CAF-1

INTRODUCTION TO ACCOUNTING

PRACTICE MANUAL
EXAMINATION QUESTIONS AND ANSWERS

BOOK CONTAINS TRANSLATION OF QURANIC AYATS AND AHADITHS, THEREFORE HANDLE CAREFULLY.

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Types of Cheque

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Bearer Cheque:

(i) Suppose accountant of the business writes a bearer cheque of MCB Bank and gives it to Ali.
(ii) Ali will go to MCB Bank to get cash.
(iii) Ali will give the cheque to the Bank Cashter.
(iv) Cashier will verify the balance in the account of the business..
(v) If balance exists Cashier will give the cash to Ali.

Crossed Cheque:

(i) Suppose accountant of the business writes a crossed cheque of MCB Bank and gives it to Ali.
(ii) Ali will go to the Bank where his own account exists (suppose in HBL).
(iii) Ali will deposit the cheque in his account in HBL.
(iv) HBL will send the cheque to MCB for balance verification.
(v) MCB will verify the balance and sent the cash to HBL if cash balance exists in account of the business.
(vi) HBL will transfer the amount to Ali's Account.
(vii) If suppose Ali wants cash he will write a cheque of his own A/c.

For the purpose of security of payment generally payments are made by crossed cheque.

Transactions of Business with Bank:

	Honda Ltd.	Meezan Bank
(i)	**Business deposited Rs. 50,000 Cash into Bank:** Mezan Bank 50,000 Cash 50,000	Cash 50,000 Honda Ltd. 50,000
(ii)	**Business withdrawn Rs. 10,000 from Bank:** Cash 10,000 Meezan Bank 10,000	Honda Ltd. 10,000 Cash 10,000
(iii)	**Crossed cheque received from a customer Rs. 500,000 (Name of customer is Hassan). Assume Hassan has account in Meezan Bank** Meezan Bank 500,000 Debtor - Hassan 500,000 (At the time of receipt of cheque)	Hassan A/c 500,000 Honda Ltd. 500,000 (At the time of clearance of cheque)
(iv)	**Crossed cheque given to supplier (Zeshan) Rs. 100,000. Assume Zeeshan has A/c in Meezan Bank** Creditor - Zeshan 100,000 Meezan Bank 100,000 (At the time of issuance of cheque)	Honda Ltd. 100,000 Zeeshan A/c 100,000 (At the time of clearance of cheque)
(v)	**Bank charges deducted debited by bank Rs. 500** Bank charges 500 Meezan Bank 500	Honda Ltd. 500 Bank Service Income 500
(vi)	**Interest income credited by bank Rs. 1,000** Meezan Bank 1,000 Interest Income 1,000	Interest Expense 1,000 Honda Ltd. 1,000

Ledger of Meezan Bank (prepared by Honda Limited)

Cash	50,000	Cash	10,000
Debtor – Hassan	500,000	Creditor – Zeeshan	100,000
Interest Income	1,000	Bank charges	500
		Balance c/d	440,500
	551,000		551,000

***Ledger of Honda Ltd. (prepared by Meezan Bank)**

Cash	10,000	Cash	50,000
Zeeshan A/c	100,000	Hassan A/c	500,000
Bank Service Income	500	Interest Expense	1,000
Balance c/d	440,500		
	551,000		551,000

***the ledger of customer prepared by bank is called as bank statement or pass book.**

Conclusion:

If all transactions are correctly recorded by both the bank and business in the same accounting period, then balance as per bank account (prepared by business) and balance as per bank statement (prepared by bank) should be equal but opposite in name.

Points to remember:

- Ledger prepared by business related to its bank is called as bank account or cash book (bank column).
- Ledger prepared by bank related to its customer is called as bank statement / pass book.

CASH BOOK

	CASH	BANK		CASH	BANK

Bank Reconciliation Statement:

If there is a difference between bank account and bank statement, then a separate page (a statement) is also prepared by business in addition to bank account to explain the reasons of difference.

Reasons of Differences between Cash Book (Bank Column) & Bank Statement

1. Items in bank statement not yet recorded in bank account e.g.
   Bank Charges debited by bank.
   Bank interest credited by bank
   Accounting Treatment:
   These items are recorded in bank Account (cash book (bank column))

2. Items in cash book (bank column) not yet recorded in bank statement.e.g.
   (i) Un-presented Cheques/outstanding cheques:
   Cheques issued and credited in bank A/c but not yet debited in bank statement.
   Cheque issued on 29-12-2014
   Bank statement date is = 31-12-2014
   Cheque cleared on 2-1-2015
   (ii) Un-credited Cheques:
   Cheques received and debited in bank account but not yet credited in bank statement.
   Accounting Treatment:
   These cheques are written in Bank reconciliation statement until recorded by bank in bank statement.

3. Errors in Cash Book: (Bank Column)
   Accounting Treatment:
   These errors are corrected in cash book (Bank column)

4. Errors in Bank Statement:
   Accounting Treatment:
   These errors are temporarily corrected in Bank reconciliation statement until corrected by bank.

Q. 1 Prepare a bank reconciliation statement as at 30th September,2001 from the following entries in the Bank column of the Cash book and corresponding Passbook.

Cash book (Bank Column Only)

2001		Rs.	2001		Rs.
Sep,1	b/d	8,000	Sep,4	Drawings	700
Sep,3	Raja Kamran	2,200	Sep,8	Suleman	3,300
Sep,9	Rashid	1,500	Sep,12	Salary	2,800
Sep,16	Rao Nadir	3,400	Sep,16	Saleem	1,700
Sep,23	Rahim	2,600	Sep,18	Surtaj	4,200
Sep,27	Rauf	100	Sep,21	Sawan	2,000
Sep,30	Rao Nisar Umar	350	Sep,26	Sarwar	1,100
			Sep,30	Commission	100
			Sep,30	c/d	2,250
		18,150			**18,150**

Bank Pass Book

2001	Particulars	Debit	Credit	Balance(Cr.)
Sep,1	b/d			8,000
Sep,4	Cheque-Drawings	700		7,300
Sep,9	Cheque-Raja Kamran		2,200	9,500
Sep,11	Cheque-Suleman	3,300		6,200
Sep,12	Cheque-Rashid		1,500	7,700
Sep,17	Cheque-Salary	2,800		4,900
Sep,20	Cheque-Saleem	1,700		3,200
Sep,30	Cheque-Rahim		2,600	5,800
	Cheque-dividend		900	6,700
	Bank charges	15		6,685
	Electricity Bill	60		6,625
	Cheque Comission	100		6,525

Note: unadjusted debit balance is written on the debit side of respective ledgers while unadjusted credit balance is written on credit side of respective ledger.

Q. 2 In preparing its bank reconciliation at June30, 2001 Carefull company has made available the following data:

i.	Balance as per bank statement June 30, 2001	38,025
ii.	Deposit in transit June 30, 2001	5,200
iii.	Outstanding cheques June 30, 2001	6,750
iv.	Amount erroneously credited by bank to Carefull's account June 28, 2001	400
v.	Bank service charges for June	75

Required:

Workout Care full Company's adjusted balance as per cash book at June30, 2001 by preparing a BRS.

Note: if nothing is mentioned then assume that the balance as per bank statement is credit balance while balance as per cash book is a debit balance.

Deposits in transit is an other name of uncredited cheques while outstanding cheques is an other name of unpresented cheques

Dishonoured Cheques:

A cheque that is not cleared and therefore balance is not transferred.

If Cheque Received is dishonoured:			**If the cheque issued is dishonoured:**		
Bank	100,000		Creditor	50,000	
Debtor		100,000	Bank		50,000
Debtor	100,000		Bank	50,000	
Bank		100,000	Creditor		50,000
(Dishonoured cheque)			(Dishonoured cheque)		

Pay-Order/Demand Draft:

Pay-order is just like a crossed cheque but it is not dishonoured because it is prepared by bank after receiving the amount to be paid against it.

Q. 3 On December31,2001 the bank column of Salims cash book showed a debit balance of Rs.4,610. On examination of the cash book and bank statement you find that:

1) Cheques amounting to Rs.6,300 which were issued to the creditors and entered in the cash book before December 31,2001 were not presented for payment until after that date.
2) Cheques amounting to Rs.2,500 had been recorded in the cash book as having been paid into the bank on December 31,2001 but were entered in the bank statement on January1,2002.
3) A cheque for Rs.730 had been dishonoured prior to December31, 2001, but no record of this fact appeared in the cash book.
4) A Dividend of Rs.380 received direct into the Bank had not been recorded in the Cash book.
5) Bank intrest and charges amounting to Rs.420 had been charged in the bank statement but not charged in the cash book.
6) No entry had been made in the cash book for a trade Subscription of Rs.100 paid by pay-order in November 2001.
7) A cheque book for Rs.10 had been entered in the cash book twice.
8) A cheque for Rs.270 drawn by Salam had been charged to Salim's bank account in the error by bank in December 2001.

You are Required :

a) To make appropriate adjustments in the cash book to find the adjusted balance and
b) To prepare a statement reconciling the adjusted balance in the cash book with the balance shown in the bank statement.

Normally:

Balance in Cash Book	**Balance in Bank Statement**
Dr.	Cr.
Exception is Overdrawn Balances (when business has taken extra funds from bank)	
Cr.	Dr.

Example when Bank Account has overdrawn balance (overdrawn balance is also called as overdraft balance):

b/d	50,000	Creditor	700,000
Debtors	500,000		
c/d	150,000		
	700,000		700,000

Casting: (Total)

Under casting **Over casting**

A bank account has two sides:

- Debit side – also called as receipt side
- Credit side – also called as payment side

Q. 4 According to M's cash book, there was a balance of Rs. 3,000 overdrawn in 30th June 2016, in his No.1 bank Account.

On Investigation you find:

(i) Cheques drawn amounting to Rs. 5,000 had not been presented.
(ii) Cheques Rs. 2,500 entered in the cash book as paid into bank, had not yet been cleared.
(iii) A cheque for Rs. 1,200 drawn on his No. 1 account has been charged by the bank to his No. 2 account
(iv) The payment side of the cash book has been under cast by Rs. 700
(v) A Dividend Rs. 400 paid direct to the bank had not been recorded in the cash book
(vi) Bank charges of Rs. 300 entered in to the bank statement had not been entered in the cash book
(vii) A cheque of Rs. 500 paid into the bank had been dishonored and
(viii) Bank charges of Rs. 10 entered in to the bank statement had not been entered in the cash book

Required :

a) Show the appropriate adjustments to be made In the cash book, and
b) Prepare a bank reconciliation statement for the No. 1 account as on 30.06.2016

Q. 5 In the books of T Co the bank account shows a balance overdrawn of 6,530 as at 31 December 2018. On comparing the bank statements with the cash book the following items are discovered:

1. Bank charges of 100 and overdraft interest of 50 have been omitted.
2. Cheques received from customers totaling 1,900 have not yet been cleared by the bank.
3. Cheques drawn in favor of suppliers amounting to 2,300 are outstanding at the year end.
4. A credit transfer from a customer of 2,000 was not recorded in cash book.
5. A direct debit to a supplier of 1,000 was omitted in cash book.

A) What figure will be shown in the balance sheet as at 31 December 2018 for 'bank overdraft1?
   - a) 5,480
   - b) 5,680
   - c) 6,130
   - d) 7,380

B) Assuming that the above items are all that is required to reconcile the cash book balance to the balance per the bank statement, what balance did the bank statement show as at 31 December 2018?
   - a) 5,280 overdrawn
   - b) 6,080 overdrawn
   - c) 7,780 overdrawn
   - d) 8,580 overdrawn

Q.6 Summary of the cash book of Rectify Co for the year to 31 May 2015 is as follows:

Cash Book

Opening balance b/d	805	Payments	146,203
Receipts	145,720	Closing balance c/d	322
	146,525		146,525

After some investigation of the cash book and vouchers you discover that:

1) bank charges of 143 shown on the bank statement have not yet been entered in the cash book;
2) a cheque drawn for 98 has been entered in the cash book as 89, and another drawn at 230 has been entered as a receipt
3) a cheque received from a customer for 180 has been returned by the bank marked refer to drawer', but it has not yet been written back in the cash book;
4) an error of transposition has occurred in that the opening balance of the cash book should have been brought down at 850;
5) cheques paid to suppliers totaling 630 have not yet been presented at the bank, whilst payments in to the bank of 580 on 31 May 20X5 have not yet been credited to the company's account;
6) a cheque for 82 has been debited to the company's account in error by the bank;
7) standing orders appearing on the bank statement have not yet been entered in the cash book:
   a. interest for the half year to 31 March on a loan of 20,000 at 11% pa;
   b. Lease repayments on the managing director's car -12 months at 55 per month;
   c. Dividend received on a trade investment - 1,147
8) a page of the receipts side of the cash book has been under cast by 200;
9) The bank statement show a bank overdraft of 870

Required: Prepare a bank reconciliation statement as on 31 May 2015. Also prepare an adjusted cash book

Note: standing order means instructions to bank to make specified payments at specified fixed dates.
Error of transposition means figures are misplaced.
Time barred cheque means a cheque which is more than 6 months old.

Q.7:

On 30 June 2015, the bank book of Ranjah Enterprises (RE) reflected a credit balance of Rs. 3,450,000 whereas the bank statement showed an overdraft of Rs. 2,415,000. On scrutinizing the record, following issues were discovered:

(i) Cheques deposited in bank in the last week of June 2015, amounting to Rs. 1,550,000 were wrongly credited in the bank book. Out of these, cheques amounting to Rs. 1,050,000 were cleared by the bank in July 2015 whereas a cheque of Rs. 500,000 deposited on 29 June 2015 was dishonoured by the bank.

(ii) Financial charges on bank overdraft amounting to Rs. 750,000 were recorded in the bank statement. However, review by the Accounts Officer indicated an error and RE recorded the correct amount of Rs. 510,000 in the bank book. The error was corrected by the bank on 10 July 2015.

(iii) A cheque issued to a supplier amounting to Rs. 4,005,000 was entered in the bank book as Rs. 4,050,000. However, the bank erroneously recorded the amount as Rs. 4,500,000.

(iv) A supplier was issued a cheque of Rs. 125,000 in place of a time barred cheque on 25 June 2015 and was cleared on the next day. However, the cancellation of time barred cheque was not recorded by RE.

(v) A payment of Rs. 50,000 through cheque was recorded twice in the bank book.

Required:

Determine the correct balance that should be reported in the bank book and prepare a statement reconciling the corrected balance with that shown in the bank statement. **(09)**

Q.8 The Cash Book and Bank Statement of Neha International appeared as follows:

Cash Book (Bank column only)

		Amount in Rupees		
Date	**Particulars**	**Dr.**	**Cr.**	**Balance**
01.06.05	Balance b/d	78,000		78,000
04.06.05	Sami Imports		12,000	66,000
05.06.05	Asim Packaging	15,000		81,000
08.06.05	Deen Exports	18,000		99,000
10.06.05	Roohi Exports		30,000	69,000
15.06.05	Samar International	19,500		88,500
16.06.05	Hina Imports		7,500	81,000
27.06.05	Channa Exports	16,500		97,500

Bank Statement - Details

		Amount in Rupees		
Date	**Particulars**	**Dr.**	**Cr.**	**Balance**
01.06.05	Balance b/d		82,500	82,500
02.06.05	Kamal		3,000	85,500
03.06.05	Suman		15,000	100,500
05.06.05	Asim Packaging		15,000	115,500
08.06.05	Sami Imports	12,000		103,500
08.06.05	Deen Exports		18,000	121,500
09.06.05	Beeta	9,000		112,500
17.06.05	Profit on Certificates of investment		75,000	187,500
18.06.05	Samar International		19,500	207,000
27.06.05	Bank charges	3,000		204,000

The bank reconciliation for the month of May 2005 is as follows:

Bank Reconciliation Statement As at May 31, 2005

	Rs.	
Balance as per cash book		78,000
Add: Cheques issued but not presented		
J.B.&Co.	7,500	
Flash & Co.	6,000	
Beeta	9.000	22,500
		100,500
Less: Cheques deposited but not cleared		
Suman	15,000	
Kamal	3,000	18,000
Favorable balance as per bank statement		82,500

Required:

Bank reconciliation statement as at June 30,2005. Also prepare an adjusted cash book

Q. 9 According to cash book there was a balance of Rs30,000 overdrawn on 30th June,2013 in his bank.

On investigation you find that:

a) Cheques Drawn Amounting to Rs.50,000 had not been presented.
b) Cheques of Rs.25,000 entered in cash book as paid into bank, had not been cleared.
c) A Cheque of Rs.12,000 drawn by the company had been charged by the bank to another account.
d) A cheque of Rs.7,000 issued by the business has not been recorded in cash book.
e) A dividend of Rs.4,000 paid direct to the bank had not been recorded in cash book.
f) Bank charges of Rs.3,000 entered in Bank statement had not been entered in cash book.
g) A dishonor cheque of Rs.5,000 has not been recorded in cash book.
h) A cheque book of Rs. 100 has not been entered in cash book.

Required

Prepare bank reconciliation statement as on 30th June, 2013 and pass journal entries for the transaction to be recorded in cash book.

Note: if accounting entries are required in a question of BRS then prepare entries of items appearing in cash book only.

Q. 10 The bank book for the month of February 2013 of Abid Ali & Brothers is as follows:

Bank Book

Date		Rupees	Date		Cheque	Rupees
01-02-13	Opening Balance	991				
05-02-13	Ayaz	2,386	04-02-13	Kashif Ltd.	184	3,120
05-02-13	Ayub	3,009	07-02-13	Qasim & Sons	185	4,092
			10-02-13	Babar	186	918
13-02-13	Zahid Ltd.	15,414	12-02-13	Supei Ltd - DD		565
21-02-13	Zubair Merchant	12,221	17-02-13	Mateen	187	2,441
27-02-13	Athar	2,055	18-02-13	Mazhar	188	4,588
			23-02-13	Tabish Ltd. - SO		1,229
			24-02-13	Salaries		4,771
			25-02-13	Ilyas	189	947
			26-02-13	Akbar	190	1,652
			28-02-13	Closing balance		11,753
		36,076				36,076

The Bank Statement for February 2013 appears as follows:

Date	Description	Debit	Credit	Balance
01-02-13	Balance			3,633
01-02-13	Cheque 182	440		3,193
01-02-13	Cheque 181	2,202		991
03-02-13	Cash deposit		2,386	3,377
03-02-13	Cash deposit		3,009	6,386
06-02-13	Cheque 184	1,320		5,066
09-02-13	DD – Waqas	551		4,515
12-02-13	DD - Super Ltd.	565		3,950
13-02-13	Clearing		15,414	19,364
19-02-13	Cheque 185	4,092		15,272
20-02-13	Cheque 187	2,414		12,858
21-02-13	Clearing		12,122	24,980
23-02-13	Tabish Ltd. - Standing Order	1,229		23,751
24-02-13	Salaries transfer	4,771		18,980
26-02-13	Yasir - Standing Order	918		18,062
27-02-13	Cheque 188	5,488		12,574
28-02-13	Bank Charges	459		12,115

The bank reconciliation for the month of Jan 2013 is as follows:

Bank Reconciliation Statement As at January 31, 2013

	Rs.	
Balance as per bank statement		3,633 Cr
Cheques issued but not presented		
182	440	
181	2,202	2,642 Dr
Balance as per cash book		991 Dr

Required:

A bank reconciliation statement for Abid Ali & Brothers as at 28 February 2013 after incorporating necessary entries/corrections in the bank book. ***All amounts appearing in the bank statement are correct.*** **(13)**

Q. 11 Following information has been extracted from the records of Eden Garments (EG), as at 30 June 2016:

	Rupees
Balance as per bank book (debit balance)	760,000
Balance as per bank statement (overdraft)	1,490,850

An examination of the bank book and the bank statement, revealed the following:

(i) Outstanding cheques amount to Rs. 3,856,000 and include:
- a cheque of Rs. 50,000 issued to a supplier bearing an incorrect payee's name. The cheque was returned and recorded on 15 July 2016.
- a cheque issued to a supplier for Rs. 85,000 was recorded in bank book as Rs. 58,000.
- a cheque dated 20 December 2015 for Rs. 4,630 issued for repair of a car was misplaced. The repair charges were paid in cash and the misplacement of the cheque was not recorded.

(ii) Un-cleared cheques amount to Rs. 6,460,000 and include:
- a cheque of Rs. 366,000 received from a customer was returned by the bank as amount in words was not in conformity with the amount in figures. The return was not recorded and the cheque was sent to the customer for replacement.
- a cheque of Rs. 76,000 received from a customer in settlement of an invoice availing payment discount of 5%. The collection was recorded by EG at gross amount of invoice.

(iii) An unidentified credit of Rs. 354,000 was appearing in the bank statement. It was found that a customer had made an online transfer to avail 5% discount allowed on payments made by 30 June 2016.

(iv) Following debit/credit advices dated 30 June 2016 were received from the bank on 5 July 2016:
- Bank charges amounting to Rs. 7,850. It has been noted that the bank had over charged EG by Rs. 1,250.
- Dividend collected by the bank amounting to Rs. 50,000.
- Payment on EG's standing instruction of an annual subscription for a magazine amounting to Rs. 12,000.

Required:

(A) Post relevant transactions to bank book of EG to arrive at the correct bank balance as at 30 June 2016. **(07)**

(B) Prepare a bank reconciliation statement for the month of June 2016 to arrive at the adjusted bank balance as per EG's books. **(03)**

Q. 12

Mr. Ahmed is a sole trader and carries on business under the name "Ahmed & Company". The balance on his cash book at 31 December 2011 did not agree with the balance as per the bank statement which shows a credit balance of Rs. 367,500.

An examination of the cash book and bank statement disclosed the following:

(i) A deposit of Rs. 49,200 made on 29 December 2011 had been credited by the bank on 1 January 2012.

(ii) Bank charges of Rs. 1,700 have not been entered in the cash book.

(iii) A cheque of Rs. 4,200 received from a customer had been returned from bank marked 'out of date'. The cheque was re-dated by his customer and paid into the bank again on 3 January 2012. The return of cheque has not been recorded.

(iv) A standing order for payment of an annual subscription amounting to Rs. 1,000 has not been entered in the cash book.

(v) On 26 December 2011, Mr. Ahmed had given the cashier a cheque for Rs. 10,000 to pay into his personal account at the bank. The cashier deposited it into the business account by mistake. The cheque was credited by bank on 27.12.2011.

(vi) On 27 December 2011, a customer had made an online transfer of Rs. 49,900 in payment against goods supplied. The advice was received and recorded in the cash book on 2 January 2012.

(vii) On 30 September 2011, Mr. Ahmed entered into a hire purchase agreement and issued a standing order to the bank to pay a sum of Rs. 2,600 on the 10th day of each month, commencing from October 2011. No entries have been made in the cash book for these payments,

(viii) A cheque for Rs. 36,400 received from Mr. Bashir had been entered twice in the cash book,

(ix) Cheques issued amounting to Rs. 467,200 had not been presented to the bank for payment until after 31 December 2011.

(x) A customer who owed Rs. 20,000 and was entitled to a cash discount of 2½% paid a cheque for the net amount on 10 December 2011. The cashier erroneously recorded the gross amount in the bank column of the cash book.

(xi) Dividend collected by the bank amounting to Rs. 12,000 has not been recorded in the cash book.
(xii) A cheque of Rs. 243,000 received from Mr. Bilal was deposited in the bank but entered in the cash book as Rs. 234,000.

Required:

(a) Prepare a bank reconciliation statement as on 31 December 2011.
(b) Prepare necessary journal entries in the books of Ahmed & Company and determine the correct cash balance that should be reported in the balance sheet. Also specify the situations in which no adjustment/entry is required. ***(13 marks)***

Q. 13 The following bank reconciliation statement pertains to Comforts Travels for the month of February 2017:

	Rupees
Balance as per bank statement	3,258,000
Outstanding cheques	(869,200)
Cheques deposited and under clearance	456,350
Debit advices for bank charges received in March 2017	9,240
Un-reconciled difference	(9,000)
Balance as per bank book	2,845,390

Scrutiny of the bank book and bank statements revealed the following:

(i) Outstanding cheques include:
- a cheque of Rs. 37,250. The cheque was recorded in the bank book as Rs. 32,750. A cheque amounting to Rs. 9,650 which is outstanding since 8 June 2016. Cheques outstanding for more than six months are not honoured by the bank.

(ii) Cheques under clearance include a post-dated cheque of Rs. 35,000 received from a customer on 27 February 2017. The cheque was deposited in the bank on 28 February 2017. The date of the cheque was 1 March 2017.

(iii) The bank charges include an amount of Rs. 2,500 which was subsequently reversed by the bank.

(iv) Un reconciled difference in above bank reconciliation statement represents a page total of payment side of the bank book amounting to Rs. 4,589,000 was carried forward to the next page as Rs. 4,598,000.

(v) The debit side of the bank book is under casted by Rs. 4,500.

Required:
- Post relevant transactions to the bank book to arrive at the correct balance as at 28 February 2017.
- Prepare a revised bank reconciliation statement for the month of February 2017 using the corrected bank book balance.

Concept of post-dated cheque.

<u>Q.14</u>

The newly appointed accountant of Fine Works Limited has prepared the following bank reconciliation statement for the month of December 2013:

Description			**Rupees**
Balance as per bank statement as at 31 December 2013			1,721,490
Outstanding cheques:			
Cheque No.	**Date**	**Rupees**	
620	25-Jun-2013	35,000	
765	15-Dec-2013	435,630	
789	28-Dec-2013	635,700	
795	20-Jan-2014	325,690	
			(1,432,020)
Cheques deposited still under clearance			535,635
Unidentified credit appearing in the bank statement			(190,000)
Balance as per bank book as at 31 December 2013			635,105

On reviewing the bank book and the bank statement, the following information has been obtained:

(i) The correct amount of outstanding cheque no. 765 appearing in above BRS is Rs. 453,630. However, the amount is correctly recorded in the cash book.
(ii) The unidentified credit is for cash deposited directly into the bank by a customer to avail agreed 5% discount on payment within one week.

(iii) A bank debit advice dated 31 December 2013 for bank charges amounting to Rs. 6,570 for the month of December 2013 was received on 3 January 2014 and recorded in the bank book in January 2014.

(iv) The debit side total of the bank book has been overcast by Rs. 11,430.

(v) Cheques outstanding for more than six months are not honoured by the bank.

Required:

(a) Prepare necessary accounting entries for the month of December 2013. **(06)**

(b) Prepare a revised bank reconciliation statement. **(04)**

Question -15

Ex Zed & Co. maintains their Current account and PLS Account with Aggressive Bank Ltd. Bank has instructions to credit all the remittances received in name of company only in Current Deposit Account. The Statement of Account sent by the bank for the period 1st January, 1990 to 31st January, 1990 showed the following balances:

	Rupees
(i) CD Account (Overdraft)	11,503
(ii) PLS Account	263,508

The balances shown by the bank did not tally with the balances shown by the books of the company which were as under:-

	Rupees
(i) CD Account	6,594
(ii) PLS Account	236,253

On scrutiny following discrepancies were noted by the Accountant;

(a) IN THE BOOKS OF COMPANY:

(i) A cheque for Rs. 5,667 issued from CD Account was recorded in PLS Account.

(ii) A sum of Rs. 25,000 deposited in PLS Account was recorded in CD Account.

(iii) Bank's Godown-keeper's salary of Rs. 750 charged to CD Account by the bank remained unrecorded.

(iv) Cheque for Rs. 8,563 deposited in the CD Account was dishonoured and returned to the company in February, 1990.

(v) Three cheques for Rs. 8,993, Rs. 5,445 and Rs. 11,633 issued from CD Account by the company remained unpaid.

(vi) A letter sent to the bank to transfer a sum of Rs. 25,000 from PLS Account to CD Account remained unrecorded.

(vii) A cheque for Rs. 15,600 issued in name of Best Furnishers from CD Account against purchase of furniture was cancelled in January but the necessary entry was not made in the books.

(b) IN THE BOOKS OF BANK:

(i) Profit of Rs. 11,577 on PLS Account was credited to CD Account.

(ii) Miscellaneous charges of Rs. 335 were charged to PLS Account instead of CD Account

(iii) Remittance of Rs. 33,500 was credited to PLS Account, instead of CD Account

(iv) A cheque of Rs. 23,200 was credited by bank on Feb 2, 1990. This amount was recorded in the books of company on 29th January , when the cheque is received.

You are required to:

(i) Pass the Journal entries in the books of the company wherever necessary.

(ii) Compute the correct balances as per books of the company on 31st January, 1990.

