		**650,000**	
Total stock available for sale		**900,000**	
Less:			
Creditors at start	**120,000**		
Unsold stock of refreshments	**390,000**		
		(510,000)	
Cost of goods sold			**(390,000)**
Profit on refreshments			**510,000**

Matero social club income and expenditure account
for the year ended 31 December 2016

Details	K	K	K
INCOME			
Subscriptions			
Add: subscriptions in advance at start			**1,200,000**
			50,000
Less: subscriptions in areas at start		**60,000**	**1,250,000**
Subscriptions in advance		**100,000**	
			(160,000)
Subscriptions for the year			**1,090,000**
Profit on refreshments			**510,000**
Sales of raffle tickets			**580,000**
Total income			**2,180,000**
Less: expenditure			
Rent and rates	**500,000**		
Less: prepaid amounts	**120,000**		
		380,000	
Stationery and postage		**200,000**	
Wages of office assistant		**450,000**	
Sundry expenses	**120,000**		
Less amounts owing at start	**(50,000)**		
		70,000	
Raffle tickets and expenses		**200,000**	
Dep: equipment		**280,000**	
Furniture		**150,000**	
Total expenditure			
surplus			**(1,730,000)**
			450,000

Example: Subscriptions
The North East Rotary Club had the following details relating to subscriptions for the year 1 January 20X1 to 31 December 20X1.
Cash received from members during the year to 31 December 20X1 K1987.
On 1 January 20X1, some members still owed the club K65 for 20X0, and some members had also not paid K85 for 20X1.
On 1 January 20X1, some members had paid in advance K10 in 20X0 for 20X1, and also at 31 December 20X1, some members had paid K37 in advance for 20X2.
Required:
Show how the entries will be made in subscription account and then show amount to be shown in income and expenditure account as subscriptions for 2017.

Solution:
Step 1: Open subscription account and show the opening balances

Dr.	Subscription account		Cr.
	K		K
1 January 2017 Bal. b/f	65	1 January 2017 Balance b/f	10

subscription account

Date	details	folio	Dr	Cr
January 1 2017	Opening Balances	b/f	65	10

The amount of K65 appearing on the debit side is an asset. Money is for the club though not yet paid. K10 is liability. Money is not yet for club though the club has it.
Step 2: Upon receiving cash as subscriptions from members.

Dr. Cash account
Cr. Subscription account

Dr.	Subscription account		Cr.
	K		K
1 January 20X1 Bal. b/f	65	1 January 20X1 Balance b/f	10
		Cash	1987

Dr.	Cash account		Cr.
	K		K
Subscriptions	1987		

Step 3: Put in the closing balances for accruals and prepayments. The balancing figure is subscription for 20X1.

Subscription account

Dates	Details	folio	Dr	Cr
1 Jan. 20X1	Balances	b/f	65	10
	Cash			1987
	Income and expenditure account		1980	
31.Dec.	Balances	c/d	37	85
			2082	2082
	balances		85	37

K1980 will be credited to income and expenditure account.
The amount to be shown as income from subscriptions for 20X1 is K1980.
K85 will be shown in balance sheet under current assets as subscriptions in arrears.
K37 will be shown in balance sheet under current liabilities as subscriptions in advance.

In statement form it will be shown as:

	K	K
Subscriptions received (cash)		1987
Add: Subscription paid in advance 2010	10	

Subscription in arrears 2011	85	
		95
		2082
Less: Subscriptions paid in advance 2012	37	
Subscriptions in arrears 2010	65	
		(102)
		1980

Income and expenditure

The following is a summary of the receipts and payments of North East Rotary Club during the year ended 31 December 20X1.

North East Rotary Club
Receipts and payments accounts for the year ended
31 December 20X1

Dr	K		K Cr.
Cash and bank balance	210	Secretarial expenses	163
Sales of competition tickets	437	Rent	1402
Members subscriptions	1987	Visiting speakers expenses	1275
Donations	177	Donations to charities	35
Refund of rent	500	Prizes for competitions	270
Balance c/d	13	Stationery & printing	179
	3,324		3,324
		Balance b/d	13

The following valuations are also available:

As at 31 December	2010	2011
	K	K
Equipment (original cost K1,420)	975	780
Subscriptions in arrears	65	85
Subscriptions in advance	10	37
Owing to suppliers of competition prizes	58	68
Inventory of competition prizes	38	46

Required:

(a) Calculate the value of the accumulated fund of the club as at 1 January 20X1.

(b) Reconstruct the following accounts for the year ended 31 December 20X1.
   (i) the subscription account
   (ii) the competition prizes account

(c) Prepare an income and expenditure account for the club for the year ended 31 December 20X1 and a balance sheet as at that date.

Solution:

(a)	Accumulated fund		
	Assets:	K	K
	Cash and bank balance	210	
	Subscriptions in arrears	65	
	Equipment	975	
	Inventory of competition prizes	38	
		1288	
	Liabilities:		
	Subscriptions in advance	10	
	Owing to suppliers	58	
		68	
	Accumulated fund at 1 January 2011	1220	

Competition prizes account

Details	folio	Dr	Cr
Balances	b/f	38	58
Bank		270	
Cost of prizes given to income and expenditure account (Bal. Fig)			272
balances	c/d	68	46
		376	376
balances	b/d	46	68

North East Rotary Club
Income and Expenditure account for the year ended 31 December 2011

	K	K
Income		
Subscriptions		1980
Ticket sales	437	
Less cost of prizes	(272)	
Profit on competition		165
Donations		177
		2,322
Expenditure		
Secretarial expenses	163	
Rent (1402 – 500)	902	
Speakers expenses	1,275	
Donations to charities	35	
Stationery and printing	179	

Depreciation	195	
		(2749)
Deficit		(427)

North East Rotary Club
Balance sheet as at 31 December 20X1

Fixed Assets	**Cost**	**Dep.**	**N.B.V.**
Equipment	1420	640	780
Current assets			
Inventory of prizes		46	
Subscriptions in arrears		85	
Total current assets			131
less current liabilities			
Current liabilities			
Payables for prizes		68	
Subscriptions paid in advance		37	
Bank overdraft		13	
Total current liabilities			(118)
Net assets/working capital			13
Total assets			793
Financed by:			
Accumulated fund at 1 January 20X1			1,220
Less deficit			(427)
			793

MASTER KEYS

PART THREE – GRADE 12 WORK

48 INCOMPLETE RECORDS – SINGLE ENTRY

48.1 Objective

- Define single entry system of accounting.
- Distinguish between double and single entry
- Explain increase and decrease in net worth and Statement of affairs
- Prepare final accounts and balance sheet from incomplete records

48.2 Definitions

- Incomplete records problems occur when a business does not have a full set of accounting records. (ZICA)
- Single entry is an accounting system that does not follow double entry system.
- **Single entry** is a system of accounting in which only one aspect of a transaction is recorded. Some of the information is missing.