(iii) Prepare bank reconciliation statement of both the banks. **(20)**

(May 1990, C.A Inter-1}

Q.16 The bank statement of AB Traders showed an overdraft of Rs. 272,000 as at June 30, 2006. The bank book showed an overdraft of Rs. 730,718. An examination of the bank book and bank statement disclosed the following:

(i) A cheque of Rs. 49,200 deposited on June 29, 2006 had been credited by the bank on July 1, 2006.

(ii) Bank charges amounting to Rs. 1,700 had not been entered in the bank book.

(iii) A cheque of Rs. 4,200 received from a customer had been returned by bank marked ' out of date'. The cheque had been re-dated by the customer and deposited into the bank again on July 3, 2006. The return of cheque has not been recorded in the books of comapny

(iv) A payment under a standing order, for annual subscription amounting to Rs. 1,000 had not been entered in the bank book.

(v) On June 25, the Managing Director had given the cashier a personal cheque of Rs. 10,000 for depositing into his personal account at the bank. The cashier had deposited it into the company's account by mistake. It was credited in the bank statement on June 27.

(vi) On June 27, two customers of AB Traders had paid direct in the company's bank account Rs. 49,900 and Rs. 15,700 respectively as payment against goods supplied. The advices were not received by the company until July 4 and were entered in the bank book on that date.

(vii) On March 30, 2006 the company had entered into a lease agreement to pay by banker's order a sum of Rs. 2,600 on the 10th day of each month commencing April, 2006. No entries had been made in the bank book.

(viii) Rs. 36,400 deposited into the bank had been entered twice in the bank book.

(ix) Cheques issued amounting to Rs. 467,200 had not been presented to the bank for payment until after June 30, 2006.

(x) A customer was given a cash discount of 2.50% on payment of Rs. 20,000 on June 10. The cashier entered the gross amount in the bank book.

(xi) The bank sent a debit advice of Rs. 16,718 being interest on overdraft for 6 months to June 30, 2006. It had been entered in the bank book twice.

Required: Show necessary adjustments in the bank book and prepare a bank reconciliation statement as on June 30, 2006.

Concept of three column cash book

Q. 17 While reconciling the bank statement with the cash/bank book of ABC Textiles for the year ended December 31, 2009, you noted the following:

		Rupees
(i)	Balance as per bank statement at December 31, 2009 overdrawn	806,436
(ii)	Cheques drawn but not presented till December 31, 2009	377,784
(iii)	Mark-up on overdraft charged by the bank on January 2, 2010 was wrongly recorded in the cash/bank book on December 31, 2009	118,686
(iv)	Collections made on December 30 and 31, 2009 were not cleared with the bank till January 3, 2010	250,600
(v)	A cheque which was due on December 29, 2009 was sent to the bank for collection on December 28, 2009, and entered in the cash/bank book (However, the proceeds were credited by the bank on January 1, 2010)	196,500
(vi)	Subscription for a magazine was paid by the bank, as per the auto-debit instructions, on December 1, 2009. This transaction has not been recorded in the cash/bank book so far	3,144
(vii)	A time-barred cheque was replaced with a new cheque on December 30, 2009 and entered in the cash/bank book without the previous cheque being cancelled / reversed. Both the cheques are included in (ii) above	5,000
(viii)	Discount allowed on prompt payment has been included in the bank column of cash book.	10,500
(ix)	A cheque received on December 21 was erroneously recorded on the credit side of the cash/bank book	7,500
(x)	A cheque for Rs.125,000 drawn by the company to pay for a new item of plant had been mistakenly entered in the cash/bank book as	12,500
(xi)	A cheque issued by the company has been entered in the credit column of the bank statement	13,200

Required: Prepare a bank reconciliation statement as at December 31, 2009 and identify the amount to be carried to the balance sheet as "Cash at Bank". Also prepare an adjusted cash book **(09)**

Time barred cheque: means a cheque which is more than six months old.

Q. 18 test question

Following information has been extracted from the records of Eden Garments (EG), as at 30 June 2016:

	Rupees
Balance as per bank book (debit balance)	800,000

An examination of the bank book and the bank statement, revealed the following:

(i) Outstanding cheques amount to Rs. 3,856,000 and include:

- a cheque of Rs. 50,000 issued to a supplier bearing an incorrect payee's name. The cheque was returned but not recorded.
- a cheque issued to a supplier for Rs. 93,000 was recorded in bank book as Rs. 39,000.
- a cheque dated 20 December 2015 for Rs. 35,000 issued for repair of a car is now time barred. The replaced cheque was issued on 25 June 2016 and recorded, however the reversal of time barred cheque was not recorded. Both cheques are included in outstanding cheques.

(ii) Un-cleared cheques amount to Rs. 6,460,000 and include:

- a cheque of Rs. 375,600 received from a customer was returned by the bank marked NSF.
- a cheque of Rs. 94,080 received from a customer in settlement of an invoice availing payment discount of 2%. The collection was recorded by EG at gross amount of invoice.

(iii) An unidentified credit of Rs. 150,000 was appearing in the bank statement. It was found that a customer had made an online transfer to avail 3% discount allowed on payments made by 30 June 2016.

(iv) Following debit/credit advices dated 30 June 2016 were received from the bank on 5 July 2016:

- Bank charges amounting to Rs. 16,000. It has been noted that the bank had under charged EG by Rs. 2,730.
- Dividend collected by the bank amounting to Rs. 33,000.
- Payment on EG's standing instruction of an annual subscription for a magazine amounting to Rs. 11,000.

Required:

(a) Post relevant transactions to bank book of EG to arrive at the correct bank balance as at 30 June 2016. **(10)**

(b) Prepare a bank reconciliation statement for the month of June 2016 to arrive at the adjusted bank balance as per EG's books. **(03)**

Q.19 Test Question

Following information has been extracted from the records of Unique Traders:

Bank book for the month of February 2018						
Date	**Receipts**	**Rupees**	**Date**	**Payments**	**Cheque**	**Rupees**
			1-1	b/d		133,500
			03	Salaries	X09	225,000
05	Debtors	315,000	05	Utilities	X10	352,000
09	Sales	525,000	08	Purchases	X11	622,000
12	Rentals	615,000	15	Rental	X12	608,000
18	Security deposit	200,000	20	Purchases	X13	71,000
25	Advance from customers	182,000	28	Balance		174,500
26	Debtors	294,000				
28	Cash deposited in bank	55,000				
		2,186,000				2,186,000

Date	Description	Cheque	Withdrawals	Deposits	Balance
			------------ Rupees	------------	
01	Balance				127,500
03	Cheque withdrawal	X09	225,000		(97,500)
05	Reversal of amount credited mistakenly		48,000		(145,500)
09	Cheque withdrawal	X05	63,000		(208,500)
14	Outward cheque clearing			315,000	106,500
20	Outward cheque clearing			525,000	631,500
22	Cheque withdrawal	X10	325,000		306,500
24	Payment against standing instructions		15,000		291,500
25	Outward cheque clearing			615,000	906,500
26	Outward cheque clearing			200,000	1,106,500
26	Transfer (from a debtor)			38,000	1,144,500
27	Direct Debit		200,000		944,500
28	Cheque withdrawal	X12	608,000		336,500
28	Cheque withdrawal	X13	71,000		265,500
28	Cash deposit			55,000	320,500
28	Bank charges		4,500		316,000
			1,559,500	1,748,000	

(All amounts appearing in the above bank statement are correct)

Bank reconciliation statement as on 31 Januarv 2018

Description	
Balance as per bank statement	127,500
Unpresented cheques:	
Cheque X05 dated 28 January 2018	(63,000)
Cheque X06 dated 31 January 2018	(150,000)
Amount mistakenly credited by bank	(48,000)
Corrected balance as per cash book	(133,500)

Required:

Prepare bank reconciliation statement as on 28 February 2018, showing the correct balance as per bank book and bank statement. **(08)**

Q. 20 State any Ten causes of disagreement between the balance as per bank book and the bank statement.

Q.21 Test

On 30 June 2015, the bank book of Ranjah Enterprises (RE) reflected a credit balance of Rs. 6,900,000 whereas the bank statement showed an overdraft of Rs. 4,830,000. On scrutinizing the record, following issues were discovered:

(i) Cheques deposited in bank in the last week of June 2015, amounting to Rs. 3,100,000 were wrongly credited in the bank book. Out of these, cheques amounting to Rs. 2,100,000 were cleared by the bank in July 2015 whereas a cheque of Rs. 1,000,000 deposited on 29 June 2015 was dishonoured by the bank.

(ii) Financial charges on bank overdraft amounting to Rs. 1,500,000 were recorded in the bank statement. However, review by the Accounts Officer indicated an error and RE recorded the correct amount of Rs. 1,020,000 in the bank book. The error was corrected by the bank on 10 July 2015.

(iii) A cheque issued to a supplier amounting to Rs. 8,010,000 was entered in the bank book as Rs. 8,100,000. However, the bank erroneously recorded the amount as Rs. 9,000,000.

(iv) A supplier was issued a cheque of Rs. 250,000 in place of a time barred cheque on 25 June 2015 and was cleared on the next day. However, the cancellation of time barred cheque was not recorded by RE.

(v) A payment of Rs. 100,000 through cheque was recorded twice in the bank book.

Required:

Determine the correct balance that should be reported in the bank book and prepare a statement reconciling the corrected balance with that shown in the bank statement. **(09)**

SOLUTIONS:

A. 1

Adjusted Cash Book

Unadjusted b/d	2,250	Bank charges	15
Dividend Income	900	Electricity bill	60
		c/d(adjusted)	3,075
	3,150		3,150

		Dr./Cr.	Rs.
Balance as per adjusted cash book		Cr.	6,525
Uncredited deposits:			
Rao Nadir	3,400		
Rauf	100		
Rao Nasir	350	Cr.	3,850
Unpresented Cheques:			
Surtaj	4,200		
Sawan	2,000		
Sarwar	1,100	Dr.	7,300
Balance as per cash book		Dr.	3,075

A. 2

Bank Reconciliation Statement

	Dr./Cr.	Rs.
Balance as per Bank Statement	Cr.	38,025
Unpresented Cheques	Cr.	5,200
Uncredited cheques	Dr.	6,750
Cheques wrongly Credited by Bank	Dr.	400
Balance as per cash Statement	Dr.	36,075

Adjusted Cash Book

Unadjusted b/d (bal)	36,150	Bank charges	75
		Adjusted c/d	36,075
	36,150		36,150

A. 3

Adjusted Cash Book

Unadjusted b/d	4,610	Bank charges	420
Dividend Income	380	Cheque Dishonoured	730
Cheque book	10	Trade Subscription	100
		Adjusted c/d	3,750
	5,000		5,000

Bank Reconciliation Statement as on 31-12-2001

	Dr./Cr.	Rs.
Balance as per Cash book	Dr.	3,750
Unpresented Cheques	Dr.	6,300
Uncredited cheques	Cr.	2,500
Cheques wrongly Credited by Bank	Cr.	270
Balance as per Bank Statement	Cr.	7,280

A. 4

Cash book # 1 Bank Account (Adjusted)

Dividend paid direct to the bank	400	Balance brought forword (unadjusted)	3,000
Balance carried forword (adjusted)	4,110	adjustment of under casting	700
		bank charges	300
		Cheque dishonoured	500
		Charges	10
	4,510		4,510

Bank Reconciliation statement
 # 1 Bank Account (Adjusted)
As at 30 June 1992

Balance as per cash book overdrawn			4,110 Cr.
Add: Cheques not cleared			2,500 Cr.
			6,610
Less: Unpresented Cheques	5,000	Dr.	
Cheque erroneously charged to #2 Account	1,200	Dr.	(6,200)
Balance as per bank pass book (Overdrawn)			410 Dr.

A.5

(A) **Adjusted Cash Book**

	Rs.		Rs.
Customer	2,000	Unadjusted Balance	6,530
		Interest (100 + 50)	150
		Supplier	1,000
c/d (Adjusted)	5,680		

(B) **Bank Reconciliation Statement**

	Rs.	
Balance as per Adjusted Cash Book	5,680	Cr.
Un-credited Cheques	1,900	Cr.
Un-presented Cheques	2,300	Dr.
Balance as Bank Statement	5,280	Dr.

A.6 (i) **Bank Reconciliation Statement**
As at May 31, 2005

Balance As Per Bank Statement	870	Dr.
Un-Credited Cheques	570	Cr.
Un-Presented Cheques	630	Dr.
Cheque Wrongly Debited by Bank	82	Cr.
Balance as per Adjusted Cash Book	838	Cr.

(ii) **Adjusted Cash Book**

	Rs.		Rs.
Un-adjusted balance	322	Bank charges	143
Error in Opening Balance (850 – 805)	45	Cheques (98 – 89)	9
		Receipt Recorded (230 × 2)	460
Dividend Income	1,147	Dishonoured Cheque	180
Under cast	200	Loan Interest (20,000 × 11% × 6/12)	1,100
c/d (Adjusted)	838	Lease payments (55 × 12)	660
	2,552		2,552

A.7

Cash Book (Bank Book)

Amount wrongly credited (1,550+1,550)	3,100,000	b/d (unadjusted)	3,450,000
Error in recording (4,050,000 – 4,005,000)	45,000	Debtors	500,000
Time barred cheque	125,000		
Cheque recorded twice	50,000		
c/d (adjusted)	630,000		

Bank Reconciliation Statement as on 30.06.2015

Balance as per bank statement	2,415,000	Dr
Uncredited cheque	1,050,000	Cr
Financial charges wrongly recoded by bank [750-510]	240,000	Cr
Error in recording by bank (4,500 – 4,005)	495,000	Cr
Balance as per cash book	630,000	Cr

A. 8

Bank Reconciliation statement

Balance as per bank Statement		204,000	Cr.
Add:			
Un-credited Deposits			
Channa Exports	16,500		
		16,500	Cr.
Less:			
Un-presented Deposits			
Roohi Exports	30,000		
Hina Imports	7,500		
JB & Co.	7,500		
Flash & Company	6,000		
		51,000	Dr.
Balance as per Cash book		169,500	Dr.

Adjusted Cash book

Unadjusted b/d	97,500	Bank Charges	3,000
Profit on COI	75,000		
		c/d (adjusted)	169,500
	172,500		172,500

A. 9

Adjusted Cash book

Divided	4,000	b/d(unadjusted)	30,000
		Creditor	7,000
		Bank charges	3,000
		Debtor	5,000
c/d	41,100	Cheque book	100
	45,100		45,100

Bank Reconciliation Statement
As on 30 June 2013

Balance as per cash book	Cr.	41,100
Unpresented Cheques	Dr.	50,000
Uncredited Cheques	Cr.	25,000
Cheques not debited by bank	Dr.	12,000
Balance as per bank statement	Dr.	4,100

A. 10

Adjusted Bank Account

Feb		Rupees	Feb		Rupees
28	Balance	11,753	28	Zubair Merchants (12,221-12,122)	99
28	Correction in Cheque 184	1,800	28	Correction in Cheque 188 (4,588-5,488)	900
28	Correction in Cheque 187	27	28	DD Waqas	551
			28	SO – Yasir	918
			28	Bank charges	459
			28	Closing balance	10,653
		13,580			13,580

Bank Reconciliation Statement
as on 28 February 2013

Closing balance as per Bank Statement	12,115
Unpaid cheques:	
Cheque 186 – Babar	(918)
Cheque 189 – Ilyas	(947)
Cheque 190 – Akbar	(1,652)
Deposit not yet cleared:	
Athar	2,055
Balance as per adjusted bank account	10,653

A. 11 (a) Eden Garments

Bank Account

b/d (Un-adjusted)	760,000	Account payable (85,000 – 58,000)	27,000
Accounts payable	50,000	Account receivable	366,000
Repair charges	4,630	Discount expense (76,000 / 0.95) – 76,000	4,000
Account receivable	354,000	Bank charges (7,850 – 1,250)	6,600
Dividend income	50,000	Subscription charges	12,000
		Balance c/f	803,030
	1,218,630		1,218,630

b) Bank Reconciliation statement for the month of 30 June 2016:

Balance as per bank statement	**1,490,850 Dr.**
Un-presented cheques (3,856,000 – 50,000 – 4,630)	3,801,370 Dr.
Un-credited cheques (6,460,000 – 366,000)	6,094,000 Cr.
Bank charges over charged by bank	1,250 Cr.
Balance as per bank book (Adjusted)	**803,030 Dr.**

A.12

(a)

Ahmed & Company
Bank Reconciliation Statement
As at 31 December, 2011

		Rs.
Balance as per bank statement		367,500 Cr
9	Less: Cheques issued but not presented	467,200 Dr
1	Add: Amount deposited but not credited by bank	49,200 Cr
Balance as per cash book		50,500 Cr

(b)

	Journal Entries	Debit	Credit
2	Bank charges Bank Account	1,700	1,700
3	Debtor's A/c Bank account (Dishonoured cheque)	4,200	4,200
4	Subscription Bank account	1,000	1,000
5	Bank account Payable toMr. Mubarak	10,000	10,000
6	Bank account Debtor's A/c (direct deposits)	49,900	49,900
7	Lease payments Bank account (2,600 × 3)	7,800	7,800
8	Mr. Bashir – cheque entered twice Bank account	36,400	36,400
10	Discount allowed Bank account (20,000 x 2.5 / 100)	500	500
11	Bank account Dividend income	12,000	12,000
12	Bank Account Debtors Account	9,000	9,000

No adjustments/entries for items 1 and 9.

Not Required for extra Information

Adjusted Cash Book

Mr. Ahmed	10,000	Unadjusted balance	79,800
Debtor	49,900	Bank charges	1,700
Dividend	12,000	Debtor	4,200
Debtor	9,000	Subscription	1,000
c/d (adjusted)	50,500	Lease payments	7,800
		Debtor	36,400
		Discount Allowed	500
	131,400		131,400

A.13

Comfort Travels:

(a) **Correct bank book balance as on Feb 28. 2017**

Bank Book

	Unadjusted balance	2,845,390	(i)	Accounts payable (37,250 – 32,750)	4,500
(i)	Accounts Payable	9,650	(ii)	Accounts Receivable	35,000
(iv)	Correction of carry forward (4,598,000 – 4,589,000)	9,000	(iii)	Bank charges (9,240–2,500)	6,740
(v)	Correction of undercast	4,500		c/d	2,822,300

(b) **Bank Reconciliation Statement as on February 28, 2017**

Balance as per Bank Statement	3,258,000 Cr.
Outstanding Cheques / Unpresented Cheques:	
[869,200 – 9,650]	859,550 Dr.
Cheques Deposited but under Clearance:	
[456,350 – 35,000]	421,350 Cr.
Bank charges wrongly recorded by bank	2,500 Cr.
	2,822,300 Dr.

Answer-14

Accounting entries

Date	Particulars	Debit	Credit
31-Dec-2013	Bank	35,000	
	Account payable		35,000
	(Being reversal of out-dated cheque)		
31-Dec-2013	Bank	325,690	
	Account payable		325,690
	(Post-dated cheque issued now reversed)		
31-Dec-2013	Bank	190,000	
	Account receivable (190,000/0.95)		190,000
	(To account for direct deposit into the bank and 5% discount availed for payment within a week)		
	Discount allowed (200,000 x 5%)	10,000	
	Account receivable		10,000
31-Dec-2013	Bank charges	6,570	
	Bank		6,570
	(To account for bank charges for December 2013)		
31-Dec-2013	Suspense account	11,430	
	Bank		11,430
	(debit side overcasted)		

Note:

No entries were required for following:

- Entry in respect of incorrect recording of cheque no. 765 in bank reconciliation statement.

(b)

Fine Works Limited
Bank reconciliation statement for the month of December 2013

Description	Rupees
Balance as at 31 December 2013 as per bank statement	1,721,490 Cr
Cheques issued but not presented for payments:	
Cheque No. 765	453,630 Dr
789	635,700 Dr
Customers cheques deposited in Dec. 2013 not yet credited by the bank	535,635 Cr
Corrected balance as at 31 December 2013 (635,105+35,000+325,690+190,000–6,570–11,430)	1,167,795 Dr

Bank book

Dr.		Cr.	
Unadjusted closing	635,105		
Creditor	35,000	Bank charges	6,570
Creditor	325,690		
Debtor	190,000	Amount overcasted	11,430
		Adjusted closing balance (bal.)	1,167,795

Answer-15

i)

	Particulars	Dr.	Cr.
(i)	PLS Account	5,667	
	CD Account		5,667
	(Payment from CD account wrongly recorded in PLS account now being rectified)		
(ii)	PLS Account	25,000	
	CD Account		25,000
	(Amount deposited in PLS account wrongly recorded in CD account)		
(iii)	Salary expense	750	
	CD Account		750
	(Expenses not recorded)		
(iv)	Debtor	8,563	
	CD Account		8,563
	(Cheque dishonour)		
(v)	These are unpresented cheques and will be shown in BRS.		
(vi)	CD Account	25,000	
	PLS Account		25,000
	(Transfer from PLS account to CD account not recorded)		
(vi)	CD Account	15,600	
	Payable for furniture-Best furnishers		15,600
	(Issued cheque reversed)		

ii)

Cash book (CD account) – adjusted

Dr.		Cr.	
Unadjusted closing balance	6,594		
PLS Account	25,000	PLS Account	5,667
Payable for furniture-Best furnishers	15,600	PLS Account	25,000
		Other expenses	750
		Debtor	8,563
		Adjusted closing balance (bal.)	7,214
	47,194		47,194

Cash book (PLS account) – adjusted

Dr.		Cr.	
Unadjusted closing balance	236,253		
CD Account	5,667	CD account	25,000
CD Account	25,000		
		Adjusted closing balance (bal.)	241,920
	266,920		266,920

iii)

Ex. Zed and Co.

Bank Reconciliation Statement Current Account

	CD account
Balance as per bank statement	11,503Dr
(a) (v) Unpresented cheques (8,993 + 5,445 + 11,633)	26,071Dr
(b) (i) Profit on PLS credited to CD account (wrongly credited bybank)	11,577Dr
(b) (ii) Miscellaneous charges (bank omitted to debit us)	335Dr
(b) (iii) Remittance (bank omitted to credit us)	33,500Cr
(b) (iv) Uncredited cheques	23,200Cr
Balance as per adjusted cash book	7,214Dr

Ex. Zed and Co.

Bank Reconciliation Statement - PLS Account

		PLS account
Balance as per bank statement	Dr./(Cr.)	263,508Cr
(b) (i) Profit on PLS credited to CD account (bank omitted to credit us)		
(b) (ii) Miscellaneous charges (wrongly debited by bank)		11,577Cr
(b) (iii) Remittance wrongly credited by bank		3,35Cr
Balance as per adjusted cash book	Cr./(Dr.)	33,500Dr
		241,920Dr

Answer-16

Bank book

Dr.		Cr.	
		Unadjusted closing (O/D)	730,718
Debtor - Credit transfer	65,600	Bank charges	1,700
(49,900+15,700)		Debtor (Out of date cheque)	4,200
Interest payable	16,718	Annual subscription expense	1,000
Managing director	10,000	Rent expense (hire purchase)	7,800
		(2,600 x 3 months)	
		Suspense (Amount debited twice)	36,400
		Discount allowed exp. (20,000 x 2.5%)	500
Adjusted closing balance (bal.)	690,000		
	782,318		782,318

AB Traders

Bank Reconciliation Statement

		Rupees
Balance as per bank statement		272,000 Dr
Add:	Unpresented cheques	467,200 Dr
Less:	Uncredited cheques	49,200 Cr
Balance as per adjusted bank book		690,000 Cr

A. 17

Bank Reconciliation Statement

Balance as per bank Statement	806,436	Dr.
Unpresented Cheques (377,784-5,000)	372,784	Dr.
Uncredited Cheques	250,600	Cr.
Uncredited Bills	196,500	Cr.
Cheque wrongly credited in bank statement (13,200 X 2)	26,400	Dr.
Balance as per Cash book	758,520	Cr.

Adjusted balance of cash book will appear in the statement of financial position of the business. Therefore 758,520 will appear in liabilities of business as a bank overdraft.

Cash book(Adjusted)

Markup	118,686	b/d (unadjusted) (bal)	771,062
Cheque entered twice	5,000	Subscription	3,144
		Discount allowed	10,500
Cheque wrongly credited	15,000	Plant(125,000-12,500)	112,500
c/d (adjusted)	758,520		
	897,206		897,206

Ans. 18

(a)

Adjusted cash book

Un-adjusted balance	800,000	Creditor (93,000 – 39,000)	54,000
Creditor	50,000	Debtor	375,600
Creditor	35,000	Debtor (94,080/98) x 100	1,920
Debtor	150,000	Bank Charges (16,000 + 2,730)	18,730
Dividend Income	33,000	Subscription charges	11,000
		c/f	606,750
	1,068,000		1,068,000

(b)

Eden Garments

Bank Reconciliation Statement

For the month of 30 June 2016

Balance as per cash book	**606,750**	**(Dr)**
Un-presented cheques: (3,856,000-50,000-35,000)	3,771,000	(Dr)
Un-credited cheques: (6,460,000-375,600)	6,084,400	(Cr)
Bank charges less debited	2,730	(Dr)
Balance as per bank statement	**1,703,920**	**(Dr)**

A. 19

Unique Traders
Bank Reconciliation Statement
As on 28 February 2018

Balance as per bank statement			316,000 (Cr)
Un-presented Cheques:			
Cheque X06	150,000		
Purchases X11	622,000	772,000 (Dr)	
Un-credited Cheques:			
Advance from customers	182,000		
Debtors	294,000		476,000 (Cr)
Balance as per adjusted bank book			20,000 (Dr)

Adjusted Bank Book

(Un-adj.) b/d	174,500	Standing Order	15,000
Expense overstated	27,000	Creditor	200,000
		Bank charges	4,500
Direct deposit	38,000	c/d	20,000
	239,500		239,500

A.20 Possible causes of disagreements between the bank balance shown in the bank statement and the bank book balance include:

- **(i)** Cheque deposited but not cleared
- **(ii)** Un-presented cheques
- **(iii)** Bank charges/interest
- **(iv)** Posting errors
- **(v)** Casting errors
- **(vi)** Direct credit
- **(vii)** E-payment (Direct debits)
- **(viii)** Automated teller machine (ATM) withdrawal
- **(ix)** Standing order
- **(x)** Credit/Debit transfer

Ans. 21

Cash Book (Bank Book)

Amount wrongly credited (3,100+3,100)	6,200,000	b/d (unadjusted)	6,900,000
Error in recording (8,100,000 – 8,010,000)	90,000	Debtors	1,000,000
Time barred cheque	250,000		
Cheque recorded twice	100,000		
c/d (adjusted)	1,260,000		

Bank Reconciliation Statement as on 30.06.2015

Balance as per bank statement	4,830,000	Dr
Uncredited cheque	2,100,000	Cr
Financial charges over recorded	480,000	Cr
Error in recording by bank (900,000 – 8,010,000)	990,000	Cr
Balance as per cash book	1,260000	Cr

Bank reconciliation statement (BRS) summary

Purpose of BRS is to ensure that the balance in cash book (Bank column) and balance as per Bank statement agree with each other.

	Deposit Account (favorable for the business)	Overdraft Account (Unfavorable for the business)
Business prepares Cash Book (Bank Column) or Bank A/C or Bank book	Entity's Asset => Dr	Entity's liability =>Cr
Bank prepares Bank statement or Pass book	Bank's Liability => Cr	Bank's asset =>Dr

Possible reasons of difference among the two balances:

1. Those need adjustment in cash book (Adjusting item)

a) Items in bank statement but not in cash book

	Effect In Cash Book/Bank Column
• Credit transfer	Dr
• Direct debit	Cr
• Standing order issued*	Cr
• Bank charges	Cr
• Interest on Overdrawn balance	Cr
• Deposited cheque returned dishonored	Cr
• interest on favorable balance (collection)	Dr

*Instructions to bank to make specified payments at specified fixed dates.

b) Mistake in cash book:

• Receipt side mistakenly overstated	Cr
• Receipt side mistakenly understated	Dr
• Payment side mistakenly Overstated	Dr
• Payment side mistakenly understated	Cr

2. Those need to be presented in bank reconciliation statement (Reconciling Items)

a) Items in cash book but not in bank Statement
-A cheque from customer recorded in cash book and deposited but not yet collected by the bank (Un-collected cheques) => Credited in BRS.
-A cheque paid to suppliers recorded in cash book but not yet presented to the bank for (payment (Un presented cheques) Debited in BRS

b) Mistakes committed in bank Statement

• Wrongly debited/charged by the bank	Credited in BRS
• Wrongly credited by the bank	Debited in BRS

Points to remember

1. Balance to be shown in statement of financial positions (balance sheet) would always be the balance as per adjusted cash Book.
2. Uncollected cheques are also named as uncredited cheques, unclear lodgments, deposits in transit.
3. Unrepresented cheques are also named as outstanding cheques, unpaid cheques.
4. When both balances are given prepare bank reconciliation statement starting with balance as per bank statement
5. When only the balance as per cash book is given first prepare adjusted cash book and then prepare BRS starting with the balance as per adjusted cash book.
6. When only the balance as per bank statement is given firstly prepare BRS to find out the balance as per adjusted cash book then put this balance in adjusted cash book as a closing balance and then find out the opening balance(balance before adjustment) that would be a balancing figure (If required in question)

PRACTICE QUESTIONS

Question - 1 (balance as per bank statement is not available)

The following is summary of a cash book as presented by George Ltd for the month of October:

	Rs.		Rs.
Receipts	1,469	Balance b/d	761
Balance c/d	554	Payments	1,262
	2,023		2,023

All receipts are banked and all payments are made by cheque.