48.3 Reasons for not keeping double entry system

- Lack of accounting knowledge
- Main concentration is on primary activity
- Lack of knowledge on legislative requirements for accounting record
- Hiding cash transactions for tax avoidance
- Confusing business and personal banking transactions
- Lost accounting records e.g. via theft or fire
- It is convenient for the business owner (cheaper, less time consuming)

48.4 Difference between double entry system & incomplete Records.

- Basis of difference

  Recording of both aspects (Double entry records every transaction and incomplete records few transactions)
- Type of accounts

  (All accounts are considered in double entry only personal account are considered in incomplete records)
- Trial balance

  (Trial balance is prepared in double entry system, Trial balance is not prepared in incomplete records)
- Net profit/ loss

  (Profit/Loss is calculated by preparing trading and profit &loss a/c in double entry system, while a Statement of profit is prepared in incomplete records to find the same.
- Financial position

  (Balance sheet is prepared in double entry whereas a statement of affairs is prepared in incomplete records)
- Adjustments

  Adjustment are considered in double entry, while adjustments are not considered in incomplete records.

48.5 Sources of Information

- Cash book/daily sales book

- Debtors book
- Creditors book
- Stock book
- Bank records
- Accounts receivable
- Accounts payable
- Business Activity Statements
- Instalment Activity Statements
- Insurance companies
- Finance or banking organizations
- The previous accountant

48.6 ASCERTAINMENT OF PROFIT OR LOSS FROM INCOMPLETE RECORDS

- Statements of affairs method
- Profit as an increase in capital
- Ascertaining profits given opening and closing balances of assets and liabilities
- Ascertaining profits using a full set of financial statements
- Conversion into double entry method

48.7 Statement of affairs method:

Under this method Opening and Closing capital is calculated.
Then statement of profit is prepared to find profit/loss during the year.

48.7.1 Computation of Profit

Capital at end
Less capital at start
= change in capital
Less additional capital
Add drawings
= profit

ILLUSTRATION

Calculate the profit or loss from the following data:
Withdrawals by the proprietor during the year K30,000.Capital at the beginning of the year i.e., 1 Jan. 2015 K120,000. Capital at the end of the year i.e., 31 Dec 2015 K200,000. Capital brought in by the proprietor during the year K50,000.

WORKINGS

Capital at the end	***200,000***	
Less capital at start	***(120,000)***	
Change in capital		***80,000***
Less additional capital		***(50,000)***
		30,000
Add: drawings		***30,000***
net profit		***60,000***

48.8

48.9 Procedure in coming up with full sets of accounts.

- Draw up the opening statement of affairs if it's not given in order to calculate the capital.
- Draw up a cashbook summary to discover the cash and bank balance.
- Draw up total debtors and total creditors accounts to calculate the sales and purchases for the year.
- Find the amount of an expense that must be shown in the profit and loss account especially where there are accruals or prepayments at the beginning and end of the year.
- Draw up the trading and profit and loss account and the balance sheet.

48.10Tasks involved in coming up with financial statements

- Computation of cost of purchases and other expenses
- Computation of total amount of sales
- Establishing the amount of accounts payable and accruals
- Establishment of accounts receivable and prepayments

48.11CREDITORS LEDGER CONTROL ACCOUNT

Dates	Details	Folio	DR.	CR.
Jan 1	Opening Balance of creditors	b/f		xxxx
	Cash payments to suppliers/creditors		xxx	
	Cheques issued to suppliers/creditors		xxx	
	Purchases returns		xxx	
	Purchases (balancing figure)		___	xxxx
			xxx	xxx

Computation of Purchases using the Cost of goods sold

Since:	Opening inventory	xxx
	plus Purchases	xxx
	Less Closing inventory	(xxx)
	Equals Cost of goods sold	xxx
Then:	Cost of goods sold	xxx
	Plus Closing inventory	xxx
	Less Opening inventory	(xxx)
	Purchases	xxx

Computation of Sales

DATES	DETAILS	folio	Dr	Dr
Jan 1	Opening balances of debtors		XXXX	
	Cash receipts from debtors			XXX
	Cheques received from debtors			Xxxx
	Sales returns			XXX
	Sales(balancing figure)		XXXX	_____
			XXXX	XXX

USING THE EQUATION

Opening balance + sales – receipts from debtors + returns= closing balance.

We can then use the missing information as the subject of the formula.

Thus; sales = opening balance – Receipts + returns + closing balance

Exam. Questions.

1) Single entry system has effect

A. None
B. One side effect
C. Two sided effect
D. Three sided effect

Correct Answer: One side effect

Q.2) In single entry system, it is not possible to prepare:

A. Receipts and payments A/c
B. Trial balance
C. Balance sheet
D. Account sales

Correct Answer: Trial balance

Q.3) Mr.Vinod a small shop-keeper is using single entry system because____

A. None of these
B. Credit transactions are many
C. It is not costly
D. Cash transactions and credit transactions are more

Correct Answer: It is not costly

Q.4) Credit sale can be obtained by preparing

A. Cash book
B. Debtors
C. Creditors
D. Statement of affairs

Correct Answer: Debtors

Q.5) Cash in hand can be obtained by preparing

A. Debtors
B. Creditors
C. Statement of affairs
D. Cash book

Correct Answer: Cash book

Q.6) Profit is calculated by the formula

A. None of these
B. Capital at the end + Drawing – Fresh capital- Opening capita
C. Opening Capital + Drawing + Fresh Capital- Ending capital
D. Capital at the end - Drawing – Fresh capital – opening capital

Correct Answer: Capital at the end + Drawing – Fresh capital- Opening capita

Q.7) A statement of assets and liabilities prepared under the single entry system is called

A. Statement of affairs
B. Financial statement
C. Balance sheet
D. Cash book

Correct Answer: Statement of affairs

Annie is a sole trader who does not keep full accounting records. The following details relate to her transactions with credit customers and suppliers for the year ended 30 June 20X6.