On investigation you discover:

(1) Bank charges of Rs.136 entered on the bank statement have not been entered in the cash book.
(2) Cheques drawn amounting to Rs.267 had not been presented to the bank for payment.
(3) Cheques received totaling Rs.762 had been entered in the cash book and paid into the bank, but had not been credited by the bank until 3 November.
(4) A cheque for Rs.22 for sundry expenses had been entered in the cash book as a receipt instead of as a payment.
(5) A cheque received from K Jones for Rs.80 had been returned by the bank and marked 'No funds available'(means cheque is dishonored). No adjustment has been made in the cash book.
(6) A standing order for a business rates installment of Rs.150 on 30 October had not been entered in the cash book.
(7) All dividends received are credited directly to the bank account. During October amounts totaling Rs.62 were credited by the bank but no entries were made in the cash book.
(8) A cheque drawn for Rs.66 for stationery had been incorrectly entered in the cash book as Rs.60.
(9) The balance brought forward in the cash book should have been Rs.711, not Rs.761.

Required

(a) Show the adjustments required in the cash book.
(b) Prepare a bank reconciliation statement as at 31 October.

Question -2 (balance as per bank statement is available)

The Bank account for Alpine Sports Co. on April 1, 2006 indicated a balance of Rs. 16,911.95. During April, the total deposits were Rs. 65,500.4 and cheques written totaled Rs. 68,127.47.

The bank statement indicated a balance of Rs. 18,880.45 on April 30, 2006.

Comparing the bank statement, the cancelled cheques and the accompanying memorandum with the records revealed the following reconciling items:

a. Cheques outstanding totaled Rs. 5,180.27
b. A deposit of Rs. 3,481.7 representing receipts of April 30, had been made too late to appear on the bank statement.
c. A cheque for Rs. 620 had been incorrectly charged by the bank as Rs. 260
d. A cheque for payment to Bray & Son has been recorded by Alpine Sports Co. as Rs. 497.3 instead of Rs. 479.3.
e. The bank statement showed direct transfer from debtors of Rs. 3,200 and interest income of Rs.224.
f. Bank service charges for April amounted to Rs. 25
g. A cheque for Rs. 880 from Shuler Co. was returned by the bank because of insufficient funds (means cheque is dishonored).

Instructions:

1. Prepare bank reconciliation as of April 30
2. Journalize the necessary entries.

Note: if accounting entries are required in a question of BRS then prepare entries of items appearing in cash book only.

Question - 3 (balance as per bank statement is not available)

On 31st December 1998, The Cash Book of XYZ showed a debit balance of Rs. 850. On comparing the Cash Book with the bank statement, the following discrepancies were noted:

a) Cheques issued for Rs. 600 were not presented at the bank by Dec. 31, 1998
b) Cheques for Rs. 800 were deposited in the bank but were not cleared.
c) The bank collected direct from debtor Rs. 2,000 but no entry was made in cash book.
d) A cheque for Rs. 100 received from X & Co. and deposited in the bank was dishonoured.
e) The bank settled a Bill Payable amounting to Rs. 450, but it has not been entered in the cash book.
f) A cheque of Rs. 800 was dishonoured.
g) A cheque of Rs. 510 was paid into bank but bank credited the amount by Rs. 501 by mistake.
h) A cheque of Rs. 50 was deposited into bank but the same was credited by bank to a wrong account.

i) Rs. 200 was deposited into bank directly by a customer not recorded in cash book.
j) The bank received directly interest of Rs. 250 on investment not recorded in cash book..
k) A cheque of Rs. 150 received from a customer and deposited in the bank was not entered in the cash book.
l) The bank paid Rs. 125 towards insurance premium through a standing order.
m) The bank charged Rs. 9 as their commission for collecting outstation cheques and allowed (credited) interest Rs. 10 on our balance.

Required:

- Prepare a bank reconciliation statement as on December 31, 1998.
- Prepare an adjusted cash book

Question -4 (balance asper bank statement is not available)

You are Chief Accountant at Ashraf Chemicals. Bank Reconciliation Statement of Ashraf Chemicals has not been prepared yet. Read the information given below and answer the questions at end:

1.	Interest on deposits Rs. 2,500 was credited by bank and Dividend of Rs. 1,500 from Standard Paints Limited was directly collected by bank on behalf of Ashraf Chemicals on March 31, 2008.
2.	One of bank's customer Mr. Musharaf deposited Rs. 10,000 but bank credited the amount in Ashraf Chemical's account instead of in Musharaf's account.
3.	Bank paid annual Insurance payment of Rs. 1,500 to Premier Insurance Company as per our standing instructions but we did not record it in our books.
4.	Mr. Bilal (one of our customer) had given us a cheque of Rs. 5,000 which was returned by bank on March 31, 2008 marked NSF (means not sufficient funds).
5.	On March 25, Mr. Akmal (one of our customer) gave us two cheques which Mr. Ashraf deposited into bank on March 28, 2008. First cheque for Rs. 3,000 was collected by bank on March 30, 2008 and second cheque of Rs. 2,500 was encashed on April 4, 2008.
6.	Bank deducted Rs. 50 as service charges and Rs. 200 as markup on overdraft facility.
7.	Mr. Naeem was a newly hired cashier. He told you following facts: a) While casting, he overcasted debit side of cash book by Rs. 500 and credit side of cash book by Rs. 350. b) A cheque for Rs. 18,000 was issued to employees for their salary but he recorded Rs. 1,800 in cash book in this regard. c) Ashraf Chemical received a cheque for Rs. 3,600 which was cleared by bank correctly for Rs. 3,600 but he credited Cash Book by Rs. 360.
8.	Cheques for Rs. 50,000 were issued by Ashraf Chemicals in the month of March 2008 out of which Cheques for only Rs. 45,500 were encashed by suppliers upto March 31, 2008.
9.	A customer directly paid into bank Rs. 20,000 on March 28 and informed Ashraf Chemicals on April 2, 2008.
10.	The bank statement also contained a debit of Rs. 3,500 which bank manager admitted was an error on its part and he promised that this mistake will be corrected next month.

Required: If balance as on March 31, 2008 is Rs. 15,000 (Dr.) as per cash book, then prepare a Bank Reconciliation Statement and tell what would be the balance as per bank statement.

Question -5 (balance asper bank statement is available)

Mr. A operated on two separate banking accounts, described as No. 1 and No. 2.

At December 31st 1990, the balances at bank, per bank sheets (means bank statement), were No.1 Rs. 809 and No. 2 Rs. 2,013. The bank balances in A's books at the same date were debit balances against the bank No. 1 Rs. 85 and No. 2 Rs. 3,094.

The differences arose by reason of the followings:

1. Cheques lodged (deposited) but not yet credited, Rs. 200 and Rs. 140 for No. 1 and No. 2 respectively.
2. Cheque Rs. 20 paid into No. 2 dishonored, the entry therefore not having been made in A's books.
3. A cheque from D & Co. Rs. 22 remitted (transferred) direct to No. 1 not entered in A's books.
4. Cheque paid out for Rs. 73 from No. 2 account was wrongly entered in our books in account No. 1.
5. Cheque of Rs. 32 drawn on No. 2 inadvertently entered in the cash book as no. 1
6. A transfer of Rs. 1,000 out of No. 2 into No. 1 is not recorded in our books.
7. A periodic payment of Rs. 10 under standing orders for No. 2 not entered in cash book.
8. A cheque drawn on No. 2 entered in correct account in the cash book but as Rs. 12 instead of the correct amount of Rs. 21
9. Bank charges of Rs. 3 and Rs. 4 for No. 1 and No. 2 respectively not entered in Cash book.
10. Cheque received Rs. 200 for No. 2 paid into No. 2 incorrectly entered in the cash book as No. 1
11. Cheque received and paid in to correct account No. 2 Rs. 18 entered as Rs. 17
12. There are no unpresented cheques except Rs. 6 no. 2 account.

Required:

- Prepare bank reconciliation statements for both of the accounts.
- Prepare adjusted cash book

Question - 6 (balance asper bank statement is not available)

Perfect Private limited has two accounts with Ever bank Limited. The accounts were known as "Account 1" and "Account 2".

As at March 31,1990, the Accounts books reflected the following :-

Account 1- Rs. 125,000 (Dr.)

Account 2 - Rs.111,250 (Cr.)

The Accountant failed to tally the balance with the bank statement and the following information was available-

1. The Bank has charged interest on account 2, Rs.11,375 and credited interest in account 1 , Rs.1,250. These were not recorded by the Accountant.
2. Rs. 12,500 drawn on March 10, 1990 from Account 1 was recorded in the books in Account 2
3. Bank charges of Rs.150 and Rs. 1,125 for Account 1and Account 2 were not recorded in the books.
4. A deposit of Rs.17,500 in Account 1 was wrongly entered in account 2 in the books.
5. Two cheques of Rs.12,500 and Rs.13,750 deposited in account 1, but entered in Account 2 in the books, were dishonored. The entries for dishonored cheques were made in Account 2.
6. Cheques issued for Rs.150,000 and Rs. 15,000 respectively from Account 1 and 2 respectively were not presented until April 5, 1990.
7. Cheques deposited Rs.125,000 and Rs.117,500 in Account 1 and 2 respectively, were credited by bank only on April 3,1990.

Required: You are required to prepare the Bank reconciliation statement, for Account 2.

Question - 7

How will you treat following items in a Bank Reconciliation Statement, mention journal entry you will pass, if any:

1. Cheque drawn for Rs. 300 but recorded as Rs. 3,000 by cashier.
2. Cheque drawn by business for Rs. 300 but recorded as Rs. 3,000 by banker.
3. Cheque deposited into bank for Rs. 775 but returned from bank because of insufficient fund.
4. Cheque deposited into bank for Rs. 775 but not credited by bank till month end.
5. Cheque written for Rs. 600 but not paid by bank till month end.
6. Cheque of Rs. 219 was incorrectly charged by bank Rs. 129.
7. Bank statement showed a credit transfer from debtors of Rs. 200.
8. The company's bookkeeper mistakenly recorded a deposit of Rs. 530 as Rs. 350.
9. The bank statement shows that a deposit for Rs. 2,300 was erroneously recorded by the bank as Rs. 2,330.
10. The bookkeeper wrote a cheque for Rs. 369 but erroneously wrote down Rs. 396 as the payment in the company's records.

Question - 8 (balance as per bank statement is available)

Arsenal Recycling Center reports the following information concerning cash balances and cash transactions for the month of September:

(i) Cash balance per bank statement as of September 30 was Rs. 20,893.25.

(ii) Two debit memoranda accompanied the bank statement: one for Rs. 10 was for service charges for the month; the other for Rs. 64.60 was attached to an NSF cheque from Saeed Anwar.

(iii) Included with the bank statement was Rs. 69 credit memorandum for interest earned on the bank account in September.

(iv) The paid cheques returned with the September bank statement disclosed an error in Arsenal Recycling Center cash records. Cheque No. 851 for Rs. 77.44 for telephone expense had erroneously been listed in the cash payments journal as Rs. 44.77.

(v) A collection charge for Rs. 26.00 (not applicable to the centre) was deducted from the account by bank. Notice this was the bank's error.

(vi) Cash receipts of September 30 amounting to Rs. 585.25 were mailed to the bank too late to be included in the September bank statement.

(vii) Cheques outstanding as of September 30 were as follows; no. 860 for Rs. 151.93, no. 867 for Rs. 82.46, and no. 869 for Rs. 123.61.

(viii) The bank account showed the following entries during September:

Bank

1998			Rs.	1998			Rs.
Sept.	1	Balance	18,341.82	Sept.	30	Month's payments	11,598.63
	30	Month's receipts	14,441.58				

Required: Bank reconciliation as at September 30, 1998

Question - 9

Following information relates to Babar Shop for the month of June:

Balance per Bank of Punjab Statement at June 30	15,023.05
Outstanding cheques	4,215.83
NSF cheques from customer	250.68
Deposits in transit	2,452.87
Interest income appearing in bank statement not appearing in bank account	251.32
Service charge deducted by bank not appearing in bank account	15.00
Cash balance as per Babar's records at June 30	13,274.45

Required:

1. Prepare a Bank Reconciliation Statement as on June 30.
2. Give the journal entries to record any needed adjustments to the general ledger's balance.
3. What is the net effect on net income for these adjustments?
4. If Babar Shop is going to prepare a statement of financial position as on June 30, what balance of cash will it report?

Question - 10 (balance as per bank statement is available)

Yaqoob Company developed the following reconciling information in preparing its September bank reconciliation:

Balance as per bank statement , Sep 30	11,000
Credit transfers from debtors appearing in bank statement not recorded in cash book	4,000
Outstanding cheques	6,000
Deposits-in-transit	3,000
Bank service charge	50
NSF check	800

Required: Determine the cash balance per books (unadjusted) for Yaqoob Company.

Solutions

Answer -1

Cash Book – adjusted

Dr.		Cr.	
		Unadjusted closing balance	554
Dividend income	62	Bank charges	136
		Payment recorded on wrong side (22x2)	44
Brought forward excess recorded (761-711)	50	K J (Dishonor cheque)	80
		Business rate expense	150
		Stationery expense less recorded (66-60)	6
Adjusted closing balance (bal.)	858		

Bank Reconciliation Statement

Balance as per adjusted cash book (overdraft)	858 Cr
Add: Unpresented cheques	267 Dr
Less: Uncredited cheques	762 Cr
Balance as per bank statement (overdraft)	1,353 Dr

Answer-2

1)

Alpine Sports Co.
Cash book – Adjusted

Dr.		Cr.	
b/d	16,911.95		
Deposits	65,500.40	Cheques written	68,127.47
		c/d	14,284.88
Unadjusted closing balance	14,284.88		
B & Son (497.3-479.3)	18.00	Bank charges	25.00
Debtors	3,200.00	S Co. - Debtor	880.00
Interest income	224.00		
		Adjusted closing balance (bal.)	16,821.88

Alpine Sports Co.
Bank Reconciliation Statement

Balance as per bank statement			18,880.45 Cr
Add:	Unpresented cheques		5,180.27 Dr
	Our account less debited by the bank	(620-260)	360.00 Dr
Less: Uncredited cheques			3,481.70 Cr
Balance as per cash book			16821.88 Dr

2)

	Particulars	Dr.	Cr.
d)	Bank	18.00	
	Creditor Bray & Co.		18.00
e)	Bank	3,200.00	
	Debtor		3,200.00
	Bank	224.00	
	Interest income		224.00
f)	Bank charges	25.00	
	Bank Account		25.00
g)	S & Co.	880.00	
	Bank Account		880.00

Answer- 3

Mr. XYZ
Cash book – adjusted

Dr.
Cr.

Unadjusted closing balance		850			
Debtor	c	2,000	X & Co.	d	100
Debtor	i	200	Bill Payable	e	450
Interest on investment	j	250	Debtor	f	800
Debtor	k	150	Insurance expense	l	125
Interest on bank acc.	m	10	Commission charges	m	9
			Adjusted closing balance (bal.)		1,976

Mr. XYZ
Bank reconciliation Statement

Balance as per adjusted cash book	1,976 Dr
Add: Unpresented cheques	600 Dr
Less: Uncredited cheques	800
Less credited by bank (510-501)	9
Bank omitted to credit our account	50
	859 Cr
Balance as per bank statement	1,717 Cr

Answer- 4

Ashraf Chemicals
Cash book – adjusted

Dr.
Cr.

Unadjusted closing balance		15,000			
Interest income	1	2,500	Insurance expense	3	1,500
Dividend income	1	1,500	Mr. Bilal – Debtor	4	5,000
Suspense - overcasted	7a	350	Bank Charges (200+50)	6	250
Suspense (3,600+360)	7c	3,960	Suspense- overcasted	7a	500
Debtors	9	20,000	Suspense (18,000-1,800)	7b	16,200
			Adjusted closing balance (bal.)		19,860

Ashraf Chemicals
Bank Reconciliation Statement

Balance as per adjusted cash book			19,860 Dr
Add: Unpresented cheques	8	(50,000-45,500)	4,500
Wrong Credit by bank	2		10,000
			14,500 Dr
Less: Uncredited cheques	5		2,500
Wrong debit by bank	10		3,500
			6,000 Cr
Balance as per bank statement			28,360 Cr

Answer- 5

Mr. A
Bank account 1 – adjusted

Dr. Cr.

Unadjusted closing balance	85		
D & Co.	22	Bank charges	3
Bank account -2	73	Bank account-2	200
Bank account -2	32		
Bank account -2	1,000		
		Adjusted closing balance (bal.)	1,009

Mr. A
Bank account 2 – adjusted

Dr. Cr.

Unadjusted closing balance	3,094		
		Debtor	20
Bank account-1	200	Bank account-1	73
Suspense (18-17)	1	Bank account-1	32
		Standing order payment	10
		Bank account-1	1,000
		Suspense (21-12)	9
		Bank charges	4
		Adjusted closing balance (bal.)	2,147

Mr. A
Bank reconciliation Statement - Bank account 1

Balance as per bank statement	809 Cr
Add: Unpresented cheques	-
Less: Uncredited cheques	200 Cr
Balance as per adjusted cash book	1,009Dr

Mr. A
Bank reconciliation Statement – Bank account 2

Balance as per bank statement	2,013 Cr
Add: Unpresented cheques	6 Dr
Less: Uncredited cheques	140 Cr
Balance as per adjusted cash book	2,147 Dr

Answer- 6

Perfect Private Limited
Cash book – adjusted (Account-2)

Dr. Cr.

		Unadjusted closing balance	111,250
Bank account-1	12,500	Interest charges	11,375
		Bank Charges	1,125
		Bank account-1	17,500
Adjusted closing balance (bal.)	128,750		

The transaction no. 5 does not relate to account no. 2. However as recording and dishonour both are recorded in this account so the effect of error is automatically eliminated.

Perfect Private Limited
Bank reconciliation Statement – Account 2

Balance as per adjusted cash book	(128,750)
Add: Unpresented cheques	15,000
Less: Uncredited cheques	(117,500)
Balance as per bank statement	(231,250

Answer- 7

		Dr.	Cr.
1.	Bank Account	2,700	
	Creditor Account		2,700
2.	Bank has given us a wrong debit by Rs. 2,700 so Rs. 2,700 will be shown as credit item in BRS.		
3.	Debtors	775	
	Bank		775
4.	Rs. 775 will be shown as credit item in BRS as Uncredited cheques		
5.	Rs. 600 will be shown as debit item in BRS as Unpresented cheques		
6.	This is an error on part of bank so it will be shown in BRS as debit item by Rs. 90.		
7.	Bank	200	
	Debtors		200
8.	Bank (530-350)	180	
	Debtors		180
9.	This is wrong credit by Bank so Rs. 30 will be shown as debit item in BRS.		
10.	Bank	27	
	Creditor		27

Answer- 8

Arsenal Recycling Center
Cash book – unadjusted

Dr.			Cr.
b/d	18,341.82	Payments	11,598.63
Receipts	14,441.58	Unadjusted closing balance	21,184.77

Arsenal Recycling Center
Cash book – adjusted

Dr.			Cr.
Unadjusted closing balance	21,184.77	Service charges	10.00
Interest Income	69.00	Saeed Anwar	64.60
		Telephone expense (less recorded)	32.67
		Adjusted closing balance (bal.)	21,146.50

Arsenal Recycling Center
Bank Reconciliation Statement

Balance as per bank statement		20,893.25 Cr
Add: Unpresented cheques		
860	151.93	
867	82.46	
869	123.61	358.00 Dr
Less: Deposit-in-transit		585.25 Cr
Less: Collection charges wrongly debited by bank		26.00 Cr
Balance as per adjusted cash book		21,146.5 Dr

Answer- 9

1)

Babar Shop
Cash book – adjusted

Dr.			Cr.
Unadjusted closing balance	13,274.45		
Interest income	251.32	Bank Charges	15.00
		Debtors (NSF)	250.68
		Adjusted closing balance (bal.)	13,260.09

Babar Shop
Bank Reconciliation Statement

Balance as per bank statement	15,023.05Cr
Add: Unpresented cheques	4,215.83Dr
Less: Uncredited cheques	2,452.87Cr
Balance as per adjusted cash book	13,260.09Dr

2)

Particulars	Dr.	Cr.
Bank Account	251.32	
Interest Income		251.32
Bank Charges	15.00	
Bank Account		15.00
Debtors	250.68	
Bank Account		250.68

3) Profit will increase by Rs. 251.32 in respect of interest income and will decrease by Rs. 15 in respect of bank charges.

4) Rs. 13,260.09 will be shown in balance sheet.

Answer- 10

Yaqoob Company
Cash book – adjusted

Dr. Cr.

Dr.		Cr.	
Unadjusted closing balance (bal.)	4,850		
Debtor (Credit transfer)	4,000	Bank Charges	50
		Debtors (NSF)	800
		Adjusted closing balance (W-1)	8,000

(W-1)

Yaqoob Company
Bank Reconciliation Statement

Balance as per bank statement	11,000Cr
Add: Unpresented cheques	6,000Dr
Less: Uncredited cheques	3,000Cr
Balance as per adjusted cash book	8,000Dr

Test question:

Q.1 Lamda Establishment is preparing bank reconciliation statement on 30 June 2019. In this respect, the following information is available:

(i) Cash book showed an overdrawn balance of Rs. 3,928,000.

(ii) Cheques outstanding as at 30 June 2019 amounting to Rs. 1,250,000 included:
- a cheque of Rs. 10,000 dated 8 December 2018 issued to a welfare organisation for donation.
- a cheque of Rs. 150,000 dated 20 June 2019 mailed to a supplier on 10 July 2019.

(iii) A cheque of Rs. 391,000 issued to a supplier was recorded in the cash book as Rs. 319,000.

(iv) Cheques received from customers amounting to Rs. 670,000 were recorded in the cash book but not credited in bank statement. These cheques included a cheque dated 10 July 2019 amounting to Rs. 25,000 received from a customer on 28 June 2019.

(v) A bank debit advice dated 30 June 2019 for interest charges amounting to Rs. 80,000 was received in July 2019.

Required:

(a) Compute the corrected cash book balance as at 30 June 2019. **(04)**

(b) Compute the bank balance as would be appearing in the bank statement as at 30 June 2019. **(04)**

Answer:

Cash Book (Bank Book)

Donation	10,000	b/d (unadjusted)	3,928,000
Post dated cheques	150,000	Under casting error (391,000 - 319,000)	72,000
		Post dated cheque	25,000
		Bank charges	80,000
c/d (adjusted)	3,945,000		

Lamda Establishment
Bank Reconciliation Statement
as on 30.06.2019

Balance as per adjusted cash book	3,945,000	Cr
Unpresented cheque (1,250,000 – 10,000 – 150,000)	1,090,000	Dr
Uncredited cheques (670.000 – 25,000)	645,000	Cr
Balance as per bank statement	**3.500,000**	**Dr**

Inventories:

Concept of Mark-up and Margin:

Cost =	100,000
Profit =	20,000
Sale price	120,000

Percentage of profit can be calculated on the basis of sales or on the basis of cost e.g.

(a) Profit / sales × 100

$20{,}000/120{,}000 \times 100 = 16.67\%$ of sales.

It means that if sale is 100 then profit is 16.67.

If profit percentage is on the basis of sales; then it is called as **margin**.

(b) Profit / cost × 100

$20{,}000/100{,}000 \times 100 = 20\%$ of cost.

It means that if cost is 100 then profit is 20.

If profit percentage is on the basis of cost; then it is called as **mark-up**.

In Summary:

- Both the words mark up and margin means profit
- 20% margin means 20% profit on sales.
- 20% mark-up means 20% profit on cost.

However, if question says that:

(a) 20% margin on cost then it means 20% profit on cost (treated as mark-up); means cost is 100.

(b) 20% mark up on sale then it means 20% profit on sales (treated as margin); means sale is 100.

Examples of Mark up & Margin

(1) Cost = 50,000

Selling Price = 55,000

Profit = 5,000

% of Margin = ?

$$\% \text{ Margin} = \frac{\text{Profit}}{\text{Sales}} \times 100$$

$$= \frac{5{,}000}{55{,}000} \times 100$$

% Margin = 9.0909% of Sales

(2) Cost = 100,000

16.67% Margin

Sales = ?

C + P = S

83.33 + 16.67 = 100

$$= \frac{100{,}000}{83.33} \times 100 = 120{,}000$$

(3) Profit = 50,000

10% Margin

Sales = ?

C + P = S

90 + 10 = 100

$= \frac{50,000}{10} \times 100 = 500,000$

(4) Sales = 500,000

25% margin

Profit = ?

C + P = 8

75 + 25 = 100

Profit = $\frac{500,000}{100} \times 25$

$\boxed{\text{Profit} = 125,000}$

(5) Profit = 100,000

25% Mark up

Sales = ?

C + P = S

100 + 25 = 125

Sales = $\frac{100,000}{25} \times 125$

$\boxed{\text{Sales} = 500,000}$

(6) Sales = 15,400

40% Mark up

Profit = ?

C + P = S

100 + 40 = 140

Profit = $\frac{15,400}{140} \times 40$

$\boxed{\text{Profit} = 4,400}$

Inventories (Stock)

Trading Business:

In such businesses items purchased are sold by adding profit in cost price. In such businesses cost of sales are calculated as follows:

Opening stock	XX
Add: Purchases (less returns)	XX
Add: Carriage Inwards	XX
Less: Closing Stock	(XX)
	XX

Format of income statement:

Sales		XX
Less: Cost of Sales		
Opening Stock	XX	
Purchases (less returns)	XX	
Closing Stock	(XX)	(XX)
Gross Profit		XX
Other Income:		XX
Operating Expenses:		
Salaries & Wages	XX	
Carriage Outwards	XX	
Rent and Rates	XX	
Insurance	XX	(XX)
Net Profit		XX

Example 1:

Stock as on 01-07-2014 : 1,000 units @ 70 each.

During the year, following units were purchased:

15-07-2014: 10,000 units @ 71 each

31-12-2014: 8,000 units @ 73 each

15-03-2015: 6,500 units @ 72 each

During the year, 15,000 units were sold @ 78 each.

Required:

Calculate the gross profit for the year ended 30th June, 2015, by preparing an income statement by using First in first out and weighted average.

Answer:

FIFO: (First in First Out) In FIFO, it is assumed that units purchased first are sold first. Therefore closing stock units comprises of latest purchases.

(a) **Statement of Comprehensive Income (FIFO)**
For the year ended 30th June, 2015

Sales (15,000 × 78)		1,170,000
Cost of Sales		
Opening Stock (1,000 × 70)	70,000	
Purchases (W-1)	1,762,000	
Closing Stock (W-2)	(760,000)	(1,072,000)
Gross Profit		98,000

(W-1) Purchases:

10,000 units × 71 =	710,000
8,000 units × 73 =	584,000
6,500 units × 72 =	468,000
	1,762,000

(W-2) Closing Stock (FIFO)

Closing stock units = 1,000 + 10,000 + 8,000 + 6,500 – 15,000 = 10,500 units.

4,000 × 73 =	292,000
6,500 × 72 =	468,000
	760,000

Weighted Average:

A rate/ units is first calculated as follows:

$$\text{Rate/unit} = \frac{\text{Opening Stock (Amount)} + \text{Purchases (Amount)}}{\text{Opening Stock (Units)} + \text{Purchases (Units)}}$$

(b) **Statement of Comprehensive Income (Weighted average)**
For the year ended 30th June, 2015

Sales (15,000 × 78)		1,170,000
Cost of Sales:		
Opening Stock (1,000 × 70)	70,000	
Purchases	1,762,000	
Closing Stock (W-3)	(754,320)	(1,077,680)
Gross Profit		92,320

$$\text{Rate/unit} = \frac{70{,}000 + 1{,}762{,}000}{1{,}000 + 24{,}500}$$

= 71.843/unit

Closing Stock = 71.843 × 10,500

= 754,320

Relationship of stocks with profit:

(i) Closing Stock has direct relationship with the profit.