Trade receivables, 1 July 20X5
Trade payables, 1 July 20X5 - 60,000
Cash received from customers-686,400
Cash paid to suppliers - 302,800
Discounts allowed- 1,400
Discounts received - 2,960

Contra between payables and receivables ledger - 2,000
Trade receivables, 30 June 20X6 - 181,000
Trade payables, 30 June 20X6 - 84,000

What figure should appear in Annie's statement of profit or loss for the year ended 30 June 20X6 for purchases?

SOLUTION

4 C

Payables:	$
Balance b/f	60,000
Cash paid to suppliers	(302,800)
Discounts received	(2,960)
Contra	(2,000)
Balance c/f	(84,000)
Purchases	331,760

Practice questions.

(1) The position of Mrs. Kaminda as at 31st December 2016 was as follows

Premises	5 000
Plant and Machinery	3 000
Stock	6 500
Debtors	8 750
Cash at bank	1 500
Creditors	9 375

On 1st January 2016, his capital was 27 000 and during the year his drawings amounted to 2 500. He paid into his business 1 000 which was the sale proceeds of his private car.

Required:

Prepare the statement of affairs and ascertain his profit or loss for the year.

Solution

Mrs. Kaminda

Statement of affairs as at 31st December, 2016 (Balance Sheet)

FIXED ASSETS	COST	DEP	NBV
Premises	**5 000**	**00**	**5 000**
Plant and machinery	**3 000**	**00**	**3 000**
	8 000	**00**	**8 000**
CURRENT ASSETS			
Stock			
Debtors		**6 500**	
Cash at bank		**8 750**	
		1 500	
		16 750	
CURRENT LIABILITIES			
Creditors		**(9 375)**	
Working Capital			**7 375**
			15 375
FINANCED BY			
Opening capital	**27 500**		
Add additional capital	**1 000**		
		28 500	
Less Net Loss		10 625	
		17 875	
Less Drawings		**2 500**	
			15 375

49 Profit as an increase in capital

This year's capital minus last year's capital = Net profit

= K3,000 - K2,000

Therefore, the profit will be K1,000

If drawings hand been for instance K700

The profit must have bee K1700

Last year capital + profits – drawings = this year capital

K2,000 + X – 700 = K3,000

K2,000 = X – 700 = K3,700 :.

= 2,000 + X = 3,700

= X = 3,700 – 2,000

X = 1,700

The statement of affairs is a balance sheet at the beginning of a Trading period. Prepared using the word equation;

Opening Capital + Profit – Drawings = Closing Capital

49.1.1 Calculation of purchases and sales using the statement format.

J. Kawaya lost the whole of his stock in fire on 17th March 2017.

The last time that a stock taking had been done was on 31st December 2016. The last balance sheet date, when stock was valued at cost @1950, purchases from then until 17th March 2017 was 6,870 and sales in that period were K9,600. All sales were made at a uniform gross profit margin of 20 per cent.

The Trading account can be drawn from known

	K	K	K
Sales			9,600
Less: Cost of Sales			
Opening stock		1,950	
Purchases		6,870	
Less: Closing stock		8,820	
Cost of sales		C ( )	
Gross profit			B ( )
			A__?
Workings			
(a) Gross profit = $^{20}/_{100}$ x 9,600			
= 1,920			
(b) 9,600 – 1,920 = 3,680		1,140	
(c) Closing stock = 8,820 – 7680 =			
Cost of goods avails able – cost of sales			

50 GROSS MARGINS AND MARK UPS

Some incomplete records questions involve the relationship between sales, cost of sales and gross profit. Using this relationship and provided the gross profit percentage is given any of the three items can be computed.

50.1 Gross Profit Percentages

Gross profit can be written or expressed either as percentage of sales or as a percentage of cost of sales.

When gross profit is expressed as a percentage of sales, it is known as the Margin. Whereas when gross profit is expressed as a percentage of cost of sales, it is known as the Mark Up.

- Margin is gross profit percentage on sales
- Mark up is gross profit percentage on cost price i.e cost of sales

50.1.1 Relationship between margin and mark up

Both mark up and margin are profit percentages of difference amount. Therefore if one is known then the other can be calculated or found. e.g Mark up then margin

$^{1}/_{4}$ $^{1}/_{5}$

Where $^1/_4$ + 1 = $^1/_5$ or $^1/_4$ = $^1/_{5-1}$

Converting from margin to mark up and vice versa
Example
Moonga a sole Trader has provided you with the following information relating to the year ended 31-12-2014.

He has not made a note of cash drawings or cash receipt/received. The following items were paid from taking profit prior to banking.

Purchases 760

Sundry expenses 400

Moonga as estimated that his gross profit percentage is 25% on cost. Calculate Moonga's profit for fee year.

Calculate Moonga's net profit for the year.

Moonga's Income statement for the year ended

	K	K	K
Sales			950
Less: Cost of sales			
Purchases			760
Gross profit			190
Less: Expenses			
Sundry expenses			400
Net loss			(210)

51 ACCOUNTING FOR PARTNERSHIP BUSINESS

51.1 Rationale

A partnership business is a business run by two or more like minded individuals with a view of making profit.
The people (individuals) who own the partnership are called partners. The purpose of partnership accounting therefore, is to develop in the learner collaborative skills necessary for them to solve problems at home and in the society.

51.2 Objectives

- Define partnership and list its essential features
- Explain the meaning and list the contents of partnership deed
- Prepare partners' capital accounts under fixed capital methods.
- Explain the distribution profit or loss among the partners and prepare the Profit and Loss Appropriation Account.
- Calculate interest on capital and drawing under various situations.
- Explain how guarantee for a minimum amount of profit affects the distribution of profits among the partners.

51.3 Purpose for individuals entering into partnership

(i) Increased capital
(ii) Sharing of business ideas
(iii) Divisions of labour/sharing of responsibilities.
(iv) Pooling of skills
(v) Sharing costs

51.4 Partnership Agreement:

When a partnership business is to be formed the parties involved should draw up an agreement which should stipulate the concerns on how the partnership should be formed and run. The concerns that need to be addressed in this agreement may include

- Partners capital contributions
- Interest on capital to be earned by the partners if any
- Interest on drawing if any
- Salaries if any to partners
- Ratio of sharing profits/loses
- Procedures to follow when
    - (i) Admitting a new partner
    - (ii) When a partner dies
    - (iii) When a partner retires

Thus a partnership agreement or partnership deed is an agreement made by the partners stipulating the conditions regarding the running of the business

51.5 Where no Partnership agreement Exists:

In partnership business where no partnership agreement exists the following occurs
(i) Profit and loss are to be shared equally
(ii) There is to be no interest on capitals

(iii) No interest is to be charged on drawings
(iv) Salaries are not allowed.

51.6 Final accounts for partnership business

- Income statement (Trading and profit and loss Account)
- Profit and loss appropriate Account
- Balance sheet

- The income statement for the partnership is exactly the same as the one you already know for the sole trader.
- The balance sheet for the partnership business is also same as for the sole trader with a small difference only on the capital structure which includes the individual partner's capital and current account balances (if credit balance i.e)

51.7 New Items

The only new items on partnership is the preparation of the partnership profit and loss appropriation Account and the partners current accounts.

51.7.1 Profit and Loss appropriation Account.

This is an account in which the profit or loss made in the partnership business are distributed/shared amongst the partners.

51.8 Contents of profit and loss appropriate Account

(i) Profit for the year
(ii) Interest on drawings
(iii) Interest on capitals
(iv) Salaries to partners
(v) Share of residues

51.8.1 Drawings:

These are advances taken against anticipated profits. Thus the Drawing taken should not exceed the expected share of profit. Drawings reduce the capital of the business. If partners are making unnecessary drawings the partnership business may eventually collapse as all the capital may be finished. Thus to prevent unnecessary drawings, interest on drawings are charged.

51.8.2 Interest on Drawings

This is a charge to partners on the drawings made which is usually done to restrict partners to a given percentage (%) of the drawings made or a fixed figure. The purpose of the interest on drawings is to deter/prevent unnecessary drawings. All the partners that have made drawings should be charged with interest on drawings if it is the firms policy to charge.

51.8.3 Interest on Capitals:

This is a reward that partners earn for the capital contribution they made in firm. The interest on capital is usually a percentage (%) of the capitals each partner contributed. Interest on capitals is earned by all the partners.

51.8.4 Salaries to partners:

There are basically two types of partners, an active partner and sleeping partner/dormant partner. An active partner is one who is actively involved in the running of the business and for his/her active involvement in the running of the business gets a salary, while a sleeping partner is not actively involved in the running of the business and should not get any salary. Only active partners get a salary.

51.8.5 Share of residues:

This is the remainder of the profits after all the rewards/earnings have been appropriated. It is distributed according to the profit sharing ratios provided in the partnership agreement.

In an event where profit and loss sharing ratios are not given the partners should share the residues according to the capital contributed by each partners. All the partners get a share of residues.

52 Format for partnership appropriation account.

A and B Partnership
Profit and Loss Appropriation Account
For the year ended 31 Dec 2016

Details				
Net profit brought down			XXX	
Add: Interest on drawings				a=K100000
A		x		
B		x		
Less: Interest on capital				b=K70 000
A	x			
B	x			
Salary B	x			
Share of residues A				
B				
		100 000		
	70 000			

The partners A and B shares profit and loss in the ratio 3:2 and assuming the total Cr side (a) = K100 000 and the total Dr side (b) = 70 000.
Complete the tables by calculating what each person will get as a share of residue.
Calculations
Residues = 100 000 – 70 000 = K30 000
A's share of residue = 3/5 x 30 000 = K18 000 while B's share of residue = 2/5 x 30 000 = K12 000

Practice Question one

Niza and Taonga were in partnership sharing profits and losses equally. The following Trial Balance was extracted from their books on 31 December 2008.

	Dr K	Cr K
Capitals: Niza		28 000
Taonga		14 000
Drawings: Niza	6 800	
Taonga	4 400	
Rent received		156
Furniture and Fittings (cost K1 759)	1 360	
Opening Stock	21 000	
Trade debtors/Trade creditors	16 328	14 380
Purchases/Sales	152 000	206 000
Wages and Salaries	25 454	
Freehold property	18 500	
General expenses	9 832	
Discounts	4 154	
Cash at Bank	2 408	
Rates	300	
	262 536	262 536

The following information was also available on 31 December 2008:
Closing stock was valued at K23 500;
Interest on capital was to be credited to the partner's Current Accounts at 5% per annum.
Interest on drawings was to be charged as follows:
Niza K170
Taonga K110
Wages and salaries due amounted to K304;
Rent received included K26 for the following year
Furniture and fittings were to be depreciated at 10% per annum on cost.
Niza is entitled to a salary of K2000 per annum
Provision for bad debts is to be 10% of debtors.
Required: The partnership Trading and Profit and Loss Accounts.The partnership Appropriation Account for the year ended 31 December 2008, and the Current Accounts.The Balance Sheet as at 31 December 2008.