(ii) Opening stock has inverse relationship with profit.

Measurement of Inventories:
Inventories are measured at lower of cost and net realisable value (NRV).

Prudence Concept:
- Anticipated losses should be recorded immediately.
- Anticipated gains should be recorded when actually occur.

In other words, Assets and Incomes should not be overstated; while liabilities and expenses should not be understated.
Cost can be calculated by using FIFO or weighted average.

Net Realisable value (NRV):

Estimated Selling price	XX
Less: Estimated Selling Expenses* necessary to make sale	(XX)
	XX

***Examples of selling Expenses:**
Carriage Outwards
Advertisement
Commission etc.

Example 1:

As on 30-06-2014

10,000 units are in hand	
Cost =	100,000
Net Realizable Value:	
Estimate Selling Price (10,000 × 12)	120,000
Estimate Selling Expenses	(15,000)
NRV	105,000

In this case there is an anticipated gain of Rs. 5,000 (which should not be recognised immediately).

Income Statement (assumed figures)
For the year ended 30-06-2014

Sales		1,200,000
Cost of Sales:		
Opening Stock	80,000	
Purchases	900,000	
Closing Stock	(100,000)	(880,000)
Gross Profit		320,000

Conclusion:
Stock is measured at cost when it is lower than NRV because anticipated gain should not be recorded immediately.

Example 2:

As on 30-06-2012

Closing stock units =	70,000
Cost =	350,000
Net Realizable Value:	
Estimate Selling Price (70,000 × 6)	420,000
Estimate Selling Expenses	(80,000)
NRV	340,000

In this case there is a loss of Rs. 10,000 (which should be recognised immediately).

Income Statement (assumed figures)
For the year ended 30-06-2014

Sales		1,800,000
Cost of Sales:		
Opening Stock	150,000	
Purchases	1,200,000	
Closing Stock	(340,000)	(1,010,000)
Gross Profit		790,000

Conclusion:

Stock is measured at NRV when it is lower than cost because anticipated loss should be recognized immediately.

Important Point to Remember:

In the calculation of NRV, estimated future selling price is to be taken. If however, it is not available then assume that current selling price will be future selling price as well. If there are more than one current selling prices during the period then use the latest selling price.

Question 1

Azhar and Company are importers of a particular item. Accountant of the company has prepared the profit and loss account following average method for valuation for closing inventory.

Particulars	Date	Quantity	Amount
Opening Stock		1,000	
Purchases	05-07-2002	5,000	3,250,000
	10-09-2002	14,000	8,750,000
	26-12-2002	9,500	6,650,000
	24-03-2003	18,600	13,857,000
	05-04-2003	15,600	11,310,000
	31-05-2003	10,100	6,969,000
Sales		57,000	
Closing Stock		16,800	

The profit and loss account prepared by the accountants on average method if valuation of closing inventory is as follows:

Particulars			Rupees	
sales				41,325,000
less:	Cost of Sales			
		opening Stock	560,000	
	Add:	Purchases	50,786,000	
			51,346,000	
	Less:	Closing Stock	(11,688,520)	(39,657,480)
Gross Profit				1,667,520
less:	Operating and Selling Expenses			(1,525,900)
Net Profit				141,620

Required:

Prepare a revised profit and loss account based on FIFO method for valuation of closing inventory at cost or net realizable value whichever is lower. The selling expenses are 2% of Sales

Assume Year end is 30.06.2003

Methods of Recording Inventories:

There are two methods of recording Inventories.

Periodic Inventory System

(1) Closing stock of last period becomes opening stock of next period.

(2) Purchases and Purchase return are recorded date wise during the accounting period.

(3) Sale and sale return are also recorded date wise during the accounting period.

(4) Cost of loss, drawings of good etc are calculated at the end of accounting period rather than date wise. Cost of sales are also calculated at the end of the period after measuring closing stock at the end of the period.

(5) Closing stock is counted at the end of period and then measured at lower of cost and NRV.

Perpetual Inventory System

(1) Closing stock of last period becomes opening stock of next period.

(2) Purchases and Purchase return are recorded date wise during the accounting period.

(3) Sale and sale return are also recorded date wise during the accounting period.

(4) Cost of loss, drawings of good as well as cost of sale etc are calculated and recorded date wise.

(5) Closing stock is counted at the end of period and then measured at lower of cost and NRV.

Question 2

Hammad deals in a single product. The transactions for the month August 2014 are summarized below:

Balance	1 August 2014	40,000 units @ Rs. 70
Purchase	12 August 2014	20,000 units @ Rs. 75
Sale	15 August 2014	30,000 units @ Rs. 120
Purchase	28 August 2014	20,000 units @ Rs. 78
Sale	30 August 2014	20,000 units @ Rs. 125

Required:

Compute the cost of ending inventory using weighted average method under each of the following assumptions:

(a) Perpetual inventories are maintained; **(4.5)**

(b) Perpetual inventories are not maintained. **(4.5)**

Question 3

Quality Products (QP) deals in various goods. Following information pertains to one of its product for the month of January 2016:

Date	Description	Units	Purchase/Sale Price Per Unit (Rs.)
6-Jan-2016	Purchase	15,000	150
10-Jan-2016	Sale	(18,000)	210
16-Jan-2016	Purchase	13,000	160
18-Jan-2016	Purchase return	(1,000)	150
25-Jan-2016	Sale	(12,000)	215
28-Jan-2016	Drawing	(2,000)	-
29-Jan-2016	Purchase	10,000	140
31-Jan-2016	Shortage	(800)	-

Opening inventory consisted of 10,000 units costing Rs. 1,480,000. Closing inventory includes 1,200 units found damaged during stock taking. Net realisable values (NRVs) of the damaged and the good units are Rs. 120 and Rs. 200 per unit respectively. QP uses perpetual inventory method to record the inventory.

Required:

Compute the value of closing inventory using:

- Weighted average cost method
- First in first out

Accounting Entries under both the systems

Description	Perpetual System			Periodic System		
	Entry	**Dr.**	**Cr.**	**Entry**	**Dr.**	**Cr.**
Opening stock	No. Entry Written as b/d in inventory a/c			No Entry Written as b/d in inventory a/c		
Purchases	Inventory a/c Creditors a/c	xxx	 xxx	Purchase a/c Creditor a/c	xxx	 xxx
Purchase return	Creditor a/c Inventory a/c	xxx	 xxx	Creditor a/c Purchase Return a/c	xxx	 xxx
Carriage-in paid	Inventory a/c Cash a/c	xxx	 xxx	Carriage in a/c Cash a/c	xxx	 xxx
Sale	Debtor a/c sales a/c (with sales figure)	xxx	 xxx	Debtor a/c Sales a/c (with sales figure)	xxx	 xxx
	Cost of goods sold a/c inventory a/c (with cost figure)	xxx		X		
Return	Sale return a/c Debtor a/c (with sales figure)	xxx	 Xxx	Sale return a/c Debtor a/c	xxx	 xxx
	Inventory a/c Cost of goods sold a/c (with cost figure)	xxx	 Xxx	X		
Closing stock	No entry Closing stock is calculated as bal. figure			No entry		
Normal loss	Cost of sales Inventory	xxx	 xxx	No entry		
Abnormal loss	Abnormal loss Inventory	xxx	 xxx	Abnormal loss Purchases	Xxx	 xxx
Drawings	Drawings Inventory	xxx	 xxx	Drawings Purchases	xxx	 Xxx

Question 4

Mr. Asif has provided the following details:

(1) Opening stock (4 units @ Rs. 40 each) 160

(2) Purchases:

- Goods costing Rs. 30,000 are purchased on 1.7.2004.
- Goods costing Rs. 25,000 are purchased on 15.8.2004.
- Goods costing Rs. 4,500 are returned by us on 16.8.2004.

(3) Sales:

- Goods costing Rs. 16,000 are sold on 19.8.2004 for Rs. 25,000.
- Goods costing Rs. 7,000 are sold on 20.9.2004 for Rs. 9,000.
- Goods costing Rs. 3,000 are returned by customer on 12.12.2004. Sale Price of goods were 4,000.

Required:

(i) Assuming perpetual system is used, prepare inventory a/c and cost of sales A/C.

(ii) Also pass necessary entries for all of above transactions.

Year end is December 31, 2004.

All purchases and sale are on credit.

Discounts

Trade Discount
(Negotiation Discount)

Treatment Sale and purchase
Is recorded net of trade discount

Settlement Discount
(Early payment Discount)

Related to credit transactions

Discount Allowed

Discount Allowed (Dr.)
Debtor (Cr.)

Discount Received

Creditor (Dr.)
Discount Received (Cr.)

Cash Sale

Good sold for Rs.100,000 on cash after negotiation Rs.5,000 is allowed as a discount

Seller		**Buyer**	
Cash 95,000		Purchase 95,000	
	Sale 95,000		Cash 95,000

Credit Sale

Goods sold for Rs.700,000 on credit to All after negotiation Rs.10,000 is allowed as a discount .It is further agreed that if payment is made within 10Days Rs.20,000 will also be allowed as a discount . Date Of sale is 1-7-2015 (and assume amount is received on 8-7-2015)

Seller

1-7-2015	Debtor	690,000	
	Sale		690,000
8-7-2015	Cash	670,000	
	Debtor		670,000
	Discount Allowed	20,000	
	Debtor		20,000

Buyer

Purchase	690,000	
Creditor		690,000
Creditor	670,000	
Cash		670,000
Creditor	20,000	
Discount Allowed		20,000

Debtor

Sale	690,000	Cash	670,000
		Discount Allowed	20,000

Creditor

Cash	670,000	Purchases	690,000
Discount Received	20,000		

Question 5

Max Savings sells goods at cost plus 30% and uses perpetual inventory method to record the inventory. The following transactions pertain to August 2017:

04-Aug	Purchased goods on cash for Rs. 568,000.
07-Aug	Sold goods on credit for Rs. 2,418,000.
10-Aug	Returned goods to a supplier costing Rs. 87,000.
13-Aug	Purchased goods on credit for Rs. 2,360,000.
13-Aug	Paid carriage inward of Rs. 48,000.
20-Aug	A customer returned goods which had been invoiced at Rs. 58,500.
24-Aug	Cash sales of Rs. 120,000 net of a special discount of Rs. 10,000.
31-Aug	Physical inventory count revealed that goods having sale price of Rs. 26,000 have expired and had to be scrapped.

Required:

Prepare journal entries to record the above transactions. (narrations are not required) **(10)**

Note:

- If question is silent, then use periodic inventory system.
- If question is silent, then always calculate cost as well as NRV of inventory (if there is an information of NRV) and then select the lower figure.

Question 6

On 1 January 2012, a company held 300 units of an item of finished goods inventory. These were valued at Rs. 22 each. During January 2012 three batches of finished goods were received into store from the production department, as follows:

Date	**Units Received**	**Production cost per unit j Rupees**
10-Jan	400	Rs. 23
20-Jan	400	Rs. 25
25-Jan	400	Rs. 26

Goods sold out of the inventory during January 2012 were as follows:

Date	**Units sold**	**Sale price per unit Rupees**
14-Jan	500	Rs. 31
21-Jan	500	Rs. 33
28-Jan	100	Rs. 32

Required:

Compute the cost of sales and inventory at 31 January 2012, applying the following basis of inventory valuation:

(i) FIFO (ii) Weighted Average Cost (Average is updated after every transaction).

INVENTORIES
ICAP QUESTIONS

QUESTION-1

Mr. Khan began business as a coffee importer in July 1996. Purchases of coffee bears were made by him as follows:

1996	Kgs	Price / Kg (Rs.)	Total (Rs.)
1 July	56	20.50	1,148
12 August	42	24.00	1,008
30 September	49	26.00	1,274
15 October	35	35.20	1,232
29 November	28	37.50	1,050
10 December	24	50.00	1,200

By 31 December, 168 Kgs. had been sold, the proceeds amounting to Rs. 8,480.

Required:

(a) Calculate closing stock on each of the following basis:
- ➢ First in, first out
- ➢ Average cost **(07)**

(b) Show the effect of each method on gross profit using the above figures. **(02)**

QUESTION-2

Bamboo private Ltd. uses the periodic inventory system The beginning inventory of an item Code-7 and data pertaining to its purchases and sales during February, 1995 are shown below:

Feb1	Unsold balance	3,000 Units	@ Rs. 6.00
Feb 4	Purchase	500 Units	@Rs. 5.40
Feb 9	Sale	2,000 Units	
Feb 12	Purchase	3,000 Units	@ Rs. 5.10
Feb 20	Sale	800 Units	
Feb 24	Sale	1,600 Units	
Feb 26	Purchase	1,200 Units	@ Rs. 4.80
Feb 27	Sale	300 Units	

On 28th February, 1995 the estimated selling price of code-7 had declined to Rs. 4.50 per unit.

Required:

Compute the value of the ending inventory of Code-7 on 28th February 1994, assuming the company used the first in first out (FIFO) method for cost determination and applied the lower of cost and net realizable value

(12)

{November 1995, C.A Inter - II, Q # 1(b)}

QUESTION-3

In the month of December 2013 there was a fire in the premises of Zee Limited resulting in loss of inventory. Relevant information related to damaged inventor is as under:

	Alpha	Beta	Gamma
	Rs. In million		
Cost	12.00	6.00	8.00
Alpha to be sold as scrap	0.90	-	
Estimated selling price	-	4.00	9.00
Estimated cost to sell	-	0.10	0.05
Estimated additional cost for re-packing	-	0.50	0.70

Required:

Compute the amount of inventory as would appear in the trading and profit and loss account of Zee Limited for the year ended 31 December 2013. **(06)**

{Spring 2014, Q # 3 (a)}

SOLUTIONS

Solution No. 1

(a) Opening Stock = Nil

kgs purchased during the period (56 + 42 + 49 + 35 + 28 + 24)	234
Kgs sold during the period (given)	(168)
Kgs in hand at the end of period	66

(i) According to FIFO:

24 × 50 = 1,200
28 × 37.5 = 1,050
14 × 35.2 = 492.8 $\boxed{2,742.8}$

(ii) According to Weighted Aug:

$$= \frac{0 + 6,912}{0 + 234} = 29.53 \times 66$$

= 1,950 (Approx)

(b) By using FIFO method as compared to weighted average method, the profit is increased by 793. (4,311 – 3,518).

Gross Profit Using FIFO:

Mr. Khan
Trading Account
For the Year ended 31-12-1996

	Rs.	Rs.
Sales		8,480
Less: Cost of Sales:		
Opening Stock	--	
Add: Purchases (1,148 + 1,008 + 1,274 + 1,232 + 1,050 + 1,200)	6,912	
Less: Closing Stock	(2,743)	(4,169)
Gross Profit		**4,311**

Gross Profit Using Weighted average:

Sales		8,480
Less: Cost of Sales:		
Opening Stock	--	
Add: Purchases	6,912	
Less: Closing Stock	(1,950)	(4,962)
Gross Profit		**3,518**

Solution No. 2

Value of closing stock is lower of cost and NRV; i.e. Rs. 13,500

W-1	Opening Stock (Units)	3,000
	Purchases (500 + 3,000 + 1,200) (Units)	4,700
	Sold (2,000 + 800 + 1,600 + 300) (Units)	(4,700)
	Closing Stock (Units)	3,000

According to FIFO:

1,200 × 4.8	5,760
1,800 × 5.10	9,180
	14,940
NRV: (3,000 × 4.5)	13,500

*As there is no indication of selling expense, therefore they are ignored.

Solution No. 3

Closing Inventory Valuation:

	Alpha	**Beta**	**Gamma**
	Rs. In million		
Cost	12.00	6.00	8.00
NRV:			
Estimated selling price	0.90	4.00	9.00
Estimated cost to sell	-	(0.10)	(0.05)
Estimated additional cost for re-packing	-	(0.50)	(0.70)
NRV	0.90	3.40	8.25
Lower	0.90	3.40	8.00

Solution:1

Azhar and Company
Trading and Profit and Loss Account
for the year ended June 30, 2003

		Rupees
Sales		41,325,000
Less: Cost of sales		
Opening Stock		560,000
Purchases		50,786,000
Closing Stock	(Lower of W-1 and W-2)	(11,826,500)
		(39,519,500)
Gross Profit		1,805,500
Less: Operating and selling expenses		(1,525,900)
Net Profit		279,600

As the cost is lower than NRV so stock is recorded at cost.

(W-1) NRV of closing stock		Rupees
Estimated selling price (Per unit selling price x No. of units in closing stock)	((W-1.1)725 x 16,800)	12,180,000
Less: Estimated cost to sell	(725x2%) x 16,800)	(243,600)
		11,936,400

(W-1.1)

Per unit selling price (Sale value/No. of units sold) (41,325,000/57,000) 725

(W-2) Cost of closing stock

Date of purchase		Quantity	Per unit cost (W-3)	Cost
5/4/2003	(16,800-10,100)	6,700	725	4,857,500
31/05/2003		10,100	690	6,969,000
				11,826,500

(W-3) Per unit cost of items purchased

Date of purchase	Quantity	Cost	Per unit cost
5/4/2003	15,600	11,310,000	725
31/05/2003	10,100	6,969,000	690

Not a part of ICAP question
Check whether weighted average calculation made by accountant is correct ?

Answer

Yes it is correct as calculated below:

		Quantity	Rupees / Cost
Value of closing stock	(16,800 x 695.7452)		11,688,520
Opening stock		1,000	560,000
Purchases			
5/7/2002		5,000	3,250,000
10/9/2002		14,000	8,750,000
26/12/2002		9,500	6,650,000
24/03/2003		18,600	13,857,000
5/4/2003		15,600	11,310,000
31/05/2003		10,100	6,969,000
		72,800	50,786,000
		73,800	51,346,000
Weighted average cost per unit	(51,346,000/73,800)		695.7452

Answer 2

(a) Weighted average method (Perpetual inventory):

Date	Received			Issued			Balance		
	Qty	Rate	Rs.	Qty	Rate	Rs.	Qty	Rate	Rs.
1 Aug. 2014							40,000	70.00	2,800,000
12 Aug. 2014	20,000	75	1,500,000				60,000	71.67	4,300,000
15 Aug. 2014				30,000	71.67	2,150,100	30,000	71.66	2,149,900
28 Aug. 2014	20,000	78	1,560,000				50,000	74.20	3,709,900
30 Aug. 2014				20,000	74.20	1,484,000	30,000	74.20	2,225,900

Value of ending inventory i.e. 30,000 units = Rs. 2,225,900

(b) Weighted average method (Periodic Inventory):

	Units	Rate	Rs.
1 August Inventory	40,000	70	2,800,000
12 August Purchase	20,000	75	1,500,000
28 August Purchase	20,000	78	1,560,000
	80,000	*73.25	5,860,000

Value of ending inventory i.e. 30,000 units (80,000 – 30,000 – 20,000) × 73.25 = 2,197,500

Answer 3 (a)

Quality Products

Valuation of Closing Inventory

Closing inventory at lower of cost or NRV, using – Weighted average cost using perpetual inventory system

Date		Received			Issues			Balance		
		Qty.	Rate	Rs.	Qty.	Rate	Rs.	Qty.	Rate	Rs.
1-Jan-16	Balance							10,000	148.00	1,480,000
6-Jan-16	Purchases	15,000	150.00	2,250,000				25,000	149.20	3,730,000
10-Jan-16	Sales				(18,000)	149.20	(2,685,600)	7,000	149.20	1,044,400
16-Jan-16	Purchases	13,000	160.00	2,080,000				20,000	156.22	3,124,400
18-Jan-16	Purchase Return	(1,000)	150.00	(150,000)				19,000	156.55	2,974,400
25-jan-16	Sales				(12,000)	156.55	(1,878,600)	7,000	156.54	1,095,600
28-Jan-16	Drawings	(2,000)	156.54	(313,080)				5,000	156.54	782,720
29-Jan-16	Purchases	10,000	140.00	1,400,000				15,000	145.51	2,182,720
31-Jan-16	Shortages	(800)	145.51	(116,408)				14,200	145.51	2,066,312

	Qty	Cost per Unit	NRV Per Unit	Closing Inventory at Lower of cost of NRV (Rs.)
Good units (14,200-1,200)	13,000	145.51	200.00	1,891,630
Damaged units	1,200	145.51	120.00	144,000
	14,200			2,035,630

Note: in case of perpetual weighted average system, average rate is calculated after every purchase and purchase return.

A. 3 (b)

Quality Products: [Perpetual Inventory System] FIFO

Date	Description	Receipts			Issuances			Balance		
1-1-2016	Balance							10,000	148	1,480,000
6-1-2016	Purchases	15,000	150	2,250,000				10,000 15,000	148 150	1,480,000 2,250,000
10-1-2016	Sales				10,000 8,000	148 150	1,480,000 1,200,000	7,000	150	1,050,000
16-1-2016	Purchases	13,000	160	2,080,000				7,000 13,000	150 160	1,050,000 2,080,000
18-1-2016	Purchase Return	(1,000)	150	150,000				6,000 13,000	150 160	900,000 2,080,000
25-1-2016	Sales				6,000 6,000	150 160	900,000 960,000	7,000	160	1,120,000
28-1-2016	Drawings	(2,000)	160	(320,000)				5,000	160	800,000
29-1-2016	Purchases	10,000	140	1,400,000				5,000 10,000	160 140	800,000 1,400,000
31-1-2016	Shortage	(800)	160	(128,000)				4,200 10,000	160 140	800,000 1,400,000

Valuation of Closing Stock

	Units	Cost/Unit	NRV/Unit	Total
Damaged Units	1,200	160	120	144,000
Good Units	3,000	160	200	480,000
Good Units	10,000	140	200	1,400,000
				2,024,000

A. 3 (c)

Quality Products:

Periodic Inventory System (Weighted Average): [Average rate is calculated at the end of the period on the basis of purchases and purchase returns]

		Units	Rate	Amount
Opening Stock		10,000	148	1,480,000
6th January	Purchase	15,000	150	2,250,000
16th January	Purchases	13,000	160	2,080,000
18th January	Purchases Return	(1,000)	150	(150,000)
29th January	Purchase	10,000	140	1,400,000
		37,000		5,580,000

$$\text{Rate} = \frac{1{,}480{,}000 + 5{,}580{,}000}{10{,}000 + 37{,}000} = 150.21/\text{unit}$$

Cost of Drawings: 2,000 × 150.21 = 300,420

Cost of Shortage: 800 × 150.21 = 120,168

Cost of Closing Stock: 14,200 × 150.21 = 2,132,982

Valuation of Closing Stock:

	Units	Cost/Unit	NRV/Unit	Total
Damaged Units	1,200	150.21	120	144,000
Good Units	13,000	150.21	200	1,952,730
				2,096,730

A. 3 (d)

Quality Products:

Periodic Inventory System [FIFO]:

Stock In hand 14,200 units

	Units	Cost/Unit	NRV/Unit	Total
Good Units	10,000	140	200	1,400,000
Good Units	3,000	160	200	480,000
Damaged Units	1,200	160	120	144,000
	14,200			**2,024,000**

Answer 4

i)

Inventory A/c

1.1.04	b/d	160	16.8.04	Creditor (purchase return)	4,500
1.7.04	Creditor	30,000	19.8.04	Cost of sale a/c (sales)	16,000
15.8.04	Creditor	25,000	20.9.04	Cost of sales a/c (sales)	7,000
12.12.04	Cost of sale a/c (sale return)	3,000	31.12.04	c/d (bal.)	30,660

Cost of sales a/c

19.8.04	Inventory a/c	16,000	12.12.04	Inventory a/c	3,000
20.9.04	Inventory a/c	7,000	31.12.04	c/d	20,000

ii) Journal entries

1.7.04	Inventory a/c	30,000	
	Creditor a/c		30,000
	(Goods purchased)		
15.8.04	Inventory a/c	25,000	
	Creditor a/c		25,000
	(Goods purchased)		
16.8.04	Creditor a/c	4,500	
	Inventory a/c		4,500
	(Good returned by us)		
19.8.04	Debtor a/c	25,000	
	Sales a/c		25,000
	(Goods sold)		
	Cost of sales a/c	16,000	
	Inventory a/c		16,000
	(Goods sold)		
20.9.04	Debtor a/c	9,000	
	Sale a/c		9,000
	(Goods sold)		
	Cost of sales a/c	7,000	
	Inventory a/c		7,000
	(Goods sold)		
12.12.04	Sale Return	4,000	
	Debtor		4,000
	(Sale return)		
	Inventory a/c	3,000	
	Cost of sales a/c		3,000
	(Sale return)		

Answer 5

Max Savings
Journal entries to record transactions using perpetual inventory

Date	Description	Debit	Credit
		Rupees	
04-Aug-2017	Inventory Cash (To record cash purchases)	568,000	568,000
07-Aug-2017	Account receivables Sales	2,418,000	2,418,000
	Cost of sales (2,418,000 ÷ 1.3) Inventory (To record sales and cost of sales)	1,860,000	1,860,000
10-Aug-2017	Account payables Inventory (To record goods returned to a supplier)	87,000	87,000
13-Aug-2017	Inventory Account payables (to record purchase of inventory)	2,360,000	2,360,000
13-Aug-2017	Inventory Cash/bank (To record carriage-inward)	48,000	48,000
20-Aug-2017	Sales return/Return inward Account receivables	58,500	58,500
	Inventory (58,500 ÷ 1.3) Cost of sales (To record sales return)	45,000	45,000
24-Aug-2017	Cash Sales	120,000	120,000
	Cost of sales (120,000+10,000)÷1.3 Inventory (To record sales and cost of sales)	100,000	100,000
31-Aug-2017	Abnormal loss (26,000÷1.3) Inventory (Inventory shortages)	20,000	20,000

Answer.6

(a) (i) By FIFO

Cost of Sales

Opening Stock (300 × 22)	6,600
Purchases	29,600
Closing Stock (W-1)	(10,400)
Cost of Sales	25,800

W-1

Closing Stock

Units = 300 + 1,200 – 1,100

Units = 400

Cost = 400 × 26

Cost = 10,400

Since estimated selling price is higher, NRV should be higher unless there are selling expenses.

(ii) By Weighted Average:

Date	Receipt			Sold			Balance		
	Qty	Rate	Amount	Qty	Rate	Amount	Qty	Rate	Amount
Jan. 1							300	22	6,600
Jan. 10	400	23	9,200				700	22.57	15,800
Jan. 14				500	22.57	11,285	200	22.571	4,514
Jan. 20	400	25	10,000				600	24.19	14,514
Jan. 21				500	24.19	12,095	100	24.19	2,419
Jan. 25	400	26	10,400				500	25.638	12,189
Jan. 28				100	25.638	2,563.8	400	25.638	**10,255**
Total	**1,200**		**29,600**			**30,159**			

Cost of Sales = 30,159

Cost of Closing Stock = 10,255

Since estimated selling price is higher, NRV should be higher unless there are selling expenses.

Test

Question No. 1

Galaxy Enterprises (GE) maintains a bank account with Zee Bank Limited. Following information pertains to the bank account for the month of January 2016:

	Bank book	Bank statement
Balance as at 31 January 2016	(Dr.) Rs. 856,000	(Cr.) Rs. 1,182,500

Other information:

(i) Following is the list of outstanding cheques as at 31 January 2016:

Cheque no.	Date	Rupees
111	14-Jul-2015	250,000
444	23-Nov-2015	79,000
666	15-Dec-2015	455,000
777	28-Jan-2016	500,000
Various	31-Jan-2016	1,350,000

Review of outstanding cheques revealed that incorrect payee's name was mentioned on cheque no. 666. Cheque no. 777 was issued to replace cheque no. 666. The difference of Rs. 45,000 represents payment against another invoice.

(ii) Cheques outstanding for more than six months are not honoured by banks.

(iii) Details of un-cleared cheques as at 31 January 2016 are as follows:

Date	Customer's name	Cheque no.	Rupees
8-Oct-2015	Zeta Enterprises	1XX	140,000
3-Dec-2015	XYZ Traders	2XX	70,000
26-Dec-2015	ABC & Co.	3XX	63,000
31-Jan-2016	Various customers	Various	1,780,000

- Cheque no. 1XX was dishonoured on 28 January 2016.
- Cheque no. 2XX was mistakenly credited by the bank to another party. GE's account was however credited on 8 February 2016.

(iv) A debit of Rs. 135,000 is appearing in the bank statement of January 2016. It represents reversal of a credit given in December 2015 against a post-dated cheque of 1 March 2016 which was mistakenly deposited by GE.

(v) A reconciling item of Rs. 9,000 is appearing in the bank reconciliation statement from December 2015. it represents the difference between a cheque of Rs. 54,000 received from a customer and recorded by GE at Rs. 45,000. The error could not be identified in December 2015.