Profit and loss account
For the year ended 31 Dec 2008

Details	K	K	K

	Sales			206 000
	Less: Cost of Sales			
	Opening Stock		21 000	
	Add: purchases		152 000	
	Total cost of goods available for sale		173 000	
	Less: closing stock		(23 500)	
App	Cost of sales			149 500
ropri	Gross profit			56 500
atio	**Add: other gains**			
n	Rent received		156	
acc	Less: rent received in advance		(26)	
ount	Total Income			130
s	Less : Expenses			56,630
	Wages and Salaries	25 454		
	Add: wages and salaries due	304	25 758	
	General expenses		9 832	
	Discount allowed		4 154	
	Rates		300	
	Furniture and fittings [10/100 x 1759]		175.9	
	Provision for Bad debts		1 632.8	
	Total expenses			41 852.7
	Net profit			14 777.3

Net profit	b/d		14 777.3
Interest on drawings:			
Niza			170
Taonga			110
Interest on capitals:			
Niza (5/100 x 28000)	1 400		
Taonga (5/100 x 14000)	700		
Salary			
Niza		2 000	
Sharing residues			15 057.3
Niza 28 000 / 42 000 x 10 957.3 = 7,305	7,305		
Taonga 14000 / 42000 x 10 957.3 = K3 652.43	3 652.43		
		15 057.3	

Current Accounts

Details		Niza Dr	Niza Cr	Taonga Dr	Taonga Cr
Drawings		6 800		4 400	
Interest on drawings		170		110	
Interest on capitals			1 400		700
Salary			2 000		
Share of residues			7 304.87		3 652.43
Balances	c/d	3 734.87			157.57
		10 704.87	10 704.87	4 510	4 510
Balance	b/f		3 734.87	157.57	

Workings
Share of residues
Niza 28 000 x 10 957.3 = K3 734.87
42 000
Taonga 14 000 x 10 957.3 = K3 652.43
42 000

Niza and Taonga Partnership Balance Sheet as at 31st December, 2008

Fixed Assets	Cost	Dep	NBV
Fee lad Premises	18 500		18,500
Furniture and fittings	1 759	574.9	1,184.1
	20 759	574.9	19,684.10
Current Assets:			
Stock		23,500	
Debtors	16,328		
Less: provision for Bad debts	(1,632.8)		
		14,695.2	
Bank		2,408	
Total current Assets		40,603.2	
Less: Current Liabilities			
Creditors	14,380		
Wages and Salaries due	304		
Rent received due	26		
Total current liabilities		(14,710)	
Working capital			25,893.2
Net assets			45,577.3
Financed by	NIZA	TAONGA	
Fixed Capitals	28,000	14 000	
Current accounts	3,734.87	(157.57)	
	31,734.87	13,842.43	
Capital employed			
			45,577.3

53 Practice Question 2

Mvula and Mubanga are in partnership.
The following is extracted from their books at 31/12/09.

	K
Premises	6 000 000
Fixtures and fittings	4 500 000
Capital accounts: Mvula	6 000 000
Mubanga	6 000 000
Current Accounts: Mvula (DR)	100 000
Mubanga (CR)	150 000
Drawings: Mvula	800 000
Mubanga	900 000
Creditors	5 000 000
Provision for bad debts	250 000
Debtors	8 000 000
Net Profit	5 000 000
Cash in hand	700 000

The following additional information is made available at 31/12/09:

1) Stock at 31/12/09 was K2 800 000.
2) Depreciate fixtures and fittings at 10 percent per annum.
3) Interest on partners' capitals to be at 5 percent.
4) Mvula is entitled to a salary of K500 000.
5) Wages accrued K400 000.
6) Partners to share profits equally.
7) Provision for bad and debts to be equal to 10 per cent of debtors

Required:

(a) Prepare the profit and loss appropriation account for the year ended 31/12/09
(b) Show the current accounts for the partners as they would appear at that date. These accounts may be shown separately in table form.
(c) Prepare the partnership balance sheet as at 31/12/09

Solution

Mvula and Mubanga Partnership
Profit and loss appropriation account
For the year ended 31 December 2009

Details			
Net profit			5 000 000
Less: Interest on capitals :			
Mvula (5/100 x 6 000 000)	300,000		
Mubanga (5/100 x 6 000 000)	300,000		
		600,000	
Salary: Mvula		500 000	
Share of residues:			
Mvula 3,900 000 / 2		1 950 000	
Mubanga 3,900 000 / 2		1 950 000	
		5 000 000	5 000 000

Current Accounts

Details		Mvula		Mubanga	
		Dr	Cr	DR.	CR.
Balances	b/f	100 000			150,000
Drawings		800 000		900,000	
Interest on capitals			300 000		300,000
Salary	c/f		500 000		xxx
Share of residues			1 950 000		1,950,000
Balances		1850 000		1,500,000	
		2 ,750,000	2, 750,000	2,400,000	2,400,000
Balances	b/d		1, 850 000		1,500,000

Mvula and Mubanga Partnership
Balance sheet As at 31 Dec 2009

Details	COST	DEP	NBV
Fixed Assets			
Premises	6 000 000		6 000 000
Fixtures and Fittings	4 500 000	450 000	4 050 000
	1 050 000	450 000	10 050 000
Current Assets			
Stock		28 000 000	
Debtors	8 000 000		
Loss: Provision for Bad debts (10/100 x 8000 000)	800 000	7 200 000	
Cash		2 100 000	
Total Current Assets		10 700 000	
Less Current Liabilities			
Creditors	5 000 000		
Wages and Salary accrued	400 000		
Total Current Liabilities		5 400 000	5 300,000
Working capital			15 350,000
Net assets.			
Financed by:	Mvula	Mubanga	
Fixed Capital	6 000 000	6 000 000	
Current accounts	1 850 00	1 500 000	
Capital employed	7 850 000	7 500 000	15 350,000

NOTE:
Salary to partners need not be shown in the profit and loss and Balance but only shown in the profit and loss appropriation account.

54 MANUFACTURING ACCOUNTS

54.1 Rationale

A manufacturing organization is one that manufactures (produces) goods for sale. This could either be a sole trader, a partnership or a company. The purpose of this topic is to help learners gain knowledge, skills, and experience to manage the costs associated with the production of a particular commodity for individuals, and local small entities, including community organizations, while acting with integrity.

54.2 Objectives:

- Define the manufacturing process.
- Describe the costing stages
- Classify the expenses according to their relationship with the production process.
- Explain the purpose of a Manufacturing Account
- Explain the treatment of opening and closing Work in Progress in Manufacturing Accounts
- Calculate the profit or loss on manufacturing
- Prepare Manufacturing Account, trading profit/loss account(Income Statement) and Balance Sheet for sole traders, partnerships and companies.

54.3 Definition of terms associated with manufacturing

*Manufacturin*g - Manufacturing is the process of converting raw materials into finished products.
Manufacturing accounts - is an account that collects together all cost involved in production to determine the production costs of goods completed.
Stocks /inventory for the manufacturing accounts – there are three types of stock in the manufacturing business :

- stock of raw materials -
- stock of work in progress
- stock of finished goods

Raw materials consumed – this the value of raw materials used up in the production process

54.4

54.5 The types of costs

Summarily, there are two types of costs in the manufacturing accounts namely,
Direct costs and indirect costs

- *Direct Costs* – these are costs that can be directly identified with each unit of production
- *Direct materials* (raw materials),
- *Direct labour* (e.g. wages paid to those working on machinery or assembly of products) and
- *Direct expenses* (direct expenses like carriage inwards on raw materials), implying (all those costs involved in production that are traceable to units of goods produced)
- The total direct costs incurred in a year is called Prime Cost
- *Indirect cost* – these are other costs that cannot be identified with each unit of production. Production overheads are all cost incurred in the factory but can't be easily traced to the units of goods produced.
- Prime costs are added to production overheads to give us the Production Cost.
- Raw materials (e.g. opening stock, purchases)
- *Finished goods* (refer to goods produced)

- *Work-In-Progress* (goods partly completed at the start of the of the accounting period is called opening work-in-progress and the one at the end of the accounting period is called closing work -in- progress)

Preparation of the manufacturing accounts Involves six key stages:

1) Computation of raw materials consumed
2) Ascertainment of prime cost
3) Allocation of overheads
4) Adjustment for work-in-progress
5) Calculation of total cost of production
6) Establishing the manufacturing profit/loss by comparing the cost of production with the market price.

55 Format for manufacturing account:

Manufacturing account for the year ended …

RAW MATERIALS CONSUMED:	KKK	KKK	KKK
Openings stock of raw materials		XXX	
Add: Purchases of raw materials	XXX		
Carriage on raw materials	XXX		
		XXX	
Total stock of raw materials available		XXX	
Less closing stock of raw materials		(XXX)	
Raw materials consumed		XXX	
ADD: DIRECT EXPENSES			
Direct labor	XXX		
Direct wages	XXX		
Royalties	XXX		
Lubricants for production equipment	XXX		
Total direct expenses		XXX	
PRIME COST			XXX
ADD FACTORY OVERHEADS		XXX	
Factory rent		XX	
Factory lighting and heating		XXX	
Factory power		XXX	
Depreciation of factory equipment		XXX	
Factory manager's salary		XX	
Insurance of factory building		XXX	
			XXX
WORK-IN-PROGRESS			
Opening stock of WIP		XX	
Less closing stock of WIP		(XX)	
			XXX
TOTAL COST OF PRODUCTION			XXX
MARKET VALUE OF GOODS			(XXX)
MANUFACTURING PROFIT/LOSS			-/+XXX

Question 1

Trial balance as at 31 December 2014

	Dr	Cr
	K	K
Stock of raw materials 01/01/2014	2,100	
Stock of finished goods 01/01/2014	3,890	
Work in progress	1,350	
Wages (direct K18,000;factory/indirect K14,500)	32,500	
Royalties	700	
Carriage inwards	350	
Purchases of raw materials	37,000	
Productive machinery (cost K28000)	23,000	
Office equipment (cost K2000)	1,200	
General factory expenses	3,100	
Lighting	750	
Factory Power	1,370	
Administrative salaries	4,400	
Salesman salaries	3,000	
Commission on sales	1,150	
Rent	1,200	
Insurance	420	
General administrative expenses	1,340	
Bank charges	230	
Discount allowed	480	
Carriage outwards	590	
Sales		100,000
Debtors and creditors	14,230	12,500
Bank	5,680	
Cash	150	
Drawings	2,000	
Capital 01/01/2014		29680
	142,180	142,180

Notes at 31st December 2014

a) Stock of raw materials K 2,400, stock of finished goods K4,000, work in progress K 1,500
b) Lighting, rent and insurance are to be apportioned: factory5/6, administration 1/6
c) Depreciation on productive and office equipment at 10% per annum on cost.

Required:

1) Prepare the manufacturing account
2) Trading profit and loss account for the year ended December 2014
3) The balance sheet as at 31st December 2014

Manufacturing, trading, profit and loss account
for the year ended 31st December 2014

Raw materials consumed	K	K	K
Opening stock of raw materials		2,100	
Purchases of raw materials	37,000		
Add: carriage inwards	350		
Net purchases of raw materials		37,350	
Raw materials available for the period		39,450	
Less: closing stock of raw materials		(2,400)	
Cost of raw materials consumed			37,050
Direct labour			18,000
Royalties			700
Prime cost			55,750
Factory Overheads Expenses			
General factory expenses		3,100	
Lighting 5/6		625	
Power		1,370	
Rent 5/6		1,000	
Insurance 5/6		350	
Depreciation of plant		2,800	
Indirect labour		14,500	
Total overheads			23,745
Factory cost of resources consumed			79,495
Add opening work in progress			1,350
			80,845
Less closing work in progress			(1,500)
Production cost of goods completed			79,345
sales			100,000
Opening stock of finished goods	3,890		
Add production cost of goods completed	79,345		
Total stock of goods available		83,235	
Less closing stock of finished goods		4,000	
Cost of goods sold			(79,235)
Gross profit			20,765
Less expenses			
Administration expenses			
Administrative salaries	4,400		
Rent 1/6	200		
Insurance 1/6	70		
General expenses	1,340		
Lighting 1/6	125		
Depreciation of accounting machine	200		
		6,335	
Selling and distribution expenses			
Salesmen salaries	3,000		
Commission on sales	1,150		
Carriage outwards	590		

		4,740	
Financial charges			
Bank charges	230		
Discount allowed	480		
		710	
			11,785
Net profit			8,980
Balance sheet as at 31 December 2010			
	K	K	K
Fixed assets	Cost	Dep.	N.B.V
Production machinery at coast	28,000	7,800	20,200
Accounting machinery at cost	2,000	1,000	1,000
	30,000	8,800	21,200
Current assets			
Stock-raw materials	2,400		
Stock- finished goods	4,000		
Work in progress	1,500		
Debtors	14,230		
Bank	5,680		
Cash	150		
		27,960	
Less current liabilities			
Creditors		(12,500)	
Working capital			15,460
Net assets			36,660
Financed by:			
Capital		29,680	
Add: net profit		8,980	
		38,660	
Less: drawings		2,000	
			36,660