(vi) Following debit advices dated 29 January 2016 were received by GE in February 2016:

- Bank charges amounting to Rs. 8,500.
- Payments of Rs. 120,000 for annual subscriptions against standing instructions.

Required:

(a) Compute corrected Bank book balance and prepare necessary journal entries to correct the errors in the Bank book. **(11)**

(b) Prepare a bank reconciliation statement for the month of January 2016. **(03)**

Question No. 2

AK Limited follows a perpetual inventory system. Following information is available from the accounting records for the month of January 2016:

	Quantity	Amount (Rs.)
Inventory as at 31 December 2015	3,500	35,000
Purchase on 7 January 2016	3,700	44,400
Purchase on 13 January 2016	4,200	58,800
Purchase on 31 January 2016	2,000	26,000
Sale on 12 January 2016	3,000	60,000
Sale on 25 January 2016	5,500	115,500

Additional information:

100 units out of 4,200 units purchased on 13 January 2016 were found defective and returned to supplier on 28 January 2016.

Required:

Prepare inventory ledger cards for the month of January 2016 under the perpetual system showing quantity, unit cost and value under each of the following basis of inventory valuation:

(a) FIFO

(b) Weighted average

Answer No. 1

Galaxy Enterprises (a)

Cash Book

b/d	856,000	Debtor	140,000
Creditors	250,000	Debtor	135,000
Creditors	455,000	Bank Charges	8,500
Debtors	9,000	Subscription	120,000
		c/d	1,166,500

Correction Journal Entries for the Month of January 2016

Date	Description	Debit	Credit
31-01-2016	Bank Accounts payable (reversal of time barred cheque # 111)	250,000	250,000
31-01-2016	Bank Accounts payable (reversal of cheque # 666 issued with an incorrect name)	455,000	455,000
31-01-2016	Account receivable Bank (reversal of dishonoured cheque # 1XX)	140,000	140,000
31-01-2016	Accounts Receivable Bank (reversal of post-dated cheque of 1 March 2016 mistakenly presented to the bank in Dec. 2015)	135,000	135,000
31-01-2016	Bank Accounts Receivable (Correction of a Customer's cheque of Rs. 54,000 mistakenly recorded as Rs. 45,000)	9,000	9,000
31-01-2016	Bank Charges Subscription Charges Bank (to record bank charges and annual subscription paid)	8,500 120,000	128,500

(b) Bank Reconciliation Statement for the Month of January 2016

		Rupees (Dr.)/Cr.	
Bank balance as per bank statement		1,182,500	Cr.
Less:	Cheque issued but not presented for payments:		
	444	(79,000)	Dr.
	777	(500,000)	Dr.
	Various	(1,350,000)	Dr.
Add:	Cheque deposited into the bank not yet cleared:		
	Amount not credited	70,000	Cr.
	3XX	63,000	Cr.
	Various	1,780,000	Cr.
Corrected bank book balance		1,166,500	

Answer No. 2

(a) Inventory Ledger Card (FIFO)

Date	Purchases			Sale			Balance		
	Quality	Rate	Total	Quality	Rate	Total	Quality	Rate	Total
1/1/2016							3,500	10	35,000
7/1/2016	3,700	12	44,400				3,500 3,700	10 12	35,000 44,400
12/1/2016				3,000	10	30,000	500 3,700	10 12	5,000 44,400
13/1/2016	4,200	14	58,800				500 3,700 4,200	10 12 14	5,000 44,400 58,800
25/1/2016				500 3,700 1,300	10 12 14	5,000 44,400 18,200	2,900	14	40,600
28/1/2016	(100)	14	(1,400)				2,800	14	39,200
31/1/2016	2,000	13	26,000				2,800 2,000	14 13	39,200 26,000

(b) Inventory Ledger Card (Weighted Average)

Date	Purchases			Sale			Balance		
	Quality	Rate	Total	Quality	Rate	Total	Quality	Rate	Total
1/1/2016							3,500	10	35,000
7/1/2016	3,700	12	44,400				7,200	11.03	79,400
12/1/2016				3,000	11.03	33,083	4,200	11.03	46,317
13/1/2016	4,200	14	58,800				8,400	12.51	105,117
25/1/2016				5,500	12.51	68,826	2,900	12.51	36,290
28/1/2016	(100)	14	(1,400)				2,800	12.46	34,890
31/1/2016	2,000	13	26,000				4,800	12.46	60,890

Inventory Extra practice questions:

Question 1

A company deals in Solar Panels which are imported from China. The company follows a perpetual inventory system and values its inventory on weighted average basis. Details of sales and purchases during the year ended 30 June 2015 are as follows:

(i) Opening inventory on 1 July 2014 amounted to Rs. 49,000,000 and consisted of 2,450 solar panels.

(ii) Purchases during the year were as follows:

Date	Quantity (Units)	Price (Rs. In '000')
30-Sep-2014	4,200	87,494
31-Mar-2015	4,350	97,440

(iii) Sales during the year were as follows:

Date	Quantity (Units)	Price (Rs. In '000')
31-Jul-2014	2,100	52,500
31-Oct-2014	2,050	48,750
28-Feb-2015	2,300	55,200
15-May-2015	2,260	53,110

(v) On 31 May 2015, 50 solar panels were totally damaged and were written off (means record as a loss).

(vi) On 30 June 2015 there was a significant decline in the prices of solar panels as a new type of solar panel was introduced in the market. Selling prices are now Rs. 18,500 per unit. However, the company has decided to make some modification in its product which will enable it to sell it at Rs. 22,000 per unit. Cost of modification will be Rs. 2,500 per unit.

Required:

Compute the value of closing inventory as on 30.06.2015.

Question 2

A company deals in imported equipment. The management follows periodic inventory system to maintain and update its inventory records, and values its stock on weighted average.

The following information pertains to the year ended 31 December 2016.

- Opening inventory amounted to Rs. 12,000,000 and consisted of 600 units.
- Purchases during the year were:

Date	Units	Per Unit
31-Mar-16	300	21,500
16-Jun-16	300	22,000
31-Oct-16	400	23,000

- Sales during the year were as follows:

Date	Units	Rate/Unit
25-Feb-16	420	30,000
15-Jul-16	340	30,000
2-Sep-16	390	30,000

- On 10 April 2016, 50 units from the purchase on 31 March were found to be damaged and returned to the supplier.
- During the year, 80 units were damaged in an accident in the warehouse and were written off.
- 75 units were returned by a customer on 25 September, from the sale made on 2 September 2016:
- During the stock count conducted on 31 December 2016, it was found that 100 units were slightly damaged with an estimated selling price of 50% of the normal selling price. Estimated repair charges are Rs. 5,000 per unit.

Required:

(a) Value of inventory to be disclosed in the financial statements on 31 December 2016. **(07)**

(b) Pass necessary journal entry for the loss of inventory. **(02)**

Q. 3

Multan Traders (MT) held 200 units of product A valued at Rs. 175 each on 1 December 2018. Following transactions related to product A have occurred during December 2018:

Date	Description
7	Purchased 400 units from Alpha on credit for Rs. 80,700. Alpha gave further 50 units at no cost under a promotion scheme.
13	Sold 360 units on cash for Rs. 72,000.
16	Purchased 500 units from Bravo on credit for Rs. 89,000. MT also incurred transportation cost of Rs. 1,580.
21	Sold 440 units for Rs. 92,400 on credit to Charlie. To avail the 5% discount on early payment, Charlie paid the amount on 24 December 2018.
25	Purchased 350 units from Delta on credit. Delta offered discount of 8% on list price of Rs. 200 per unit if at least 250 units were purchased. Delta also offered further 2% discount if payment was made within 10 days.
27	30 units were found in unsaleable condition and were removed from the inventory.
28	Sold 300 units on cash for Rs. 61,000. MT incurred cost of Rs. 1,600 for delivery.

MT follows weighted average method for valuation of its inventory.

Required:

(a) Prepare inventory ledger card for product A for the month of December 2018 under perpetual inventory system. (09)

(b) Compute gross profit on sale of product A for December 2018. (02)

Solutions:

Answer 1

	2015
Value of Closing stock	43,680

Workings:

Rs. In '000'

Date	Purchases / receipts			Sales/Issuance			Balance		
	Qty	PUC	Value	Qty	PUC	Value	Qty	PUC	Value
1-7-14							2,450	20.000	49,000
31-7-14				2,100	20.000	42,000	350	20.000	7,000
30-9-14	4,200	20.832	87,494				4,550	20.768	94,494
31-10-14				2,050	20.768	42,574	2,500	20.768	51,920
28-2-15				2,300	20.768	47,766	200	20.768	4,154
31-3-15	4,350	22.400	97,440				4,550	22.328	101,594
15-5-15				2,260	22.328	50,462	2,290	22.328	51,132
31-5-15	(50)	22.328	(1,116)				2,240	22.328	50,015
Total	**8,500**		**183,818**	**8,710**		**182,802**			

Net Realizable Value

		Rs. '000'
Estimated selling price	(22 × 2,240)	49,280
Less: Estimated cost of completion/repair	(2.5 × 2,240)	(5,600)
		43,680

Loss due to lower NRV is (50,015 – 43,680) 6,335

Cost of sales:

	Rs. '000'
Opening stock	49,000
Purchases (87,494 + 97,440 -1,116)	183,818
Closing stock	(43,680)
	189,138

***Or** [42,000 + 42,574 + 47,766 + 50,462 + 6,335 (loss of NRV)] = 189,138*

***Note:** cost of sales are increased by 6,337 which is loss due to lower NRV. This loss is to be recorded immediately.*

***If* Periodic Inventory System: (Weighted Average Method)**

Value of closing stock (W 1) 43,680

Loss due to lower NRV [47,645 – 43,680] = 3,965

W 1

$$= \left[\frac{49{,}000 + 87{,}494 + 97{,}440}{2{,}450 + 4{,}200 + 4{,}350}\right]$$

$$= \frac{233{,}934}{11{,}000} = 21.27/\text{unit}$$

Cost of Closing Stock = 2,240 × 21.27 = 47,645

Net Realizable Value

		Rs. '000'
Estimated selling price	(22 × 2,240)	49,280
Less: Estimated cost of completion/repair	(2.5 × 2,240)	(5,600)
		43,680

Cost of damaged goods = 50 × 21.27 = 1,064.5

Cost of Sales:

Opening Stock	49,000
Add Purchases [87,494 + 97,440 – 1,064.5]	183,869
Less Closing Stock	(43,680)
	189,189

Answer 2

(a) Cost of Closing Stock

Weighted average cost per unit – Opening stock (Rs.) + Purchases (Rs.) – Purchase returns (Rs.)/ Opening Units + Units Purchased – Units Returned

		Rs.	Units
Opening stock		12,000,000	600
Purchases	31-Mar-16	6,450,000	300
	16-Jun-16	6,600,000	300
	31-Oct-16	9,200,000	400
Purchase returns	(50*21,500)	(1,075,000)	(50)
Total		33,175,000	1,550

Per unit = 33,175,000/1,550

21,403

Value of closing stock

= 600 + 300 + 300 + 400 – 420 – 340 – 390 – 50 – 80 + 75 =	395		
Damaged units =	100		
Good units = 395 – 100 =	$\boxed{295}$		
			Rs.
Value of good units = 295 × 21,403 =			6,313,885
Value of damaged goods:			
Cost (100 x 21,403)			2,140,300
NRV per Unit:			
Estimated selling price (50% x 30,000)		15,000	
Less: Cost of repairs		5,000	
NRV		10,000	
Total NRV of damaged goods = 100 x 10,000 =			1,000,000
Total Value of closing inventory on 31 Dec. (6,313,885 + 1,000,000)			7,313,885

(b)

Cost of inventory lost in an accident = 80 x 21,403 =		1,712,240
Journal Entry:		
Loss of stock	1,712,240	
Purchases		1,712,240

Ans. 3 Multan Traders

(a) Inventory ledger card - weighted average

Date		Receipts			Issues			Balance		
		Unit	Rate	Amount	Unit	Rate	Amount	Unit	Rate	Amount
01	Balance							200	175	35,000
07	Purchases	450	179.33	80,700				650	178	115,700
13	Sales				360	178	64,080	290	178	51,620
16	Purchases	500	181.16	90,580				790	180	142,200
21	Sales				440	180	79,200	350	180	63,000
25	Purchases	350	184	64,400				700	182	127,400
27	Unsaleable	(30)	182	(5,460)				670	182	121,940
28	Sales				300	182	54,600	370	182	67,340
		1,270		**230,220**	**1,100**		**197,880**			

(b)Gross Profit:	**Rupees**
Sales: (72,000 for 360 units)+(92,400 for 440 units)+(61,000 for 300 units)	225,400
Cost of goods sold	(197,880)
Gross profit	**27,520**

Property, Plant & Equipment [PPE] (IAS 16)

These are those tangible items that:

- Are **held for use** in business for production or supply of goods or for administrative purposes; and
- Are expected to be used during **more than on accounting period**.

⇒ The asset are capitalized and then depreciated over their useful life.

⇒ Examples of these assets include:

- Land & Building
- Plant & Machinery
- Furniture & Fixtures
- Motor Vehicles
- Computer Equipment etc

Depreciation is the systematic allocation of *depreciable amount* of an asset over its *useful life*.

Depreciable Amount = *Cost –Residual Value*

Cost means purchase price and all costs incurred in bringing the asset into working condition as intended by management.

Residual Value is the amount expected to be obtained from an asset at the end of its useful life.

Useful Life is the period over which asset is expected to be used by an entity.

Methods of depreciation:

➢ ***Straight line method:***

$$\text{Annual Depreciation} = \frac{\text{Cost} - \text{Residual Value}}{\text{Estimated useful life}}$$

or

$$\text{Rate of depreciation} = \frac{1}{\text{Useful life}} \times 100$$

In this method, depreciation will be same for every year.

➢ ***Reducing Balance method (Diminishing Balance Method):***

In this method, a rate of depreciation is calculated as follows:

$$\left[1 - \sqrt[n]{\frac{s}{c}}\right] \times 100$$

n = Useful Life

s = Scrap Value/ Residual Value

c = Cost of asset

- The rate will then be multiplied in first year on the cost of asset (without deducting residual value).
- From second accounting period onwards, rate of depreciation is multiplied with WDV at the beginning of the year, to calculate depreciation for the year.
- If however, a rate of depreciation is given then simply use that rate.

➢ ***Sum of year's digit method:***

Depreciation expense is calculated as follows:

$$\text{Sum of digits} = \frac{n(n+1)}{2}$$

n = *Useful life*

$$\text{Depreciation} = \frac{\text{Factor of current year}}{\text{Sum of digits}} \times [\text{cost} - \text{R.V}]$$

➢ ***Machine Hour method:***

$$\text{Machine Hour Rate} = \frac{cost - R.V}{\textit{Effective total working Hours}}$$

Depreciation for the year = Rate x Actual hours used during the period

➢ ***Production Units Method:***

$$\text{Production unit rates} = \frac{\text{Cost - R.V}}{\textit{Total Units to be produced}}$$

Depreciation for the year = Rate x Actual units produced during the period

Discussion of methods:

1. **Straight Line Method: (Fixed Instalment Method)**

Example:

Cost = 100,000
Residual Value = 20,000
Useful Life = 4 years
Date of Purchase = 01-07-2014
Accounting year end = 30-06-2015

$$\text{Depreciation} = \frac{100{,}000 - 20{,}000}{4} = 20{,}000/\text{Annum}$$

If depreciation is to be calculated by rate, then:

Rate = 1/4 × 100 = 25%
Depreciation = (Cost – Residual Value) × Rate
= (100 – 20,000) × 25%
= 20,000/Annum

2. **Reducing Balance Method: (Diminishing Balance Method)**

In this method, rate is always required; if not available then it can be calculated as follows:

$$\text{Rate} = 1 - n\sqrt{\frac{RV}{Cost}}$$

$$= 1 - 4\sqrt{\frac{20{,}000}{100{,}000}}$$

= 33.13%

Calculation of Depreciation:

		Depreciation	Accumulated Depreciation	Written Down Value (WDV)
30-06-2015	100,000 × 33.13%	33,125	33,125	66,875
30-06-2016	66,875 × 33.13%	22,152	55,277	44,723
30-06-2017	44,723 × 33.13%	14,814	70,091	29,909
30-06-2018	29,909 × 33.13%	9,907	79,998*	20,002
		79,998		

*At the end of the useful life:

(1) Accumulated Depreciation = Depreciable amount; or

(2) WDV = Residual Value

Accumulated Depreciation:

Means total depreciation that has been charged upto the period end.

3. Sum of Digits Method:

		Depreciation	Accumulated Depreciation	WDV
1	4/10 × (100,000 – 20,000) =	32,000	32,000	68,000
2	3/10 × (100,000 – 20,000) =	24,000	56,000	44,000
3	2/10 × (100,000 – 20,000) =	16,000	72,000	28,000
4	1/10 × (100,000 – 20,000) =	8,000	80,000	20,000
10				

4. Machine Hour Method:

Cost of Machine = 5,000,000

Residual Value = 200,000

Estimated Total Working Hours = 100,000

Actual hours Used During the year = 5,000

Depreciation / Hour = $\frac{5{,}000{,}000 - 200{,}000}{100{,}000}$ = 48 / hour

Depreciation for the year = 5,000 × 48 = 240,000

5. Production Units Method:

Cost of Machine = 1,000,000

Residual Value = 100,000

Estimated Total units of production = 10,000 Units

Actual units produced during the year = 1,000

Depreciation / Unit = $\frac{1{,}000{,}000 - 100{,}000}{10{,}000}$ = 90 / unit

Depreciation for the year = 1,000 × 90 = 90,000

Accounting Entries of Depreciation

If there is no separate ledger of account deprecation	If there is a separate ledger of account depreciation
Depreciation Xx Asset xx	Depreciation xx Accumulated Depreciation Xx
In this case closing balance in the ledger of asset will equal to WDV.	In this case closing balance in the ledger of asset will equal to cost.

Example:

Cost = 100,000

RV 20,000

Useful Life = 4 years

Purchased = 01-07-14

Nature of accumulated depreciation account is just like a purchase return account, sale return account and drawings account etc.

Suppose:

Purchases	500,000	
Creditor		500,000
Creditor	40,000	
Purchase Returns		40,000

Similarly, Accumulated depreciation account is prepared to reflect the decrease in the value of asset so that we have while having complete knowledge of cost, total depreciation & WDV of the asset.

Conclusion:

If question is silent, always use separate ledger of accumulated depreciation.

Depreciation Policy:

- **Time Basis:** in this method, depreciation is charged from the date of purchase to date of disposal (sale).
- **Full year Basis**: in this method, depreciation is charged for full year in the year of purchase, while no depreciation is charged in the year of disposal.

If the question is silent and the dates are available then always use policy of time basis.

Example:

Cost of Assets	=	400,000
Residual value	=	40,000
Date of purchase	=	1-7-2010
Useful life	=	10 years

Year ended 31st December

Time Basis:

Depreciation for the year ended 31st December = $\frac{400{,}000 - 40{,}000}{10}$ = 36,000 × 6/12 = 18,000

Full year Basis:

Depreciation for the year ended 31st December = $\frac{400{,}000 - 40{,}000}{10}$ = 36,000

Question bank:

1. AUBREY

Aubrey purchased a van for Rs.800 cash. He estimates that in four years it will have a scrap value of Rs.104.

Required:

Calculate the annual depreciation charge on

(a) the straight line method

(b) the reducing instalment method (you will need to calculate the rate).

2.SUNDRY DEPRECIATION PROBLEMS

a. The financial year of a company is 1st January to 31st December. A non-current asset was purchased on 1st May for Rs.60,000. Its expected useful life is five years and its expected residual value is zero. It is depreciated by the straight-line method.

Required:

Calculate the charge for depreciation in the year of acquisition if a proportion of a full year's depreciation is charged, according to the period for which the asset has been held.

b. An office property cost Rs.5 million, of which the land value is Rs.2 million and the cost of the building is Rs.3 million. The building has an estimated life of 50 years.

Required:

Calculate the annual depreciation charge on the property, using the straight-line method?

3.MATURIN

Maturin bought a machine for Rs.10,000 on 1 January 2012. He estimates a useful life of 8 years and a residual value of Rs.800. Depreciation is to be calculated on a straight line basis.

Required:

(a) Write up for 2012 and 2013 the

(i) Machinery account

(ii) Accumulated depreciation account

(iii) Depreciation expense account.

(b) Show how the machine would be presented in the statement of financial positions as at 31 December 2012 and 31 December 2013.

Notes:

The machinery account and accumulated depreciation accounts are statement of financial position items.

Depreciation account is an income statement item.

Important Points to remember:

- Opening Balances are only of Assets, Liabilities and Capital (SOFP items).
- Income Statement items (Incomes & Expenses) are for the period.

4. SOPHIE

Since he commenced business on 1 January 2010 Sophie has purchased for cash the following three machines.

	Date of purchase	Cost Rs.	Rate of depreciation
Machine 1	20 January 2010	4,200	25%
Machine 2	17 April 2011	5,000	30%
Machine 3	11 July 2012	3,500	35%

Sophie's policy is to charge a full year's depreciation in the year of purchase irrespective of the date of purchase. The reducing balance method is used to calculate depreciation.

Accounts are prepared to 31 December each year.

Required:

(a) Prepare the machinery account and accumulated depreciation account showing the charge to the depreciation account for each year.

(b) Show the relevant statement of financial position extracts for each year.

A.1

Straight Line = $\frac{\text{Cost} - \text{R.V}}{\text{Useful Life}} = \frac{800 - 104}{4} = 174$

Reducing Balance:

Rate $= \left[1 - \sqrt[n]{\frac{\text{R.V}}{\text{Cost}}}\right] \times 100$

$= \left[1 - \sqrt[4]{\frac{104}{800}}\right] \times 100$

= 40%

Calculation of depreciation	Depreciation	Accounting Depreciation	WDV
800 × 40%	320	320	480
480 × 40%	192	512	288
288 × 40%	115	627	173
173 × 40%	69	696	104

A.2. (a)

1-5-2000 60,000

$= \frac{60,000 - 0}{5} = 12,000 \times \frac{8}{12} = 8,000$

A.2. (b)

$= \frac{3,000,000}{50} = 60,000\text{/Annum.}$

A.3

Machinery Account

1-1-12	Cash	10,000			
				c/d	10,000
31-12-12		10,000			10,000
	b/d	10,000			
				c/d	10,000
		10,000			10,000

Accumulated Depreciation Account

			31-12-12	Depreciation	1,150
	c/d	1,150			
		1,150			1,150
				b/d	1,150
				Depreciation	1,150
	c/d	2,300			
		2,300			2,300

Depreciation Account

Acc. Depreciation	1,150			
			c/d (I/S)	1,150
	1,150			1,150
Acc. Depreciation	1,150			
			c/d (I/S)	1,150
	1,150			1,150

	Dr.	Cr.
Machinery	10,000	
Accumulated Depreciation		2,300
Depreciation	1,150	

Statement of Financial Position
As on 31-12-2012 (Extract)

Assets:

Machine (10,000 – 1,150) 8,850

Statement of Financial Position
As on 31-12-2013 (Extract)

Assets:

Machine (10,000 – 2,300) 7,700

A.4 (a)

Machinery Account

10-1-10	Cash	4,200			
				c/d	4,200
31-12-12		4,200			4,200
	b/d	4,200			
17-4-11	Cash	5,000			
				c/d	9,200
31-12-11		9,200			9,200
	b/d	9,200			
11-7-12	Cash	3,500			
				c/d	12,700
31-12-13		12,700			12,700

Accumulated Depreciation Account

c/d	1,050	31-12-10	Depreciation (W-I)	1,050
	1,050			1,050
			b/d	1,050
			Depreciation (W-II)	2,288
c/d	3,338			
	3,338			3,338
			b/d	3,338
			Depreciation (W-III)	2,866
c/d	6,204			
	6,204			6,204

(b) Statement of Financial Position (Extract)

For the year ended 31-12-2010

Assets:

Machinery (4,200 – 1,050) 3,150

Statement of Financial Position (Extract)

For the year ended 31-12-2011

Assets:

Machinery (9,200 – 3,338) 5,862

Statement of Financial Position (Extract)

For the year ended 31-12-2012

Assets:

Machinery (12,700 – 6,204) 6,496

Workings:

W-I Depreciation for 2010:

4,200 × 25% = 1,050

W-II Depreciation for 2011:

Machine # 1	= [4,200 – 1,050] x 25%	788
Machine # 2	5,000 × 30% =	1,500
		2,288

W-III Depreciation for 2012:

Machine # 1	= [4,200 – 1,050 – 788] x 25%	591
Machine # 2	(5,000 – 1,500) x 30%	1,050
Machine # 3	3,500 × 35% =	1,225
		2,866

DEPRICIATION
PRACTICE QUESTIONS

Question-1 (C.W)

Mr. Baber provided you with following information:

	Cost as on 1.1.2009	Accumulated Depreciation as on 1.1.2009	Rate S.L
Machinery	600,000	250,000	10%
Vehicle	700,000	90,000	20%

Following are the additions made during the year:

	Date of Purchase	Cost
Machinery	1.3.2009	90,000
Vehicle	1.5.2009	80,000
Vehicle	1.6.2009	100,000

Required: Prepare machinery A/C and vehicle A/C (cost and accumulated depreciation) for December 31, 2009 and December 31, 2010.

Question-2 (H.W)

Mr. Black has provided you with following information:

	Cost as on 1.1.2001	Accumulated Depreciation as on 1.1.2001	Rate S.L
Plant and Machinery	600,000	200,000	20%
Furniture	700,000	130,000	10%
Vehicle	800,000	170,000	25%

Following are the additions made in year ended December 31, 2001.

	Date	Cost
Plant and Machinery	1.1.2001	60,000
Furniture	1.6.2001	80,000
Vehicle	1.9.2001	70,000

Required:

Prepare Assets Accounts and Accumulated Depreciation A/C for year ended December 31, 2001 only.

Question-3

A Gill, purchased a notebook PC on 1.1.2005 for Rs. 2,600.It has an estimated life of four years and a scrap value of Rs. 200.

He is not certain whether he should use the straight line or the reducing balance basis for the purpose of calculating depreciation on the computer.

Required:

You are required to calculate the depreciation (to the nearest Rs.) using both methods, showing clearly the balance remaining in the computer account at the end of each of the four years under each method. (Assume that 45 per cent per annum is to be used for the reducing balance method).

Question-4

Mr. Taimoor has started the business on January 1, 2009 of manufacturing cars. He has disclosed the following data for first three years of his business operations which relates to additions in fixed assets:

	Date of Purchase	Cost
Year end December 31, 2009		
Asset-1	1.1.2009	30,000
Asset-2	1.7.2009	10,000
Year end December 31, 2010		
Asset-3	1.4.2010	50,000
Year end December 31, 2011		
Asset-4	1.7.2011	60,000

Method is WDV for depreciation and rate is 10%.

Requirement:

Prepare relevant accounts for years ended December 31, 2009, 2010 and 2011.\

Question-5 (C.W)

Mr. Wasif has informed you that following balances are appearing on 1.1.2013 in his books of accounts:

	Cost	Accumulated Depreciation
Building	400,000	150,000

Following is the detail of additions during the year ended December 31, 2013:

	Date of Purchase	Cost
Building – Defence	1.3.2013	300,000
Building – Green Town	1.8.2013	100,000

Method for depreciation is WDV and rate is 20%.

Requirement:

Prepare relevant accounts for year ended December 31, 2013.

Question-6 (H.W)

Mr. Ali has informed you that following balances are appearing on 1.1.2013 in his books of accounts:

	Cost	Accumulated Depreciation
Machinery a/c	600,000	300,000

Following is the detail of additions during the year ended December 31, 2013:

	Date of Purchase	Cost
Cutter machine	1.3.2013	500,000
Molding machine	1.8.2013	250,000

Method for depreciation is WDV and rate is 20%.

Requirement:

Prepare asset account and accumulated depreciation account for year ended December 31, 2013.

Question-7 (H.W)

Mr. Faiq has informed you that following balances are appearing on 1.1.2009 in his books of accounts:

	Cost	Accumulated Depreciation
Machinery a/c	600,000	200,000

Following is the detail of additions during the year ended December 31, 2009:

	Date of Purchase	Cost
Machinery B	1.3.2009	10,000
Machinery C	1.5.2009	70,000

Method for depreciation is WDV and rate is 30%.

Requirement:

Prepare relevant accounts for year ended December 31, 2009.

Question-8 (C.W)

Mr. Nasir has disclosed the following data:

	1.1.2009
Furniture – book value	25,000

Following transactions took place during the year ended December 31, 2009.

Additions	Cost	Date of purchase
	60,000	1.3.2009
	90,000	1.6.2009

Required:

Prepare asset A/C. Rate of depreciation is 20% W.D.V.