Practice Question 2

The following information has been extracted from the books of major manufacturing company for the year to 30th September 2015:

Stock at 1st January 2015:	
Raw materials	7,000
Work in progress	5,000
Finished goods	6,900
Purchases of raw materials	38,000
Direct labour	28,000
Factory overheads:	
Variable	1,600
Fixed	9,000
Administrative expenses:	
Rent and rates	1,900
Heat and light	6,000
Stationary	2,000
Staff salaries	19,380
Sales	192,000
Plant and machinery:	
At cost	30,000
Provision for depreciation	12,000
Motor vehicles (for sales delivery)	
At cost	16,000
Provision for depreciation	4,000
Creditors	5,500
Debtors	28,000
Drawings	11,500
Balance at bank (Dr)	16,600
Capital at 1st January 2015	48,000
Provision for unrealised profit at 1st January 2015	1,380
Motor vehicle running costs	4,500

Additional information:

1) Stock at 31st December 2004, were as following:
   Raw materials..... K 9,000
   Work in progress.....K 8,000
   Finished goods .....K 10,350

The finished goods are transferred to the trading account at the factory cost plus 25% for factory profit. The finished goods stock is valued on the basis of amount transferred to the debit of the trading account.

2) Depreciation is provided annually at the following percentages of the original cost of fixed assets held at the end of each financial year.
   Plant and machinery..... 10%
   Motor vehicles..... 25%
3) Amount accrued due on 31st December 2004 for direct labour amounted to K3,000 and rent rates prepaid at 31st 2004 amounted to K 2,000

Required

Prepare the manufacturing, trading, profit and loss account for the year ended 31st December 2004, and the balance sheet as at that date.

Note: the prime cost and factory cost should be clearly shown.
solution

Manufacturing, trading profit and loss account
for the year ended 31st December 2004

Raw materials consumed:			
Opening stock	7,000		
Purchases	38,000		
Total stock available		45,000	
Less: closing stock		(9,000)	
Cost of raw materials consumed			36,000
Direct labour:			
Wages		28,000	
Add: wages accrued		3,000	
			31,000
Prime cost			67,000
Add: factory overheads:			
Variable		16,000	
Fixed		9,000	
Depreciation- plant and machinery		3,000	
			28,000
			95,000
Add: opening work in progress			5,000
			100,000
Less: closing work in progress			8,000
Factory cost of production			92,000
Market value			**115,000**
Less: factory cost			**92,000**
Manufacturing profit			**23,000**
Sales			192,000
Opening stock		6,900	
Market value		115,000	
Total stock available for sale		121,900	
Less: closing stock		(10,350)	
Cost of goods sold			(111,550)
Gross profit on trading			80,450
Add: profit on manufacturing			23,000
			103,450
Less: expenses:			
Rent and rates	19,000		
Less: prepayments	(2,000)		
		17,000	
Provision for unrealized profit (w1)		690	
Heat and light		6,000	
Stationery and postage		2,000	
Staff salaries		19,380	
Depreciation – motor vehicles		4,000	
Motor vehicle running costs		4,500	
Total expenses			(53,570)

Net profit	49,880

BALANCE SHEET AS AT 31ST DECEMBER 2004

	COST	DEP.	N.B.V
Fixed assets			
Plant and machinery	30,000	15,000	15,000
Motor vehicles	16,000	8,000	8,000
	46,000	23,000	23,000
Current assets			
Stock- raw materials		9,000	
Work in progress		8,000	
Finished goods	10,350		
Less: provision for unrealised profit	2,070		
		8,280	
Debtors		28,000	
Cash at bank		16,600	
Rent and rates prepaid		2,000	
		71,880	
Less: current liabilities			
Creditors	5,500		
Direct labour accrued	3,000		
		(8,500)	
Working capital			63,380
Net assets			86,380
Financed by:			
capital		48,000	
Add net profit		49,880	
		97,880	
Less drawings		(11,500)	
			86,380

Working s 1

Provision for unrealized profit account

Balance c/d	K 2,070	Balance b/d	K 1,380
		Profit and loss account	K 690
	K 2,070		K 2,070

56 ACCOUNTING ETHICS

Explain the ethics in accountancy?

Ethics – Ethics are the set of moral principles that guide a person behavior. The word ethics is commonly used interchangeably with morality and sometimes it is used to mean the moral principles of a particular tradition, group or individual.

Ethics in accountancy refers to a set of beliefs about what is right and wrong in the accountancy professional. There are a number of them to which professional accountants should comply with such as:

Integrity This is an important fundamental element of the accountancy profession. It imposes an obligation on all professional accountants to be straight forward and honest in professional and business relationship. Integrity also implies fair dealing and truthfulness. Accountants should avoid or restrict themselves from personal gain and intentional opportunity to deceive and manipulate financial information.

Trustworthy: trust is a fundamental relationship between client and the professional accountant. A trustworthy person is someone in whom you can place your trust and rest assured trust shall not be betrayed.

Discipline

These are impositions of obligations on an accountant to comply with relevant laws and regulations

Honest: Allows investors and other stakeholders to trust the information received.

Accountability – being answerable or taking responsibility for one's actions

Confidentiality - the accountant should not disclose any important information to third parties.

56.1 IDENTIFY EFFECTS OF NON ADHERENCE TO ETHICS

The following are the effects

- Corruption
- Fraud
- Money laundering
- Embezzlement
- Breach of confidentiality
- Betrayal of trust

56.2 Corruption

This is the abuse of entrusted power for private gain

56.3 Fraud

This is intentional manipulation of financial statement to create a positive picture to deceive people.

56.4 Money laundering

Process of making illegally earned money appear clean by carrying out certain cleansing activities

56.5 Embezzlement

Misappropriation of company funds by a person entrusted to be the custodian of funds.

56.6 Breach of confidentiality

The accountant gives confidential information to competitors.