Question-9 (C.W)

Mr. Sannan has provided you with following information:

	Book value 1.1.07
Building	1,500,000

(i) Detail of addition for year ended Dec. 31, 2007

On February 01, 2007	400,000
On April 01, 2007	650,000

(ii) Depreciation rate is 10% on diminishing balance method.

Prepare building account for the year ended December 31, 2007.

Question-10

ABC Ltd. has a building A/c having book value of Rs. 700,000 on 1.1.2011. The depreciation is directly credited to asset a/c and no separate accumulated depreciation account is maintained.

During the year ended 31.12.2011, following transaction took place:

Additions of Rs. 80,000 took place on 1.3.2011.

Required:

Prepare relevant accounts assuming that rate is 30% WDV.

SOLUTIONS

Answer-1

Machinery a/c

Dr.					Cr.
1.1.09	b/d	600,000			
1.3.09	Cash	90,000	31.12.09	c/d	690,000
1.1.10	b/d	690,000			
			31.12.10	c/d	690,000

Accumulated Dep. a/c (Machinery)

Dr.				Cr.
		1.1.09	b/d	250,000
31.12.09 c/d	317,500	31.12.09	Depreciation Exp	67,500
		1.1.10	b/d	317,500
31.12.10 c/d	386,500	31.12.10	Depreciation Exp	69,000

Depreciation Machinery – 2009

On opening assets	(600,000 x 10%)	60,000
On addition	(90,000 x 10% x 10/12)	7,500
		67,500

Depreciation Machinery – 2010

On opening assets	(690,000 x 10%)	69,000

Vehicle a/c

Dr.					Cr.
1.1.09	b/d	700,000			
1.5.09	Cash	80,000			
1.6.09	Cash	100,000	31.12.09	c/d	880,000
1.1.10	b/d	880,000	31.12.10	c/d	880,000

Accumulated Dep. a/c

Dr.				Cr.
		1.1.09	b/d	90,000
31.12.09 c/d	252,334	31.12.09	Depreciation Exp	162,334
		1.1.10	b/d	252,334
31.12.10 c/d	428,334	31.12.10	Depreciation Exp	176,000

Depreciation - 2009	On opening	(700,000 x 20%)	140,000
	On addition	(80,000 x 20% x 8/12) + (100,000 x 20% x 7/12)	22,334
			162,334
Depreciation - 2010	On opening	(880,000 x 20%)	176,000

Answer-2

Plant and Machinery - At Cost

Dr.					Cr.
1.1.01	b/d	600,000			
1.1.01	Cash	60,000			
			31.12.01	c/d	660,000

Accumulated Depreciation - Plant and Machinery

Dr.				Cr.
		1.1.01	b/d	200,000
		31.12.01	Dep. Exp	132,000
31.12.01 c/d	332,000			

Depreciation:	On opening assets	(600,000 x 20%)	120,000
	On addition	(60,000 x 20%)	12,000
			132,000

Furniture – A/C

Dr.					Cr.
1.1.01	b/d	700,000			
1.6.01	Cash	80,000			
			31.12.01	c/d	780,000

Accumulated Depreciation – Furniture

Dr.					Cr.
			1.1.01	b/d	130,000
			31.12.01	Dep. Exp	74,667
31.12.01	c/d	204,667			

Depreciation:	On opening assets	(700,000 x 10%)	70,000
	On addition	(80,000 x 10% x 7/12)	4,667
			74,667

Vehicle a/c

Dr.					Cr.
1.1.01	b/d	800,000			
1.9.01	Cash	70,000			
			31.12.01	c/d	870,000

Accumulated Depreciation – Vehicle a/c

Dr.					Cr.
			1.1.01	b/d	170,000
			31.12.01	Dep. Exp	205,833
31.12.01	c/d	375,833			

Depreciation :	On opening	(800,000 x 25%)	200,000
	On addition	(70,000 x 25% x 4/12)	5,833
			205,833

Answer-3

Calculation of depreciation (Using straight line method)

Cost		2,600
Depreciation (2005)	(2,600 - 200) / 4	(600)
WDV		2,000
Depreciation (2006)	(2,600 - 200) / 4	(600)
WDV		1,400
Depreciation (2007)	(2,600 - 200) / 4	(600)
WDV		800
Depreciation (2008)	(2,600 - 200) / 4	(600)
WDV (31.12.2008)		**200**

Calculation of depreciation (Using write down value method)

Cost	2,600
Depreciation (2005)	(1,170)
WDV	1,430
Depreciation (2006)	(644)
WDV	786
Depreciation (2007)	(354)
WDV	432
Depreciation (2008)	(194)
WDV (31.12.2008)	**238**

Answer-4

Asset A/c

Dr.			Cr.		
1.1.09	b/d	-			
1.1.09	Cash	30,000			
1.7.09	Cash	10,000	31.12.09	c/d	40,000
1.1.10	b/d	40,000			
1.4.10	Cash	50,000	31.12.10	c/d	90,000
1.1.11	b/d	90,000			
1.7.11	Cash	60,000	31.12.11	c/d	150,000

Accumulated Depreciation

Dr.			Cr.		
			1.1.09	b/d	-
31.12.09	c/d	3,500		Depreciation expense	3,500
			1.1.10	b/d	3,500
31.12.10	c/d	10,900		Depreciation expense	7,400
			1.1.11	b/d	10,900
31.12.12	c/d	21,810		Depreciation expense	10,910

Calculation for Depreciation

Depreciation for 2009

On additions	(30,000 x 10%) + (10,000 x 10% x 6/12)	3,500

Depreciation for 2010

On opening assets	(40,000 – 3,500) x 10%	3,650
On additions	(50,000 x 10% x 9/12)	3,750
		7,400

Depreciation for 2011

On opening assets	(90,000 – 10,900) x 10%	7,910
On additions	(60,000 x 10% x 6/12)	3,000
		10,910

Answer-5

Building a/c

Dr.			Cr.		
1.1.13	b/d	400,000			
1.3.13	Cash	300,000			
1.8.13	Cash	100,000	31.12.13	c/d	800,000

Accumulated Depreciation

Dr.			Cr.		
			1.1.13	b/d	150,000
31.12.13	c/d	258,333		Depreciation expense	108,333

Calculation for Depreciation

On opening assets	(400,000 – 150,000) x 20%	50,000
On additions during the year	(300,000 x 20% x 10/12) + (100,000 x 20% x 5/12)	58,333
		108,333

Answer-6

Dr.		Asset a/c			Cr.
1.1.13	b/d	600,000			
1.3.13	Cash	500,000			
1.8.13	Cash	250,000	31.12.13	c/d	1,350,000

Dr.		Accumulated Depreciation			Cr.
			1.1.13	b/d	300,000
31.12.13	c/d	464,167		Depreciation expense	164,167

Calculation for Depreciation

- On opening assets	(600,000 – 300,000) x 20%	60,000
- On additions	(500,000 x 20% x 10/12) + (250,000 x 20% x 5/1/2)	104,167
		164,167

Answer-7

Dr.		Machinery a/c			Cr.
1.1.09	b/d	600,000			
1.3.09	Cash	10,000			
1.5.09	Cash	70,000	31.12.09	c/d	680,000

Dr.		Accumulated Depreciation			Cr.
			1.1.09	b/d	200,000
31.12.09	c/d	336,500		Depreciation expense	136,500

Calculation for Depreciation expense

- On opening assets	(600,000 – 200,000) x 30%	120,000
- On additions	(10,000 x 30% x 10/12) + (70,000 x 30% x 8/12)	16,500
		136,500

Answer-8

Dr.		Furniture – Book value			Cr.
1.1.09	b/d	25,000			
1.3.09	Cash	60,000	Depreciation	(W-1)	25,500
1.6.09	Cash	90,000	c/d		149,500

(W-1) Depreciation expense

- Opening assets	25,000 x 20%	5,000
- On addition	(60,000 x 20% x 10/12) + (90,000 x 20% x 7/12)	20,500
		25,500

Answer-9

	Dr.	Building – BV		Cr.
	b/d	1,500,000		
1.2	Cash	400,000		
1.4	Cash	650,000	Depreciation Expense(W-1)	235,417
			c/d	2,314,583

Workings

(W-1) Depreciation Expense

- On opening assets (1,500,000 x 10%)	150,000
- On addition (400,000 x 10% x 11/12) + (650,000 x 10% x 9/12)	85,417
	235,417

Answer-10

Building A/c – at BV

Dr.					Cr.
1.1.11	b/d	700,000			
1.3.11	Cash	80,000	Depreciation	(W-1)	230,000
			c/d	(bal.)	550,000

(W-1) Depreciation expense

- Opening assets	(700,000 x 30%)	210,000
- On addition	(80,000 x 30% x 10/12)	20,000
		230,000

Cost of Purchase of a Non-Current Asset:

All amount incurred to bring the asset into working condition as intended by management of business are added to the cost of Asset: (means capitalized to the Cost of Asset)

Purchase Price	Xx
Add Carriage Inwards	Xx
Add Custom duty	Xx
Add Assembly cost	xx
Add Installation / wiring	xx
Cost of Asset	xx

Expenditures

Capital Expenditures	**Revenue Expenditures**
Expenditure which has a useful life of more than one accounting period.	Expenditures which benefit the business upto one accounting period.
Accounting Treatment:	**Accounting Treatment:**
Record these expenditures as an asset and then depreciate them over their useful life.	Record these expenditures as an expense in the period in which they are incurred.
Example:	**Example:**
Land, Building, Vehicle, Machinery etc. However land is generally not depreciated because it has an indefinite useful life.	Salaries, Rent, Utilities, Advertisement, Stationary etc.

Conclusion:

⇒ Capital Expenditure are Capitalized (means recorded as an asset) and Revenue expenditures are expensed out (means recorded) as an expense.

Important point to remember:

Repairs of an asset are always considered as a revenue expense unless it is mentioned that it will improve efficiency or the benefit the business for more than me accounting period.

TIME LIFE ENTERPRISES

The draft statement of financial position of Time Life Enterprises (TLE) as on December 31, 2013, depicts the following:

	Rupees
Plant and Machinery – Cost	12,387,060
Less: Accumulated Depreciation	4,792,540
	7,594,520

On reviewing the accounts of the business, its auditor found that the records have been correctly maintained except for the following events:

(i) On January 17, 2013 a contract was signed for the purchase of a machine from Makers Limited for Rs. 1,125,000 which is to be delivered on July 17, 2014. TLE paid an advance of Rs. 450,000 on the signing of the contract and the balance was to be paid on delivery of the machine. The advance was debited to plant and machinery account.

(ii) Installation of a machine was completed on January 21, 2013. The cost of machine of Rs. 2,700,000 was debited to plant and machinery account. The cost of installation amounting to Rs. 300,000 had been debited to Repairs Account.

Depreciation is charged on a reducing balance method at 10% per annum. Depreciation on new assets commences in the month in which the asset is acquired.

The depreciation expense for the year 2013 have been correctly calculated and recorded except for the impact of errors discussed above.

Required:

Determine the correct balances as at December 31, 2013 by recording appropriate adjustments in the following accounts:

(a) Plant and machinery

(b) Accumulated depreciation - plant and machinery

A.

Plant	450,000		(Posted entry)
Cash		450,000	
Advance to Supplier	450,000		(Required entry)
Cash		450,000	
Advance to Supplier	450,000		(Rectifying entry)
Plant		450,000	

Repairs	300,000		Plant & Machinery	300,000		Plant & Machinery	300,000	
Cash		300,000	Cash		300,000	Repairs		300,000
(Posted)			(Required)			(Rectifying)		

Plant & Machinery Account (Adjusted)

Unadjusted balance	12,387,060	Advance	450,000
Repairs	300,000		
		c/d (adjusted)	12,237,060
	12,687,060		12,687,060

Accumulated Depreciation Account (Adjusted)

Depreciation (W)	45,000	Unadjusted balance	4,792,540
		Depreciation (W)	30,000
c/d (adjusted)	4,777,540		
	4,822,540		4,822,540

Workings:

Depreciation Adjustments:

450,000 × 10% = 45,000 (to be reversed)

Accumulated Depreciation	45,000	
Depreciation		45,000

300,000 × 10% = 30,000 (to be charged)

Depreciation	30,000	
Accumulated Depreciation		30,000

DISPOSAL / SALE OF ASSET

Machine

Cost	=	750,000
Accumulated Depreciation =	600,000	
Written down value	=	150,000

Suppose this machine is now sold for 180,000.

Gain / Loss	=	different between WDV and Sale proceeds.
	=	180,000 – 150,000
Gain	=	30,000

ACCOUNTING ENTRIES OF DISPOSAL

(a) Calculating Gain / Loss by Entries

If there is no separate ledger accumulated depreciation			If there is a separate ledger of accumulated depreciation		
Cash	130,000		Cash	180,000	
Machine (At WDV)		150,000	Account Depreciation	600,000	
Gain (Bal.)		30,000	Machine (At Cost)		750,000
			Gain (Bal.)		30,000
Difference in this entry is gain or loss to be recognised in Income Statement			Difference in this entry is gain or loss to be recognized in Income Statement		

(b) Calculating Gain / Loss by Disposal Account

It is a ledger which is used to calculate the gain or loss on disposal of an asset.

Disposal Account (if asset account is at WDV)

Machine	150,000	Cash	180,000
Gain (I/S)	30,000		

Disposal Account(if asset account is at cost)

Machine	750,000	Cash	180,000
		Accumulated Depreciation	600,000
Gain (I/S)	30,000		

SUMMARY OF ACCOUNTING ENTRIES IF A DISPOSAL ACCOUNT IS REQUIRED TO BE PREPARED

No separate ledger of accumulated depreciation			Separate ledger of accumulated depreciation		
Cash	XX		Cash	XX	
Disposal A/c		XX	Disposal A/c		XX
Disposal A/c	XX		Disposal A/c	XX	
Machine (At WDV)		XX	Machine (At Cost)		XX
			Acc Depreciation	XX	
			Disposal A/c		XX

Q. 1 The Machinery Account (at Cost) of a firm for the three years ended December 31, 2014 appears as follows

Machinery

2012		**2012**	
Jan 1 to Cash (No-1)	50,000	Dec 31 Balance c/d	50,000
	50,000		50,000
2013		**2013**	
Jan 1 Balance b/d	50,000		
July 1 to Cash (No-2)	20,000	Dec 31 Balance c/d	70,000
	70,000		70,000

2014			2014		
Jan 1	Balance b/d	70,000			
July 1	to Cash (No-3)	15,000	Dec 31	Balance c/d	85,000
		85,000			85,000

Depreciation @20% on the diminishing value basis was accumulated in provision for depreciation Account

On October 1, 2015 machines # 2 was damaged and has to be replaced by a new machine costing Rs. 25,000 . The Machine was insured and insurance claim of Rs. 12,400 was received.

Required:

Prepare the 2015 Machinery Account, Provision for Depreciation Account and machinery disposal Account. All workings are to be shown. Depreciation is provided on time basis.

Note: Provision for depreciation account is another name of accumulated depreciation account.

Q.2 A Company charges depreciation on Plant and Machinery under reducing balance method at the rate of 15% p.a. On 1st April 1997, the balance in the ledger stood as 460,000 (WDV). The following particulars are given relating to the plant and machinery during the four years ending 31 March 2001.

Date	
1-Sep-1997	A Machine purchased for Rs. 21,000 on 1 May 1995 was fully destroyed in an accident
1-Jul-1998	A new Machine was purchased costing 52,500. A sum of Rs .30,000 was paid on the same date and remaining balance was paid in May 1999
31-Aug-1999	Plant Purchased on 1st April 1996 for Rs. 31,500 was disposed of for Rs. 36,000
1-Nov-2000	Some old Machine having book value of Rs 10,000 on 1st April1997 was sold for Rs. 4,000

Required:

Prepare plant and machinery account for four years ending 31 March 2001.

Q. 3 A trading organisation charges depreciation on its plant and machinery on a reducing balance method @ 15% per annum. On 1 July 2011, the net book value in the ledger stood at Rs. 5,660,000. Movements in the plant and machinery account during the two years ended 30 June 2013 were as follows:

Date	Particulars
1 October 2011	A new machine costing Rs. 80,000 was purchased. A sum of Rs. 30,000 was paid on the same date and the balance was paid on 31 March 2012.
1 December 2011	A machine that was purchased for Rs. 200,000 and installed at a cost ofRs. 10,000 on 1 August 2009 was fully destroyed in an accident.
1 February 2012	Some old machinery (book value on 1 July 2011 Rs. 20,000) was sold for Rs. 8,000.
30 November 2012	A machine imported on 1 July 2010 was disposed of for Rs. 63,000. The value of machine was Rs. 70,000 whereas import levies amounted to Rs. 5,000.

Required:

Prepare the plant and machinery account for the years ended 30 June 2012 and 2013. **(19)**

Q-4 Following is the extract from the Balance Sheet of Tayab Limited as on 31.12

	Rupees	
	2004	**2003**
Fixed Assets (at cost)	684,500	518,000
Less: Accumulated depreciation	249,750	277,500
Net Book Value	434,750	240,500

During the year 2004:

(i) Additions in fixed assets was	481,000
(ii) Loss on sale of old fixed assets was	92,500
(in) Depreciation provided for the year was	138,750

Required:

Determine the amount of sale proceeds received on the disposal of fixed assets during the year 2004.

Q.5 The following balances are appearing in the books of Faizan Ahmad & Co. as at 31st December 2015

	Rs.
Machinery – Cost	12,500,000
Machinery -Acc. Depreciation	2,505,000

Following additional information related to the year ended 31st December 2016 is also available:

(i) On 1st July 2016, second hand machinery was purchased for Rs. 900,000. An amount of Rs. 100,000 was spent on its overhauling before use. Overhauling was necessary to bring it to working condition.

(ii) On 1st August 2016, the machinery purchased on 1st June 2013 for Rs. 225,000 was destroyed by fire and claim of Rs. 65,000 was received in cheque from JJ Insurance Company.

(iii) Machinery purchased on 1st January 2014 for Rs. 435,000 was sold on 30th November 2016 at Rs. 140,000 in cash.

(iv) Faizan Ahmad & Co. provides depreciation on machinery @ 10% on written down value.

(v) Depreciation on addition/deletion is provided in proportion to the period of use.

Required:

Prepare the following ledger for the year ended December 31st, 2016

(a) Machinery Account

(b) Accumulated Depreciation Account

(c) Disposal Account **(12)**

Summary of entries of disposal (if no disposal account is required to be prepared)

Q.6 The following balances pertaining to fixed assets have been extracted from the trial balance of Star Traders for the year ended 31 December 2016:

	Rupees
Fixed Assets – Cost	25,000,000
Accumulated depreciation	6,250,000
Depreciation expense	1,250,000
Gain on disposal of fixed assets	58,000

Depreciation on fixed assets is charged from the month of addition to the month prior to disposal using reducing balance method at 20% per annum.

Depreciation expense for the current year has been correctly calculated and recorded except for the following:

(i) Physical verification of fixed assets carried out on 31 December 2016, revealed the following matters:

- Two laptops purchased on 1 July 2015 at a cost of Rs. 245,000 were withdrawn by the proprietor on 1 May 2016 for his personal use.
- Equipment costing Rs. 800,000 purchased on 1 January 2014 was damaged in rain in December 2016 and was scrapped.
- A machine costing Rs. 75,000 is not in the list of fixed assets, but has been in the use of sales department since 1 March 2016. On investigation it was found that the machine was transferred from stock-in-trade but no adjustment was made in the books.

(ii) Installation of an assembly plant was completed on 1 December 2016. Installation charges amounting to Rs. 240,000 have not yet been recorded in the books due to non-receipt of the invoice.

(iii) An invoice of Rs. 683,000 for a machine purchased on 1 October 2016 was mistakenly accounted for as Rs. 863,000.

Required:

Prepare necessary adjusting entries for the year ended 31 December 2016. **(14)**

Q. 7 The following balances pertaining to fixed assets have been extracted from the trial balance of Star Traders for the year ended 31 December 2016:

	Rupees
Fixed assets – cost	50,000,000
Accumulated depreciation	12,500,000
Depreciation expense	2,500,000
Gain on disposal of fixed assets	116,000

Depreciation on fixed assets is charged from the month of addition to the month prior to disposal using reducing balance method at 20% per annum.

Depreciation expense for the current year has been correctly calculated and recorded except for the following:

(i) Physical verification of fixed assets carried out on 31 December 2016, revealed the following matters:

- Two laptops purchased on 1 February 2015 at a cost of Rs. 490,000 were withdrawn by the proprietor on 1 August 2016 for his personal use.
- Equipment costing Rs. 1,600,000 purchased on 1 June 2014 was sold in September 2016 for Rs. 400,000.
- A machine costing Rs. 150,000 is not in the list of fixed assets, but has been in the use of sales department since 1 September 2016. On investigation it was found that the machine was transferred from stock-in-trade but no adjustment was made in the books.

(ii) Installation of an assembly plant was completed on 1 December 2016. Installation charges amounting to Rs. 480,000 have not yet been recorded in the books due to non-receipt of the invoice.

(iii) An invoice of Rs. 750,000 for a machine purchased on 1 November 2016 was mistakenly accounted for as Rs. 570,000.

Required:

Prepare necessary adjusting entries for the year ended 31 December 2016.

Q. 8 The written down value of plant and machinery of Azfar and Company as at 1 july 2011 is Rs. 2,110,443

Following additional information is also available:

i. On 1 July 2009, second-hand machinery was purchased for Rs. 600,000. An amount of Rs. 400,000 was spent on its overhauling, before use.
ii. On 1 January 2010 machinery costing Rs. 500,000 was purchased.
iii. The machinery purchased on 1 July 2009 became obsolete and was sold for Rs. 200,000 on 1 January 2012. On the same date, new machinery was purchased at a cost of Rs. 1,200,000.
iv. Machinery purchased on 1 January 2010 was sold on 30 June 2013 at its book value plus Rs. 100,000.

Azfar and Company provides depreciation on machinery @ 15% on written down value.

Depreciation on addition / deletion is provided in proportion to the period of use.

Required:

a) Machinery Account from 1 July 2011 to 30 June 2013
b) Machinery Disposal Account for the years ended 30 June 2012 and 2013

Q. 9 Ziakot steel Works provides depreciation on plant and machinery at 20% per annum on diminishing balance method.

On 1 July 2012 the balances in the plant and machinery account and accumulated depreciation accounts were Rs. 712,000 and Rs. 240,000 respectively.

A machine which was purchased on 1 January 2010 for Rs. 100,000 was sold on 31 March 2013 at Rs. 50,000.

Only one new machine was purchased during the year ended june 30 2013 costing Rs. 60,000. The machine was received in the factory on October 1, 2012 and was installed on 1 January 2013.

Required:

Plant and machinery account and accumulated depreciation account for the year ended 30.06.2013.

Q.10 Mr. umer has provided you the following data

Furniture – WDV as on 01.01.2008	400,000

Following transactions took place during the year.

1) Additions made Rs. 30,000 on 1.6.2008.
2) An asset having cost of Rs.50,000 on 01.04.2006 is sold on 30.6.2008 for Rs.12,000
3) Rate of depreciation is 20% WDV.

Required:

1) Asset account for the year ended December 31,2008 and disposal account.
2) Also prepare asset a/c for year ended December 31, 2009 assuming no additions and deletion took place

A. 1

Machinery Account – At Cost

b/d	85,000	1-10 Disposal Account	20,000
1-10 Cash	25,000		
		c/d	90,000

Accumulated Depreciation Account

Disposal A/c (W-3)	7,760	b/d (W-1)	31,500
		Depreciation (W-2)	11,230
c/d	34,970		

***Disposal Account**

Machinery	20,000	Cash	12,400
		Acc Depreciation	7,760
Gain (I/S)`	160		

*It is prepared to find out the gain or loss on disposal of an asset. It is prepared for the year; therefore there is no concept of opening and closing balance in this ledger (an income statement item).

WORKINGS:

(W-1) Accumulated Depreciation as on 1st January, 2015:

Machine No.	Cost	2012	2013	2014	Total
1 (1-1-2012)	50,000	10,000	8,000	6,400	24,400
2 (1-1-2013)	20,000	--	2,000	3,600	5,600
3 (1-1-2014)	15,000	--	--	1,500	1,500
		10,000	10,000	11,500	31,500

(W-2) Depreciation for the year 2015:

Machine #	Calculations	Depreciation
1	(50,000 – 24,400) × 20%	5,120
2	(20,000 – 5,600) × 20% × 9/12	2,160
3	(15,000 – 1,500) × 20%	2,700
4	25,000 × 20% × 3/12	1,250
		11,230

(W-3) Accounting Depreciation of Asset Disposed Off:

5,600 + 2,160 = 7,760

A.2

Plant & Machinery Account (At WDV)

Date	Particular	Rs.	Date	Particular	Rs.
1-4-97	b/d	460,000	1-9-97	Disposal a/c (W-1)	14,433
			31-3-98	Depreciation (W-2)	67,653
				c/d	377,914
1-4-98	b/d	377,914	31-3-99	Depreciation (W-3)	62,593
1-7-98	Cash	30,000			
	Payable	22,500			
		52,500		c/d	367,821
1-4-99	b/d	367,821	31-8-99	Disposal A/c (W-4)	18,136
			31-3-2000	Depreciation A/c (W-5)	53,480
				c/d	296,205
1-4-2000	b/d	296,205	1-11-2000	Disposal (W-6)	5,604
			31-3-2001	Depreciation (W-7)	44,047
				c/d	246,554

WORKINGS:

(W-1) WDV of Asset Destroyed:

Period		Depreciation	WDV
1-5-95 – 31-3-96	21,000 × 15% × 11/12	2,888	18,112
1-4-96 – 31-3-97	18,112 × 15%	2,717	15,395
1-4-97 – 1-9-97	15,395 × 15% × 5/12	962	14,433

(W-2) Depreciation for the year ended 31-3-98:

(460,000 – 15,395) × 15% =	66,691
Add: Depreciation of destroyed machine =	962
	67,653

(W-3) Depreciation for the year ended 31-3-99:

377,914 x 15% =	56,687
52,500 × 15% × 9/12 =	5,966
	62,593

(W-4) Disposal of Machine on 31-8-1999:

Purchase on 1-4-96 for Rs. 31,500

Period		Depreciation	WDV
1-4-96 – 31-3-97	31,500 × 15%	4,725	26,775
1-4-97 – 31-3-98	26,775 × 15%	4,016	22,759
1-4-98 – 31-3-99	22,759 × 15%	3,414	19,345
1-4-99 – 31-8-99	19,345 × 15% × 5/12	1,209	18,136

(W-5) Depreciation for the year ended 31-3-2000:

(367,821 – 19,345) × 15% =	52,271
Depreciation on disposed asset	1,209
	53,480

(W-6) Disposal of Machine on 1-11-2000:

Book Value on 1-4-97 = Rs. 10,000

Period	Depreciation		WDV
1-4-97 – 31-3-98	10,000 × 15%	1,500	8,500
1-4-98 – 31-3-99	8,500 × 15%	1,275	7,225
1-4-99 – 31-3-2000	7,225 × 15%	1,084	6,141
1-4-2000 – 1-11-2000	6,141 x 15 % x 7 /12	537	5,604

(W-7) Depreciation for the year ended 31-3-2001:

(296,205 – 6,141) × 15% =	43,510
Add: Depreciation on disposal	537
	44,047

A.3

Plant & Machinery A/c

		Rs.			Rs.
1-7-11	Balance b/d	5,660,000	1-12-11	Disposal account	144,334
1-10-11	Bank/creditors	80,000	01-02-12	Disposal account	18,250
			30-6-12	Dep. Expense	843,279
			30-6-12	Balance c/d	4,734,137
		5,740,000			**5,740,000**
1-7-12	Balance b/d	4,734,137	30-11-12	Disposal account	50,800
			30-6-13	Dep. Expense	705,380
			30-6-13	Balance c/d	3,977,957
		4,734,137			**4,734,137**

Workings:

Loss due to Accident:	**Rs.**
Cost of purchases	210,000
Depreciation for 11 months in 2009-2010	(28,875)
Book value at 30-06-2010	181,125
Depreciation for the year 2010-11	(27,169)
Book value at 30-06-2011	153,956
Depreciation for five months up to 1-12-2011 (153,956 x 15% x 5/12	(9,622)
WDV	**144,334**
Disposal of old plant and machinery:	
WDV as on 1-7-2011	20,000
Depreciation for seven months up to 1-02-2012	(1,750)
WDV	**18,250**

Depreciation for the year ended June 2012	
Depreciation on addition (80,000 x 15% x 9/12)	9,000
Depreciation on deletion due to accident	9,622
Depreciation on disposal of old plant and machinery	1,750
Depreciation on opening assets still available [5,660,000 - 153,956 - 20,000] x 15%	822,907
Total depreciation	843,279

Disposal of imported plant and machinery:	
Cost of purchases	75,000
Depreciation for the year 2010-11	(11,250)
Book value at 30-06-2011	63,750
Depreciation for the year 2011-12	(9,563)
Book value at 30-06-2012	54,187
Depreciation for five months up to 30-11-2012	(3,387)
WDV	50,800

Depreciation for the year ended June 2013	
Depreciation on disposal of imported plant and machinery	3,387
Depreciation on opening assets still available [4,734,137 - 54,187] x 15%	701,993
Total depreciation	705,380

A. 4

(a) Fixed Assets (at Cost)

	Rs.		Rs.
b/d	518,000	Disposal (Bal. Figure)	314,500
Additions	481,000	c/d	684,500
	999,000		999,000

Accumulated Depreciation Account

	Rs,		Rs,
Disposal (Bal. Fig)	166,500	b/d	277,500
c/d	249,750	Depreciation	138,750
	416,250		416,250

Disposal Account

	Rs,		Rs,
Asset	314,500	Accumulated Depreciation	166,500
		Loss on sale (given)	92,500
		cash (Bal. Fig)	55,500
	314,500		314,500

So amount of sale proceeds received on disposal of fixed assets during the year 2004 were Rs. 55.500.

A. 5

Machinery – Cost

b/f	12,500,000	1/8/2016 Disposal	225,000
		30/11/2016 Disposal	435,000
1/7/2016 Bank (900+100)	1,000,000	c/f	12,840,000
	13,500,000		13,500,000

Acc. Depreciation – Machinery

1/8/2016 Disposal	63,392	b/f	2,505,000
30/11/2016 Disposal	114,949	31/12/2016 Dep.	1,039,413
c/f	3,366,072		
	3,544,413		3,544,413

Disposal

1/8/2016 Machinery – Cost	225,000	1/8/2016 Acc. Dep	63,392
30/11/2016 Machinery –Cost	435,000	30/11/2016 Acc. Dep	114,949
		1/8/2016 Bank	65,000
		30/11/2016 Cash	140,000
		Loss	276,659
	660,000		660,000

Workings:

W-1) Depreciation Expense for the year:

On B/F — 947,103

(12,500,000 – 2,505,000 – 171,619 – 352,350) x 10%

On Additions: — 50,000

(1,000,000/10 x 100 x 6/12)

On Disposals:

(225,000 – 53,381) x 10/100 x 7/12 — 10,011

(435,000 – 82,650) x 10/100 x 11/12 — 32,299

Total: 1,039,413

W-2)

(i) Machine – 1:

				WDV
1 – 6 – 2013	225,000 x 10% x 7/12	= 13,125	=	211,875
1 – 6 – 2014	211,875 x 10%	= 21,187	=	190,687
1 – 6 – 2015	190,687 x 10%	= 19,069	=	171,618
1 – 8 – 2016	171,618 x 10% x 7/12	= 10,011	=	161,607
		63,392		

Machine – 2:

1 – 1 – 2014	435,000 x 10%	= 43,500	= 391,500
1 – 1 – 2015	391,500 x 10%	= 39,150	= 352,350
1 – 1 – 2016	352,350 x 10% x 11/12	= 32,299	= 320,051
		114,949	

A. 6 Star Traders:
Adjusting and closing entries

(1) 31 – 12 – 2016

(a) Drawings (245,000 – 39,200)	205,800	
*Accumulated Depreciation	39,200	
Fixed Asset Account		245,000

***Accumulated Depreciation at the date of drawings:**

1 – 7 – 2015	245,000
x 20% x 6/12	(24,500)
	220,500
x 20% x 4/12	(14,700)
Accumulated Depreciation (24,500+14,700)	39,200

(b) Accumulated Depreciation	29,400	
Depreciation		29,400
(245,000 – 24,500) x 20%x 8/12		
(Reversal of depreciation)		

(2) 31 – 12 – 2016

(a) *Accumulated Depreciation	381,867	
Loss on fixed assets (800,000 – 381,867)	418,133	
Fixed Assets		800,000
(Equipment damaged in rain)		

***Accumulated Depreciation at the date of damage:**

*1 – 1 – 2014	800,000
x 20%	(160,000)
31 – 12 – 2014	640,000
X 20%	(128,000)
31 – 12 – 2015	512,000
X 20% x 11/12	(93,867)

Accumulated Depreciation [160,000 + 128,000 + 93,867] = 381,867

(b) Accumulated Depreciation	8,533	
Depreciation		8,533
[512,000 x 20% x 1/12]		
[Reversal of Depreciation of December]		

(3) 31 – 12 – 2016:

(a) Fixed Assets	75,000	
Purchases/Stock		75,000
[Machine issued from stock for office use]		

(b) Depreciation	12,500	
Accumulated Depreciation		12,500
[75,000 x 20% x 10/12]		
[Depreciation charged from March to December]		

(4)

		Debit	Credit
(a)	Fixed Assets	240,000	
	Installation Charges Payable		240,000
	[Recording of installation charges]		
(b)	Depreciation	4,000	
	Accumulated Depreciation		4,000
	[240,000 x 20% x 1/12]		
	[Depreciation charged for December]		

(5)

		Debit	Credit
(a)	Accounts Payable	180,000	
	Fixed Assets		180,000
	[Excess Recording of Invoice]		
(b)	Accumulated Depreciation	9,000	
	Depreciation		9,000
	[180,000 x 20% x 3/12]		
	[Reversal of Extra Depreciation]		

A. 7 STAR TRADERS:

Adjusting and Closing Entries:

(1) 31-12-2016

		Debit	Credit
(a)	Drawings	353,480	
	*Accumulated Depreciation	136,519	
	Fixed Asset Account		490,000

***Accumulated Depreciation at the Date of Drawings:**

1-2-2015	490,000
× 20% × 11/12	(89,833)
WDV 31-12-2015	400,167
× 20% × 7/12	(46,686)
WDV 1-8-2016	353,480

Accumulated Depreciation (89,833+46,686) =136,519

		Debit	Credit
(b)	Accumulated Depreciation	33,347	
	Depreciation		33,347
	[490,000 – 33,347] × 20% × 5/12		
	[Reversal of Depreciation]		

(2) 31-12-2016

		Debit	Credit
(a)	Cash	400,000	
	*Accumulated Depreciation	620,090	
	Loss on fixed assts (I/S)	579,910	
	Fixed Asset		1,600,000

***Accumulated Depreciation at the Date of Damage:**

*1-6 -2014	1,600,000
× 20% x 7/12	(186,667)
31-12-2014	1,413,333
× 20%	(282,667)
31-12-2015	1,130,666
× 20% × 8/12	(150,756)
31-12-2016	979,910

Accumulated Depreciation [186,667+282,667+150,756] = 620,090

		Debit	Credit
(b)	Accumulated Depreciation	75,378	
	Depreciation Expense		75.378
	[1,130,666 × 20% × 4/12 = 75,378]		
	Reversal of Depreciation		

(3)	31-12-2016		
(a)	Fixed Assets	150,000	
	Purchases/Stock		150,000
	[Machine issued from stock for office use].		
(b)	Depreciation	10,000	
	Accumulated Depreciation		10,000
	[150,000 × 20% × 4/12]		
	[Depreciation charged from September to December].		
(4)			
(a)	Fixed Assets	480,000	
	Installation Charges Payable		480,000
	[Recording of Installation Charges].		
(b)	Depreciation	8,000	
	Accumulated Depreciation		8,000
	[480,000 × 20% × 1/12]		
	[Depreciation charged for December].		
(5)			
(a)	Fixed Asset	180,000	
	Accounts Payable		180,000
(b)	Depreciation	6,000	
	Accumulated Depreciation		6,000
	[180,000 × 20% × 2/12]		

A. 8

Machine WDV

b/d (bal)	2,110,443	Disposal	668,313
Cash	1,200,000	Depreciation	352,379
		c/d	2,289,751
	3,310,443		3,310,443
b/d (bal)	2,289,751	Disposal	284,033
		Depreciation	343,462
		c/d	1,662,256
	2,289,751		2,289,751

Disposal account

Machine	668,313	Cash	200,000
		Loss (I/S)	468,313
	668,313		668,313

Disposal account

Machine	284,033	Cash (284,033 + 100,000)	384,033
Gain (I/S)	100,000		
	384,033		384,033

W-1) Machine Purchased on 01-07-2009:

Cost = purchases price	600,000
Overhauling cost	400,000
Total cost	1,000,000
Depreciation @15%	(150,000)
30-06-2010	850,000
Depreciation @ 15%	(127,500)
30-06-2011	722,500
Depreciation @ 15% x 6/12	(54,188)
01-01-2012	668,313

W-2) Machine Purchased on 01-01-2010:

Cost	500,000
Depreciation @ 15% x 6/12	(37,500)
30-06-2010	462,500
Depreciation @ 15%	(69,375)
30-06-2011	393,125
Depreciation @ 15%	(58,969)
30-06-2012	334,156
Depreciation @ 15%	(50,123)
30-06-2013	284,033

W-3) Depreciation for 2012:

(2,110,443-722500) x 15%	= 208,191
722,500 x 15% x 6/12	= 90,000
1,200,000 x 15% x 6/12	= 54,188
	352,379

W-4) Depreciation for 2013:

(2,289,751 – 334,156) x 15% =	293,339
334,156 x 15% =	50,123
	343,462

A. 9

Plant and machinery

b/d	712,000	Disposal	100,000
Cash	60,000		
		c/d	697,000
	722,000		722,000

Accumulated depreciation account

		b/d	240,000
Depreciation (W 1)	51,040	Depreciation (W-2)	97,520
c/d	286,480		
	337,520		337,520

W-1 Accumulate depreceation of machine sold:

Cost (01.01.2010)	100,000
Depreciation @ 20% x 6/12	(10,000)
30 June 2010	90,000
Depreciation @ 20%	(18,000)
30 June 2011	72,000

Depreciation @ 20%	(14,400)
30 June 2012	**57,600**
Depreciation @ 20% x 9/12	(8,640)
31 March 2013	**48,960**
Total depreciation upto disposal (10,000 + 18,000 +14,400+8,640)	51,040

W-2 depreciation for the year:

Opening WDV (712,000 - 240,000)	472,000
Less opening WDV of Disposal	(57,600)
	414,400
X 20%	82,880
+57,500 x 20% x 9/12	8,640
+600,000x20% x 6/12	6,000
Total	**97,520**

A.10

Building A/C-2008(WDV)

b/d	400,000	Disposal (W-2)	30,600
Cash	30,000	Depreceation (W-1)	80,100
		C/d	319,300
	430,000		430,000

Disposal A/C

Building	30,600	Cash	12,000
		Loss(bal)	18,600
	30,600		30,600

Building A/C-2009(WDV)

b/d	319,300	Deprecation (319,300 x 20%)	63,860
		c/d	255,440
	319,300		319,300

(W-1) Depreciation expenses	
On opening excluding disposal	73,200
(400,000 - 34,000) * 20%	
On addition (30000 * 20% * 7/12)	3,500
On disposal (34,000 * 20% * 6/12)	3,400
	80,100

(W-2) WDV of disposal	
Cost (1-04-06)	50,000
Less: deprecation (50000*20%*9/12)	(7,500)
31-12-06	42,500
Depreciation (42500*20%)	(8,500)
31-12-07	34,000
Depreciation (34000*20%*6/12)	(3,400)
30-06-08	30,600

BAD & DOUBTFUL DEBTS:

Bad Debts: Amount which was receivable is now irrecoverable.

Debtor

b/d (01.07.2014)	10,000	Cash	300,000
Sales	500,000	Discount Allowed	5,000
		Bad debts (Actual)	50,000
		c/d (30.06.2015)	155,000
	510,000		510,000

Prudence Concept

Anticipated loses are recognised immediately

Anticipated gains re recognised when actually occur

↓

Doubtful debts (Estimated bad debts)

↓

Anticipated Loss

↓

Accounting entry:

Bad & doubtful debts 15,500

(Expense account)

* allowance for doubtful debs 15,500

*balance sheet item to be deducted from debtors.

Allowance for doubtful debt account:

(It is like an Acc Depreciation Account, Purchase Returns Account Sales Return Account in its nature)

Allowance Account

		b/d	--
		Bad debts	15,500
c/d	15,500		
	15,500		15,500

Statement of financial position:

Assets:

Debtors	155,000
Less: Allowance	(15,500)
	139,500

Summary:

Entry of actual bad debts:

Bad debts

Debtors

Entry of estimated bad debts:

Bad debts

Allowance

Another example:

Debtors Account

b/d	--	Cash	70,000
Sales	100,000	Bad debts	5,000
		c/d	25,000
	100,000		100,000
b/d	25,000	Cash	150,000
Sales	200,000	Discount Allowed	5,000
		c/d	70,000
	225,000		225,000
b/d	70,000	Cash	350,000
Sale	500,000	Discount allowed	7,500
		c/d	212,500
	570,000		570,000
b/d	212,500	Cash	--
Sales	500,000	c/d	712,500
	712,500		712,500

Allowance Account

		b/d	--
		Bad debts (bal)	2,500
c/d (25,000 x 10%)	2,500		
	2,500		2,500
		b/d	2,500
c/d (70,000 x 5%)	3.500	Bad debts (bal)	1,000
	3,500		3,500
		b/d	3,500
		Bad debts (bal)	7,125
c/d (212,500 x 5%)	10,625		
	10,625		10,625
Bad debts (bal)	3,500	b/d	10,625
c/d (712,500 x 1%)	7,125		
	71,250		71,250

ICAP QUESTION BANK

1. **HUBBARD**

   The doubtful debts allowance brought forward on 1 January in the books of Hubbard was Rs.86,000. Trade receivables at 31 December amounted to Rs.2,840,000 and bad debts to be written off totalled Rs.115,000. Hubbard has estimated that the closing balance on the doubtful debts allowance account should be 5% of accounts receivable.

   Required:

   Write up the bad debts expense account and the doubtful debts allowance account.

2. **APU**

   The financial records of Apu include an allowance for doubtful debts of Rs.206,000 brought forward on 1 January. Trade receivables at 31 December amount to Rs.2,440,000 and bad debts to be written off total Rs.55,000. An allowance for doubtful debts of 5% of receivables is to be carried forward.

   Required:

   Write up the bad debts expense account and the doubtful debts allowance account.

3. NELSON

Nelson makes allowance for doubtful debts at varying percentages based on statistical analysis and the level of outstanding trade receivables. The result of this policy for the last three years is as follows.

Year to December

	2010	**2011**	**2012**
		Rs.(000)	
Trade receivables at the year end (before adjusting for any bad debts)	196,860	151,020	216,020
bad debts to be written off (accounts in liquidation)	1,860	1,020	6,020
Doubtful debts allowance (%)	5%	6%	7.5%

The doubtful debts allowance at 1 January 2010 was Rs.10,000,000.

Required:

Write up the bad debts expense account and doubtful debts allowance account for each of the three years. Show the relevant extracts from the statement of financial position for each of the three years.

Summary of above discussion:

Actual Bad Debts: (Also called as Bad debts Written Off).

Bad Debts	XX	
Debtors		XX

Increase in Allowance of Bad Debts:

Bad Debts	XX	
Allowance for bad debts		XX

Decrease in Allowance of Bad Debts:

Allowance for bad debts	XX	
Bad debts		XX

Point to remember:

Allowance for bad debts is also called as Provision for bad debts.

<u>**Question-4**</u>

Mr. Aftab commenced business on January 1, 1995. The following information relates to the first three years of his business.

Year to December 31,	**1995**	**1996**	**1997**
	Rs.	**Rs.**	**Rs.**
Sales (all credit)	458,400	567,600	537,200
Cash received	355,300	512,700	481,200
Discount allowed	45,800	47,300	48,600
Bad debts to be written off	2,200	4,900	2,500
Provision to be made for doubtful debts	5%	10%	7.5%

Required: Write up the following for each of the three years:

(i) Trade debtors Account
(ii) Provision for Bad Debts Account
(iii) Bad debts A/c
(iv) Charge to Profit and Loss account (means income statement) during three years
(v) Balance sheet extracts for three years

There are two types of Allowance for bad debts:

- Specific Allowance → Allowance against specific customers
- General Allowance → Allowance on remaining customers

Following steps should be followed if both types of allowances are to be created:

1. First create specific allowance.
2. Secondly, deduct the balance of customers on which specific allowance is created from the closing balance of debtors.
3. Then multiply the percentage of general allowance against the amount calculated in second step.
4. Total allowance will be equal to sum of specific allowance and general allowance.

5. BELL

Bell is a sole trader making up his accounts to 31 July each year.

At 31 July Year 6 the balance on the allowance for doubtful debts account was Rs.1,420,000. During the following financial period ending 31 July Year 7, Bell suffered a number of bad debts amounting to Rs.723,000, which he wrote off to the bad debts account.

At 31 July Year 7 Bell listed out all his receivables balances, which totalled Rs.32,456,000. After reviewing the list Bell decided that three balances - namely Lee Rs.230,000, Bee Rs.562,000 and Yee Rs.56,000 - were all doubtful and had to be allowed for as doubtful debts. In addition, he considered that 2% of all the remaining balances were doubtful and had to be provided for.

Required

Show the ledger accounts reflecting the necessary adjustments, and the relevant extracts from the financial statements.

Note: if percentage of specific allowance is not given then create 100% allowance.

Contra Entry:

If a person is simultaneously our customer as well as supplier, his respective balances can be adjusted against each other by making a set – off or contra entry.e.g.

1. Ali

50,~~000 Dr~~.	**10,~~000 Cr~~.**
40,000 Dr.	**Cr.**

Contra Entry

Creditor Ali	10,000	
Debtor Ali		10,000

2. Shahid

5,~~000 Dr~~.	**60,~~000 Cr~~.**
-- Dr.	**55,000 Cr.**

Contra Entry

Creditor Shahid	5,000	
Debtor Shahid		5,000

Bad Debts Recovered means amount is received after recording of bad debts.

	If amount is received **after** bad debts actually being written off				If amount is received **before** bad debts actually being written off		
2014	Bad debts	10,000		2014	Bad debts	10,000	
	Debtor – Aslam		10,00		Allowance		10,00(
2017	Bank/Cash	10,000		2015	Cash	10,000	
	Bad Debts		10,00		Debtor		10,00(

Q.6 LOPEZ

In his first year of trading to 31 December 2011 Lopez made credit sales of Rs.200,000 and received Rs.150,000 from his credit customers.

At the end of the year he decided to write off Ludmila's debt of Rs.8,000, make a specific allowance for Jozef's debt totalling Rs.3,500 and create a general allowance of 5% of remaining trade receivables.

During his second year of trading he made sales on credit of Rs.300,000 and received cash of Rs.280,000 including Rs.4,000 from Ludmila. At 31 December 2012, he decided to write off Jozef's debt, and create a specific allowance against 50% of

Chokin's total debt of Rs.6,000. He decided that his general allowance should now be 8% of remaining accounts receivable.

In the year to 31 December 2013 Lopez made credit sales of Rs.500,000 and received cash of Rs.400,000. Separate from this he also received a cheque from Chokin for Rs.6,000.

At the year end he decided to create a specific allowance against Paulo's debt of Rs.50,000 and maintain his general allowance at 8%.

Required:

For each of the above years show the trade receivables account, bad debt expense account and allowance for doubtful debts account, and the statement of financial position extract as at each year end.

Question 7

You have been provided following information relating to the business of Ghazi traders (GT) for the year ended 30 June 2015.

	Rupees
Sales	12,000,000
Sales return	700,000
Discount allowed	500,000
Collection from customers	8,540,000

(i) Credit sales were 80% of the total sales.

(ii) As at 1 July 2014, debtors account and provision for doubtful debts account had a balance of Rs. 5,630,000 and 690,000 (comprising of specific provision of Rs. 430,000) respectively.

(iii) Details of specific provision on 30 June 2014 and recoveries there against during the year ended 30 June 2015 are as follows:

	Amount due and provided	**Recoveries**
	---------- Rupees	**----------**
Sabir Enterprises	100,000	50,000
Babur Traders	150,000	75,000
Zubair Associates	180,000	30,000
	430,000	155,000

Remaining debt from Zubair Associates needs to be written off.

(iv) Specific provision is also required to be made against the entire balances of the following debtors:

	Rupees
Rahil Stores	50,000
Adam Enterprises	75,000
Shahid Traders	25,000
	150,000

(v) A customer Nadir who had a debit balance of Rs. 280,000 had also supplied goods to GT worth Rs. 250,000. The two balances were adjusted with mutual consent.

(vi) Sales return and discount allowed pertain to credit sales only.

(vii) GT follows a policy of making a general provision of 5% against debtors.

(viii) Collection from customers includes recovery against debts written off during the year ended 30 June 2014 amounted to Rs. 199,000.

Required:

Prepare debtors account and provision for doubtful debts. **(08)**

Question 8

Ravi enterprises (RE) maintains specific provision for doubtful debts on the basis of individual assessment of its major customers. A general provision is also made at 5% of the remaining month-end balances. Following information pertains to trade debtors and provision for doubtful debts for the month of August 2016:

(i) Opening balance:

		Rs. In million
Trade debtors		200.00
Provision for doubtful debts:		
- Specific	BEE Traders, 100% of the balance	(8.00)
	RAY Brothers, 60% of the balance	(6.00)
- General	5% of the remaining balance	(9.10)
		176.90

(ii) Credit sales for the month amounted to Rs. 900 million.

(iii) Collections from customers were Rs. 850 million, which included:

- a recovery of Rs. 4.5 million against trade debts written-off in previous years; and
- an amount of Rs. 7.2 million received net of 10% discount in full and final settlement of invoices.

(iv) RAY Brothers were declared bankrupt and their debt has to be written-off.

(v) A customer, TAJ & Co. has disputed certain sales invoices aggregating Rs. 2.8 million which have been outstanding for more than one year. RE estimates that the customer will eventually pay half of the disputed amount.

(vi) Amounts aggregating Rs. 1.5 million due from general customers are not recoverable and have to be written-off.

Required:

Prepare following ledger accounts for the month of August 2016:

(a) Provision for doubtful debts **(10)**

(b) Bad debts expense **(02)**

Q.9 Following information pertains to Global Network Supplies (GNS) for the year ended 30 June 2017:

	Rs. "000"
Trade debtors – as at 1 July 2016	55,975
Transactions for the year ended 30 June 2017:	
– Sales (including cash sales which is 20% of credit sales)	540,000
– Sales returns pertaining to credit sales	6,300
– Collection from credit customers (including Rs. 8.1 million	
from customers who availed 10% discount)	438,000

GNS maintains specific provision for doubtful debts on the basis of assessment of its debtors. In addition, a general provision is maintained at 4% of the remaining customers' balances.

The status of debtors being considered for the purpose of specific provision is as under:

Customer's name	Balances as on		Specific provision as at 1 July 2016	Adjustments required as at 30 June 2017
	1 July 2016	30 June 2017*		
	-------------- Rs. in '000 --------------			
Mehran Link	400	320	65	Mehran Link is facing severe cash flow difficulties; therefore, a provision at 30% of the outstanding balance is required.
Bolan Dialing	480	480	240	The entire amount needs to be written-off as Bolan Dialing has been declared bankrupt.
Khyber Cables	135	90	95	The balance is in respect of old disputed invoices and needs to be written-off.
Ravi Rays	460	460	-	Ravi Rays has stopped buying from GNS. It has been decided to set-off Rs. 120,000 payable by GNS to Ravi Rays and make provision at 25% of the remaining balance.
	1,475	**1,350**	**400**	

before adjustment

Required:

Prepare following ledger accounts for the year ended 30 June 2017:

(a) Trade debtors **(04)**

(b) Provision for doubtful debts **(05)**

(c) Bad debt expense **(03)**

Q.10 MZH & Co. maintains specific provision for doubtful debts on the basis of individual assessment of its major customers and also maintains general provisions @ 8% of the year end balance:

The following are the balances as on 1st January 2016;

	Rs.
Trade debtors	420,240
Provision for doubtful debts	38,880

The following information relates to the year 2016:

i) Credit sales and credit sales return for the year were Rs. 2,983,500 and 9,300 respectively.

ii) Details of provision for doubtful debts as on 1 January 2016 are as follows:

		Provision Amount
Alpha Traders	40% of the balance	1,500
Beeta Associates	80% of the balance	2,160
Gamma Brothers	100% of the balance	1,290
Theta & Co.	70% of the balance	1,050
General provision	8% of the remaining balance	32,880
		38,880

iii) During the year no further sales were made to the following customers

Alpha Traders   Beeta Associates   Gamma Brothers   Theeta & Co.

iv) Collection from credit customers amounting to Rs. 2,506,360 included the following:

- A recovery of Rs. 2,450 against trade debts written-off in previous years
- An amount of Rs. 11,500 received net of 20% discount in full and final settlement of invoices
- Alpha traders Rs. 3,750, Beeta Associates Rs. 2,200 & Theeta & Co. Rs. 400
- Rs. 15,600 from Shayan & Co. after adjustment of contra amounting to Rs. 40,000
- Cheque of Rs. 4,900 from Waqas & Co. which is dishonored

v) Beeta Associates and Theeta & Co. were declared bankrupt and their debt should be written off.

vi) Other bad debts to be written off Rs. 81,600.

vii) Specific provision is also required to be made against the following trade debtors

Trade Debtor	**Amount Due**	**Provision required**
Raza Brothers	4,100	70% of the balance
Abbas & Co.	1,450	40% of the balance
SD & Co.	800	100% of the balance

Required:

Prepare the following ledgers for the year ended 31 December 2016:

a) Trade Debtors

b) Bad & Doubtful debts expense

c) Provision for doubtful debts **(12)**

Answers:

A.1

Debtors Account

Unadjusted bal	2,840,000	Bad debts	115,000
		c/d adjusted	2,125,000
	2,840,000		2,840,000

Bad Debts Expense Account

Debtor	115,000		
Allowance	50,250		
		c/d (I/S)	165,250
	165,250		165,250

Allowance for Bad Debts Account

		b/d	86,000
		Bad debts	50,250
c/d (2,125,000 x 5%)	136,250		
	136,250		136,250

A.2

Bad Debts Account

Debtors	550,000	Allowance	88,750
c/d (I/S)	31,750		
	86,750		86,750

Debtors Account

Unadjusted bal	2,440,000	Bad debts	55,000
		c/d	2,385,000
	2,440,000		2,440,000

Allowance Account

Bad debts	86,750	b/d	206,000
c/d (2,385,000)	119,250		
	206,000		206,000

Allowance	86,750	
Bad debts		86,750

A.3

Bad Debts Account

Debtors	1,860	Allowance	250
		c/d (I/S)	1,610
Debtors	1,020	Allowance	750
		c/d (I/S)	270
Debtors	6,020		
Allowance	6,750		
		c/d (I/S)	12,770

Allowance Account

Bad debts	250	b/d	10,000
c/d	9750		
Bad Debts	750	b/d	9,750
c/d	9,000		
		b/d	9,000
c/d	15,750	Bad debts	6,750

A.4

(i)

Dr. Debtors account-1995 Cr.

Sales	458,400	Cash	355,300
		Discount allowed	45,800
		Bad debt expense	2,200
		c/d	55,100

Dr. Debtors account-1996 Cr.

b/d	55,100		
Sales	567,600	Cash	512,700
		Discount allowed	47,300
		Bad debt expense	4,900
		c/d	57,800

Dr. Debtors account-1997 Cr.

b/d	57,800		
Sales	537,200	Cash	481,200
		Discount allowed	48,600
		Bad debt expense	2,500
		c/d	62,700

(ii)

Dr. Provision for doubtful debt account Cr.