Questions

Which of the following is one of the ethics in accounting?

a) Trustworthy
b) Double entry
c) Consistency
d) Realization

Which of the following is one of the effects of non-compliance to accountancy ethics

a) Embezzlement
b) Contra entry
c) Objectivity
d) Dual aspect

57 Explain the benefits to the company of adhering to ethics in accountancy [5]

57.1.1 Better Professional Environment

An accounting code of ethics that is enforced at public accounting firms or company accounting departments can ensure that individuals working with financial information act in the highest ethical manner possible. Accounting firms may review their code of ethics with potential employees to ensure that no misrepresentations are given regarding the expected ethical manner of employees during daily accounting functions. The code of ethics ensures that current employees understand the importance of acting ethically and that they respond to business scenarios with the proper mindset for maintaining high ethical standards.

57.1.2 Increased Reputation

Public accounting firms or companies using a standard accounting code of ethics may discover that they have a more positive reputation in the business environment than companies without a code of ethical conduct. Clients, consumers and other businesses tend to have a positive opinion of companies who act ethically and maintain a high level of professionalism when conducting

operations. Favorable reputations may allow companies to increase their market share and earn higher profits founded on positive consumer good will.

57.1.3 Standards for Employee Discipline

A code of ethics can allow companies to develop disciplinary practices for employees who violate the ethical standards when conducting daily accounting functions. Accounting managers and controllers may be able to address difficult employee situations by reviewing the accounting code of conduct and instructing the employee on how to correct his behavior. Managers may reiterate the specific expectations the employee must adhere to when working for the public accounting firm or company.

57.1.4 Decreased Legal Liability

Public accounting firms and private accountants often face increased legal liabilities when acting unethically. As seen in the accounting scandals of 2001, individual accountants were convicted of attempting to destroy unfavorable or inappropriate reports and communications with clients regarding accounting situations. These employees increased the legal liability of their company; the actions of a few employees severely impacted the lives and reputations of thousands of other accountants. Creating and following an accounting code of ethics can ensure companies and their employees decrease legal liability from inappropriate action.

58 INTERPRETATION TO FINAL ACCOUNTS

58.1 OBJECTIVES

a) Explain the importance of accounting ratios and percentages
b) Explain the various accounting ratios and percentages
c) Calculate various ratios/ percentages

58.2 Importance of Accounting Ratios /Percentages

- Both ratios and percentages are critical to help understand financial statements,
- Determining whether the business is moving in right direction and ascertain the business profitability
- For identifying trends overtime
- For measuring the overtime
- For measuring the overall financial state of the business.
- In addition, lenders and potential investors often rely on ratio analysis when lending and investing decisions.

58.3 Various Accounting Ratios

58.3.1 Return On Capital Invested (ROCE)

This is the percentage amount that a company is making for every percentage point over the cost of capital or is the percentage that a business makes over its investments capital.

58.3.2 Return on Capital Employed

This is the profitability ratio that measures how efficiently a company can generate profits from its company employed by comparing net operating profit to capital employed.

58.3.3 Acid Test Ratio

This is a measure of how well a business can meet its short term financial liabilities.

58.3.4 Liquidity Ration

This is an indicator of whether a company's current assets will be sufficient to meet the company's obligations when they become due.

58.3.5 Capital Employed

The total capital collected in a firm's fixed and current assets viewed from the funding side, it equals stock holders' funds (equity capital) plus long term liabilities (loan capital), viewed from the assets side, it equals fixed assets plus working assets.

58.3.6 Working Capital

This is the cash available for day to day operations of an organizations. It is also called current capital.

58.3.7 Creditors/ Purchases Ratio

Determines the rate at which a business pays off its creditors. It is sometimes called creditors turnover ratio

58.3.8 Debtors/ Sales Ratio

It is s the relationship between net sales and average debts. It is also called debtors turnover ratio.

58.3.9 Rate of Stock Turn or Turnover

Is stock metric that measures the rate at which the stock is used

58.3.10 Turnover

Is the number of times an asset (such as cash, stock, raw materials) is replaced or revolved during an accounting periods.

Calculate The Following Ratios

Gross profit percentage of sales	$= \frac{315,000}{555,000} \times \frac{100}{1} = 56.8\%$
Net profit as a percentage of sales	$= \frac{100,000}{555,000} \times \frac{100}{1} = 18\%$
Expenses as a percentage of sales	$= \frac{215,000}{555,000} \times \frac{100}{1} = 38.7\%$
Rate of stock return	$= \frac{240,000}{(100,000+60,000)/2} = 4.4$ Times

Average stock = $\frac{(\text{closing stock + opening})}{2}$	$(\frac{cost\ of\ goods\ sold}{average\ stock})$

Example

KIMS Trading Profit and Loss Account for The Year Ended 31,12,2012

Sales		**555,000**	
Opening stock	100,000		
Add: purchase	200,000		
Total goods available	300,000		
Less: closing stock	60,000		
Cost of sales		240,000	
Gross profit		315,000	
Less: expenses			
Depreciation	5,000		
Wages, salaries & commissions	105,000		
Other expenses	45,000		
		215,000	
Net profit			100,000

KIMS balance sheet at that date

Fixed Assets	**Cost**	**Dep**	**NBV**
Equipment	50,000	40,000	10,000
Current assets			
Closing stock		60,000	
debtors		125,000	
Bank		25,000	
		210,000	
Less: Current Liabilities			
Creditor		(104,000)	
Working capital			106,000
Net assets			116,000
Financed By:			
Capital		76,000	
Net profit		100,000	
		176,000	
Less: Drawings		80,000	
Capital owned			9,600
Add: Long Term Liabilities			
Loan			20,000
Capital employed			116,000

Rate of Return On Capital Employed I.E. $\frac{net\ profit}{capital\ employed} \div \frac{100}{1}$	$= \frac{100,\ 000\ x\ 100}{(76,000+96,000)} \div 2 = 104.2\ \%$
Current Ratio **I.E.** $\frac{current\ assets}{current\ liabilities}$	$= \frac{210,000}{104,000} = 2.02$

Acid Test Ratio $= \frac{current\ assets - closing\ stock}{current\ liabilities}$	$= \frac{210{,}000 - 60{,}000}{104{,}000} = 1.4$
Debtor / Sales Ratio $= \frac{debtors\ x\ 12\ moths}{sales}$	$= \frac{125{,}000}{555{,}000} = 2.7$ months
Creditors / Purchases Ratio $= \frac{creditors\ x\ 12\ months}{purchases}$	$= \frac{104{,}000\ x\ 12\ months}{200{,}000} = 6.24$ months