1995			b/d	-
			Bad debt expense	2,755
	c/d (55,100 x 5%)	2,755		
1996			Opening balance (b/d)	2,755
			Bad debt expense (Bal.)	3,025
	c/d (57,800 x 10%)	5,780		
1997			Opening balance (b/d)	5,780
	Bad debt expense (bal)	1,077		
	c/d (62,700 x 7.5%)	4,703		

(iii)

	Dr.	Bad debt expense account		Cr.
1995	Debtor	2,200		
	Provision	2,755	c/d (I/S)	4,955
1996	Debtor	4,900		
	Provision	3,025	c/d (I/S)	7,925
	Debtor	2,500	Provision	1,077
			c/d (I/S)	1,423

(iv)

Income statement Extracts

Expenses:	1995	1996	1997
- Bad debts	4,955	7,925	1,423
- Discount allowed	45,800	47,300	48,600

(v)

Balance sheet Extracts

	1995	1996	1997
Debtors	55,100	57,800	62,700
Provision for doubtful debt account	(2,755)	(5,780)	(4,703)
	52,345	52,020	57,998

A.5

Allowance Account

		b/d	1,420,000
		Bad debts (bal)	60,160
c/d (working)	1,480,160		
	1,480,160		1,480,160

Bad Debts Account

Debtors	723,000		
Allowance	60,160		
		c/d (I/S)	783,160
	783,160		783,160

Working:

Specific Allowance		General Allowance	
↓		↓	
Allowance against specific customers		Allowance on remaining customers	
↓		↓	
Lee	230,000	Debtor	32,456,000
Bee	562,000	Less: Balance on which specific allowance is created	(848,000)
Yee	56,000		31,608,000
	848,000		× 2 % = 632,160

Total allowance: sum of specific allowance and general allowance=848,000+632,160=1,480,160

Income Statement (Extracts)
For the year ended 31st July, year 7
Operating Expenses:

Bad debts	(783,160)

Statement of financial position (Extracts)
As on 31st July, year 7

Assets:

Debtors	32,546,000
Less: Allowance for bad debts	(1,480,160)
	31,065,840

Ans.6 LOPEZ

Trade receivables

		Rs.		Rs.
2011			***2011***	
	Sales revenue	200,000	Cash receipts	150,000
			Bad debt expense (w/o)	8,000
			31.12.99 Balance c/d	42,000
		200,000		200,000
2012			***2012***	
1.1.01	Balance b/d	42,000	Cash receipts	276,000
	Sales revenue	300,000	Bad debt expense (w/o)	3,500 (2)
			31.12.01 Balance c/d	62,500
		346,000		346,000
2013			***2013***	
1.1.02	Balance b/d	62,500	Cash receipts	400,000
	Sales revenue	500,000	Cash (Chokin)	6,000 (3)
			31.12.02 Balance c/d	156,500
		562,500		562,500
2014				
1.1.03	Balance b/d	156,500		

Bad debt expense a/c

	Rs.			Rs.
2011		***2011***		
Trade receivables (Ludmila)	8,000			
Allowance for doubtful debts	5,425	31.12	c/d I/S	13,425
	13,425			13,425
2012		***2012***		
Trade receivables (Jozef)	3,500	Cash (Ludmila)		4,000
Allowance for doubtful debts	2,095	31.12	c/d I/S	1,595
	5,595			5,595

2013		*2013*	
Allowance for doubtful debts	51,000	31.12 c/d I/S	51,000

Allowance for doubtful debts a/c

	Rs.		Rs.
2011		*2011*	
31.12.99 Balance c/d (W1)	5,425	Bad debt expense	5,425
2012		*2012*	
31.12.01 Balance c/d (W2)	7,520	1.1.01 Balance b/d	5,425
		Bad debt expense	2,095
	7,520		7,520
2013		*2013*	
		1.1.02 Balance b/d	7,520
31.12.02 Balance c/d (W3)	58,520	Bad debt expense	51,000
	58,520		58,520

Workings

		Rs.
(1)	Allowances year 1	
	Specific (Jozef)	3,500
	General 5% x Rs.(42,000 – 3,500)	1,925
		5,425
(2)	Allowances year 2	
	Specific (Chokin) (50% × 6,000)	3,000
	General 8% x Rs.(62,500 – 6,000)	4,520
		7,520
(3)	Allowances year 3	
	Specific (Paulo)	50,000
	General 8% x (Rs.156,500 – 50,000)	8,520
		58,520

Statement of financial position extracts

	31 December		
	2011	**2012**	**2013**
	Rs.	**Rs.**	**Rs.**
Trade receivables	42,000	62,500	156,500
Less Allowance for doubtful debts	(5,425)	(7,520)	(58,520)
	36,575	54,980	97,980

A. 7

Debtor Account

b/d	5,630,000	Sales Return	700,000
Sales (1,200,000 × 80%)	9,600,000	Discount Allowed	500,000
		Collection (8,540 – 199)	8,341,000
		Bad debts – Zubair	150,000
		Creditors – Nadir	250,000
		Cash (50+75+30)	155,000
		c/d	5,134,000

Allowance for Bad Debts Account

		b/d	690,000
Bad debts (bal)	172,050		
c/d (Working)	517,950		

Bad Debts Account

Bad debts (Zubair)	150,000	Cash (Bad debts recovered)	199,000
		Allowance for bad debts	172,050
c/d (I/S)	221,050		

Workings:

Provision for Doubtful Debts:

Debtor balances as on 30 June 2015 (adjusted)			5,134,000
Less:	Debtors against which specific allowance is required:		
	Sabir Enterprises (100,000 – 50,000)	50,000	
	Babur Traders (150,000 – 75,000)	75,000	
	Rahil Stores	50,000	
	Adam Enterprises	75,000	
	Shahid Traders	25,000	
			(275,000)
Debtors balance on which general provision is to be made			4,859,000
General provision (4,859,000 × 5%)			242,950
Specific provision (as above)			275,000
Total closing balance of provision			517,950

A. 8

Bad Debts Account

Debtor	10	Cash	4.5
Debtor	1.5	Allowance	2.13
		c/d (I/S)	4.87

Allowance Account

Bad debts	2.13	b/d (8+6+9.1)	23.1
c/d (W-1)	20.97		

Workings:

(W-1) **Debtor Account**

b/d	200	Discount allowed	0.8
Sales	900	Cash (850 – 4.5)	845.5
		Bad debts (6 ÷ 60%)	10
		Bad debts	1.5
		c/d	242.2

(W-2) Specific Allowance:

BEE (from Opening)	8.00
Taj (2.8 × 50%)	1.40
	9.40

General Allowance:

Debtors	242.2
Less: Amounts on which allowance is created (8 + 2.8)	(10.8)
	231.4
× 5%	11.57
Total allowance (9.4 + 11.57)	20.97

A. 9

(a) <u>Global Network Supplies:</u> **Rs. '000'**

Debtors Account

b/d	55,975	Sales return	6,300
		Bank	438,000
Sales (540,000/120 x 100)	450,000	Discount allowed (8,100/90 x 10)	900
		Accounts payable – Ravi Rays	120
[100 + 20 = 120]		Bad debts – Bolan	480
		Bad debts – Khyber	90
		c/d	60,085
	505,975		505,975

(b) **Provision Account**

Bad debts	40	b/d (W-1)	2,598
c/d (W-2)	2,558		
	2,598		2,598

(c)

Bad Debts Account

Debtors – Bolan	480	Allowance	40
Debtor – Khyber	90		
		c/d (I/S)	530
	570		570

Workings:

(W – 1) Calculation of opening allowance:

1)	Specific allowance – Given (65+240+95)		400	
2)	Closing debtors	55,975		
	Less: Balance on which specific Allowance was created (400+480+135)	(1,015)		
	Remaining debtors	54,960		
3)	x 4%		2,198	
4)	Total allowance (400 + 2,198)			2,598

(W – 2) Calculation of closing allowance:

1)	Specific allowance:				
	Mehran (320 x 30%)	=	96		
	Ravi Rays (460 – 120) x 25%	=	85		
				181	
2)	Closing debtors		60,085		
	Less: Balance on which specific allowance is created:				
	Mehran		(320)		
	Ravi Rays (460 – 120)		(340)		
			59,425		
3)	x 4%			2,377	
4)	Total allowance (181 + 2,377)				2,558

A.10

a)

Trade Debtors

b/d	420,240	Sales return	9,300
sales	2,983,500	Collection (2,506,360 – 2,450)	2,503,910
Bank (Dishonored cheque)	4,900	Discount allowed (11,500/80 x 20)	2,875
		Creditors	40,000
		Bad debts	1,600
		Other bad debts	81,600
		c/d	769,355

Beeta Associates:

2,160/80 x 100 = 2,700 – 2,200 = 500

Theeta & Co:

1,050/70 x 100 = 1,500 – 400 = 1,100

1,600

b)

Bad debts

Debtors	1,600	Cash	2,450
Debtors	81,600		
Allowance	27,592		
		c/d (I/S)	108,347

c)

Provision for Bad debts Account

		b/d	38,880
		Bad debts (bal)	27,597
c/d (working)	66,477		

Workings:

(W-1) Closing balance of allowance:

	Amount Due	Allowance
Specific:		
Gamma [from opening 100%]	1,290	1,290
Raza Brothers [70%]	4,100	2,870
Abbas & Co. [40%]	1,450	580
SD & Co. [100%]	800	800
	7,640	5,540

* From Alpha Traders 100% amount is received during the year so no further allowance; i.e. 1,500/40 x 100 = 3,750 [in point (iv)]

General Allowance:

Debtors	769,355		
Less: Amount on which specific allowance is created	(7,640)		
	761,715		
x 8%		60,937	
Total allowance (5,540 + 60,937)			= 66,477

Further practice questions:

QUESTION-1

A company maintains its Provision for Bad Debts at 5%. The following details are available:

	2004	2003
	Rupees	**Rupees**
Bad Debts	13,500	7,200
Discount allowed	4,500	10,800
Recovery of bad debts written off in earlier years	2,700	4,500

Sundry debtors (before writing off Bad Debts and discounts) amounted to Rs. 378,000 on December 31, 2004 and Rs. 540,000 on December 31, 2003.

On January 1, 2003, Provision for Bad Debts had balance of Rs. 40,950.

Required: Prepare the Provision for Bad Debts Account and bad debts account for the years 2003 and 2004.

(Spring 2005, Q# 7}

QUESTION-2

(a) Explain briefly why a provision may be made for doubtful debts.

(b) Explain the book keeping procedure to be followed when a customer whose debt has been written off as bad subsequently pays the amount originally owing.

(c) Mr. Inam Ellahi on January 01, 2001 had debtors of Rs. 2,500,000 on which he had made provision for doubtful debts of 4%. During the year.

(i) Mr. Mujahid who owed Mr. Inam Ellahi Rs. 120,000 was declared bankrupt and a settlement of Rs. 250 in one thousand rupees was made, the balance being treated as a bad debt.

(ii) Other bad debts written off during the year was Rs. 230,000.

(iii) On December 31, 2001 total debtors amounted to Rs. 2.43 million but this requires adjustment as follows:

- Ms Samreen, a debtor owing Rs. 60,000 was considered unrealizable. This amount is to be written off.
- A cheque amounting to Rs. 20,000 received from Mr. Saleem deposited earlier but returned unpaid by the bank at the year-end (a dishonored cheque).

Mr. Inam Ellahi maintained his provision for doubtful debts at 4% debtors.

Required:

(a) For the year ended December 31, 2001, show the entries in the following accounts:

(i) Provision for doubtful debts;

(ii) Bad debts expenses.

(b) What is the effect on net profit of the change in the provision for doubtful debts?

(Autumn 2002, Q # 3

QUESTION-3

Balance Sheet as at Dec.31, 1999 of Asma Traders included a provision for doubtful debt of Rs. 6,900. The company's accounts for the year ended Dec.31, 2000 are under preparation. The company's policy now is to relate the provision for doubtful debts to the age of debts outstanding. The debts outstanding at December 31, 2000 and the required provision for Doubtful debts are as follows:

Debts Outstanding	Rupees	Prov. for doubtful debts %
Upto 1 Month	72,000	1
More than 1 month & upto 2 months	30,000	2
More than 2 months & upto 3 months	24,000	4
More than 3 months	9,000	5

Required: Prepare the following account for the year ended December 31, 2000 to record the above transactions:

Provision for doubtful debts

QUESTION-4

The age analysis of debtors of ABC Ltd. as at December 31, 1999 is as under:

	Rs.
Current month	120,000
30 to 60 days	75,000
60 to 90 days	36,000
Over 90 days	11,000

The balance of provision for doubtful debts as at December 31, 1998 was Rs. 4,500. Following additional information is available:

(i) The current month total includes Rs. 600 for discounts allowed to debtors not recorded.

(ii) The "30 to 60 days" total includes a balance of Rs. 2,000 to be taken as a contra entry.

(iii) The "over 90 days" total includes an amount of Rs. 2,400 to be written off as bad debts.

(iv) Provisions for doubtful debts has to be made on following basis:

Over 90 days	20%
60 - 90 days	10%
30 - 60 days	5%
Current month	Nil

Required:

(a) Calculate the amount of provision for doubtful debts as at December 31, 1999.

(b) Prepare ledger account for provision for doubtful debts. **(05)**

(Spring 2000, Foundation -1}

QUESTION-5

The following financial information is available with respect to operation of Ahmed Corporation.

	Rupees
Accounts receivable at 31-12-90	380,640
Allowance for doubtful debts at 31-12-90	9,720
Sales in 1991	2,562,000
Cash collected from customers in 1991	2,478,768

Additional information:

The cash collections also include a recovery in full of Rs. 4,680 receivable from Mr. Ali a customer whose account balance had been written off late in 1990.

During 1991, customers' accounts totaling Rs. 10,098 have been written off.

At December 31, 1991, the accounts receivable included Rs. 60,174 of past due balances. The management estimated that the probable loss contained therein is 20% and in addition 2% of the current accounts receivable might prove uncollectible.

Required:

i) Prepare journal entries for all the above transaction in year 1991.

ii) Calculate the amount of bad/doubtful debts expense for the year 1991.

iii) Prepare the necessary adjusting entries at December 31, 1991. Round amount to the nearest rupees for bad / doubtful debts expense.

iv) Show the amount of accounts receivable and the allowance for doubtful debts as they would appear in the balance sheet as at December 31, 1991. **(20)**

Question No.6

Flying Courier used to maintain a provision for doubtful debts at 5% of the total debtors. Due to increase in bad debts, the management has decided to increase the provision to 8% from the current year.

The following summarized information pertains to the year ended 31 December 2013:

	Rs. In million
Debtors control account balance as at 1st January, 2013	35
Transactions during the year ended 31 December, 2013:	
• Cash Sales	51
• Credit Sales	740
• Payments by debtors (including recoveries of Rs. 3 million against balances previously written off)	680
• Old outstanding balance written off	5

Required:

Prepare a ledger account for provision for doubtful debts and bad debts account for the year ended 31 December 2013.

Question 7

Following balances are appearing in the trial as on December 31, 2010.

Debtors	50,000
Provision for doubtful debts (1.1.2010)	5,000
Bad debt	700
Discount allowed	300

i) Further bad debt of Rs. 70 are to be recorded.
ii) A debtor cheque of Rs. 60 is dishonoured.
iii) Further discount allowed of Rs. 80 is to be recorded.
iv) A debtor who owes Rs. 450 is declared bankrupt (means balance to be written off).
v) Mr. Asim owes Rs. 1,200 from which 60% recovery is expected only.
vi) Create provision for doubtful debt @ 5%
vii) A bad debt recovery of Rs. 320 relating to debt written off in previous periods is to be recorded .

Required:

a) Debtor a/c.
b) Provision for doubtful debt account.
c) Bad debt expense a/c
d) Discount allowed expense a/c
e) Profit and loss and balance sheet extract

SOLUTIONS

Answer-1

Provision for doubtful debts account-2003

Dr.			Cr.
		Opening balance (b/d)	40,950
Bad debt expense (bal)	14,850		
c/d ((W-1)522,000 x 5%)	26,100		
	40,950		40,950

Provision for doubtful debts account-2004

Dr.			Cr.
		Opening balance (b/d)	26,100
Bad debt expense (bal)	8,100		
c/d ((W-2)360,000 x 5%)	18,000		
	31,500		31,500

bad debts account-2003

Dr.			Cr.
Debtors	7,200	Allowance	14,850
c/d (I / S)	12,150	Cash	4,500
	19,350		19,350

bad debts account-2004

Dr.			Cr.
		Allowance	8,100
Debtors	13,500	Cash	2,700
		c/d	2,700
	13,500		13,500

Workings

(W-1)

Debtors account-2003

Dr.			Cr.
Unadjusted closing balance	540,000		
		Discount allowed	10,800
		Bad debt expense	7,200
		Closing balance-adjusted (c/d)	522,000
	540,000		540,000

(W-2)

Debtors account-2004

Dr.			Cr.
Unadjusted closing balance	378,000		
		Discount allowed	4,500
		Bad debt expense	13,500
		Closing balance-adjusted (c/d)	360,000
	378,000		378,000

Answer-2

a)

According to the prudence concept foreseen losses are always recorded immediately. The sale of current period against which we expect some bad debts in coming periods is a foreseen loss which is recorded in the year in which sale is recorded.

b)

Following book keeping procedure is followed on the recovery of bad debt.

	Dr.	Cr.
Cash	xxx	
Bad debt		xxx
(On receiving cash in respect of debt which has been previously written off)		

c)

Provision for doubtful debt account

Dr.			Cr.
Bad debt expense	4,400	Opening balance (b/d) (2,500,000 x 4%)	100,000
c/d ((W-1)2,390,000 x 4%)	95,600		
	100,000		100,000

Bad debt Expense

Dr.			Cr.
Debtor (120,000/1,000x750)	90,000	Allowance	4,400
Debtors (others)	230,000		
Debtors (Ms. Samreen)	60,000	c/d (I/S)	375,600
	380,000		380,000

Workings

(W-1)

Debtors account (adjusted) – 2001

Dr.			Cr.
Unadjusted closing balance	2,430,000		
Bank (Dishonour)	20,000	Bad debt expense (Ms. Samreen)	60,000
		Closing balance-adjusted (c/d)	2,390,000
	2,450,000		2,450,000

d) Net profit will decrease by Rs. 375,600 because of charging bad debts in income statement.

Answer-3

a)

Provision for doubtful debt account

Dr.			Cr.
		Opening balance (b/d)	6,900
Bad debts (bal.)	4,170		
c/d (W-1)	2,730		
	6,900		6,900

Workings

(W-1) Calculation of closing provision

	Amount of Debt	Rate	Amount of provision
Up to 1 month	72,000	1%	720
1 month - 2 month	30,000	2%	600
2 month - 3 month	24,000	4%	960
More than 3 month	9,000	5%	450
	135,000		2,730

Answer-4

a) Calculation of closing provision

		Amount of adjusted Debt	Rate	Amount of Provision
Current month	(W-1)	119,400	0%	-
30 to 60 days	(W-1)	73,000	5%	3,650
60 to 90 days	(W-1)	36,000	10%	3,600
Over 90 days	(W-1)	8,600	20%	1,720
		237,000		8,970

(W-1)	Current month	30 to 60 days	60 to 90 days	Over 90 Days
Un adjusted balance	120,000	75,000	36,000	11,000
Adjustments:				
Discount allowed	(600)			
Contra entry		(2,000)		
Bad debt				(2,400)
Adjusted balance	119,400	73,000	36,000	8,600

Dr. Provision for doubtful debt account Cr.

		Opening balance (b/d)	4,500
		Bad debt (bal.)	4,470
c/d (part-a)	8,970		
	8,970		8,970

Answer-5

i)

	Dr.	Cr.
Account receivable	2,562,000	
Sales		2,562,000
(Recording of sales)		
Cash	2,474,088	
Account receivable (2,478,768-4,680)		2,474,088
(Cash received from debtors)		
Cash	4,680	
Bad debt		4,680
(Bad debt recovery)		
Bad debt expense	10,098	
Account receivable		10,098
(Bad debt recording)		

ii)

Dr. Bad debts account Cr.

Debtors	10,098	Cash received	4,680
Allowance	10,281	Income statement	15,699
	20,379		20,379

(W-1)

Dr. Allowance for doubtful debts Cr.

		Opening balance (b/d)	9,720
		Bad debt (bal)	10,281
c/d(W-1.1)	20,000		
	20,000		20,000

(W-1.1) Calculation of closing provision

	Debtor	Rate	Provision
Debtor on which general provision of 20% is required	60,174	20%	12,035
Debtor on which general provision of 2% is required ((W-2)458,454-60,174)	398,280	2%	7,966
Total			20,000

(W-2)

Dr. Account receivable account Cr.

Opening balance (b/d)	380,640		
Credit sales	2,562,000	Cash received (2,478,768-4,680)	2,474,088
		Bad debt expense	10,098
		Closing balance (c/d)	458,454
	2,942,640		2,942,640

iii)

	Dr.	Cr.
Bad debts	10,281	
Provision for doubtful debt		12,281
(Entry for bad/doubtful debt expense)		

iv) <u>Balance sheet extract</u>

Account receivable	458,454
Provision for doubtful debt	(20,000)
	438,454

Answer 6

Allowance for Bad Debts **Rs.000**

	Rs.		**Rs.**
		b/d (35,000 × 5%)	1,750
		Bad debts (balancing)	5,690
c/d (93,000 × 8%)	7,440		
	7,440		**7,440**

Bad Debts Account **Rs.000**

	Rs.		**Rs.**
Debtors	5,000	Cash	3,000
Allowance	5,690	c/d (I/S)	7,690
	10,690		**10,690**

WORKINGS:

(W-1) Debtors Account **Rs.000**

	Rs.		**Rs.**
b/d	35,000	Cash (680,000 – 3,000)	677,000
Sales	740,000	Bad debt expense	5,000
		c/d	93,000
	775,000		**775,000**

<u>Answer-7</u>

a) Debtor a/c

Dr.			Cr.
Unadjusted closing balance	50,000	Bad debt	70
Bank	60	Discount allowed	80
		Bad debt	450
		c/d	49,460

b) Provision for doubtful debt account

Dr.			Cr.
Bad debt (bal)	2,107	b/d	5,000
c/d (W-1)	2,893		

d)

Dr.	Bad debt a/c		Cr.
Unadjusted closing balance	700	Allowance	2,107
Debtor	70	Cash	320
Debtor	450		
c/d (I/S)	1,207		

e)

Dr.	Discount allowed a/c		Cr.
Unadjusted closing balance	300		
Debtor	80	c/d (I/S)	380

f) **Profit and loss extracts**

Expenses	
Discount allowed	(380)
Bad debts reversed	1,207

Balance sheet extracts

Debtors	49,460
Less: Provision for doubtful debt	(2,893)
	46,567

(W-1) Closing provision

- Specific provision

	Total debt	Rate of specific provision	
- Mr. Asim	1,200	40%	480
- General provision	[(49,460 – 1,200) x 5%)]		2,413
Total closing provision (c/d balance of provision for doubtful debt account			2,893

(W-2) Calculation of remaining debtors on which general provision is to be charged

Total closing debtors	49,460
Less: Debtors on which specific provision is to be charged – Mr. Asim	(1,200)
Remaining debtors (on which general provision is to be charged)	48,260

FINAL ACCOUNTS

- Income Statement (Statement of comprehensive income or statement of profit or loss)
- Statement of Financial Position (Balance Sheet)

Formats

Business Name
Statement of Financial Position
As on ____________

Assets:	
Non-Current Assets:	
Land	--
Building	--
Machine	--
Intangible Assets (e.g Software)	--
Current Assets:	
Stock	--
Debtors	--
Cash and Bank	--
Total Assets	--
Capital and Liabilities:	
Capital	--
Add: Net Profit	--
Less: Drawings	(--)
Non-Current Liabilities:	
Long Terms Loans	--
Current Liabilities:	
Creditors	--
Bank Overdraft	--
Expenses payable	--
Total Capital & Liabilities	--

Non-Current Liabilities:

Liabilities which are payable after more than one year from balance sheet date

Current Liabilities:

Liabilities which are payable within one year from the balance sheet date

Business Name
Income Statement
For the year ended 30-06-2014

Sales	--
Cost of Sales (note 1)	(--)
Gross Profit	--
Other Income (note 2)	--
Selling and administrative expenses (note 3)	(--)
Financial charges (note 4)	(--)
Net profit	--

Notes:

(Note 1) Cost of Sales

Opening Stock	--
Add Purchases	--
Carriage Inwards	--
Closing Stock	(--)

(Note 2) Other Income

Dividend income	--
Commission income	--
Rent Income	--

(Note 3) Selling and administrative expenses

Salaries	--
Bad debts	--
Depreciation	--
Repair	--

(Note 4) Financial charges

Interest expense	--
Bank charges	--

Important Points to remember:

1. Trial Balance contains Closing Balance of ledgers, unless any adjustment is required in an accounting head.
2. The amounts which are appearing in trial balance are after their debit credit effects in journal. Therefore, figures appearing in the trial balance should be written only once according to their nature either in income statement or in balance sheet.
3. The amounts which are in additional information should be recorded by making double entry.
4. administrative and selling expenses include all expenses other than interest and bank charges.

Accrual Concept

Incomes	**Expenses**
Income are recorded when earned whether or not cash is received:	Expenses are recorded when they are incurred whether or not cash is paid

Q.1 HERBERT

The following trial balance has been extracted from the ledger of Herbert, a sole trader, as at 31 May 2013, the end of his most recent financial year.

Herbert: Trial balance as at 31 May 2013

	DR Rs.(000)	CR Rs.(000)
Land and buildings at cost	90,000	
Equipment at cost	57,500	
Accumulated depreciation (as at 1 June 2012)		
On land and buildings		12,500
On equipment		32,500
Inventory as at 1 June 2012	27,400	
Sales		405,000
Purchases	259,600	
Discounts allowed	3,370	
Discounts received		4,420
Wages and salaries	52,360	
Bad debts	1,720	
Loan interest	1,560	
Other operating expenses	38,800	
Trade receivables	46,200	
Trade payables		33,600
Allowance for doubtful debts		280
Cash in hand	151	
Bank overdraft		14,500
Carriage out	5,310	
Drawings	28,930	
10% loan		15,600
Capital as at 1 June 2012		94,501
	612,901	**612,901**

The following additional information as at 31 May 2013 is available:

(a) Inventory as at 31 May 2013 was valued at Rs.25,900,000.

(b) Depreciation for the year ended 31 May 2013 has yet to be provided as follows:
- Property – 1% using the straight-line method;
- Equipment – 15% using the straight-line method.

(c) There are accrued wages and salaries of Rs.140,000.

(d) Other operating expenses include some prepaid expenses of Rs.500,000 and does not include some accrued expenses of Rs.200,000.

(e) The allowance for doubtful debts should be adjusted to 5% of trade receivables as at 31 May 2013.

(f) The amount for purchases includes goods valued at Rs.1,040,000 which were withdrawn by Herbert for his own personal use.

Required:

Prepare Herbert's statement of comprehensive income for the year ended 31 May 2013 and his statement of financial position as at that date.

Q.2 STEVEN CHEE

The following trial balance was extracted from the main ledger of Steven Chee, a sole trader, as at 31 May 2013 – the end of his financial year.

Steven Chee: Trial balance as at 31 May 2013

	DR Rs.(000)	CR Rs.(000)
Land and buildings at cost	120,000	
Equipment at cost	80,000	
Accumulated depreciation (as at 1 June 2012)		
On land and buildings		20,000
On equipment		38,000
Purchases	250,000	
Sales		402,200
Inventory as at 1 June 2012	50,000	
Discounts allowed	18,000	
Discounts received		4,800
Returns outwards		15,000
Wages and salaries	61,800	
Bad debts	4,600	
Loan interest	2,100	
Other operating expenses	17,700	
Trade payables		36,000
Trade receivables	38,000	
Cash in hand	300	
Bank	1,300	
Drawings	24,000	
Allowance for doubtful debts		500
7% long-term loan		30,000
Capital as at 1 June 2012		121,300
	667,800	**667,800**

The following additional information is available:

- **(a)** Inventory as at 31 May 2013 has been valued at cost at Rs.42,000,000.
- **(b)** There are accrued wages and salaries of Rs.800,000.
- **(c)** Other operating expenses are prepaid by Rs.300,000.
- **(d)** The allowance for doubtful debts is to be adjusted so that it is 2% of trade receivables.
- **(e)** Depreciation for the year ended 31 May 2013 should be provided for as follows:
  - Land and buildings – 1.5% per annum on cost, using the straight-line method.
  - Equipment – 25% per annum, using the reducing balance method.

Required:

Prepare Steven Chee's statement of comprehensive income for the year ended 31 May 2013 and his statement of financial position as at that date.

Q.3 SWAN

The following balances were extracted from the main ledger of SWAN at 31 December 2013.

	Rs.(000)
Capital	10,059
Inventory at 1 January 2013	2,720
Cash in hand	55
Bank overdraft	2,522
Sundry receivables	7,009
Sundry payables	6,735
Motor vans (Cost Rs.2,000)	1,500
Drawings in cash	2,459
Fixtures and fittings (Cost Rs.4,000)	3,800
Purchases	33,436
Allowance for doubtful debts	162
Sales	50,261
Purchases returns	120
Carriage inwards	546
Rent	626
Salaries and wages	5,226
Motor vehicle expenses	920
Interest on bank overdraft and bank charges	56
Carriage outwards	720
Discounts allowed	65
Discounts received	59
Returns inwards	240
Freehold land	10,300
Bad debts	240

You are given the following information:

(1) The inventory at 31 December 2013 was Rs.4,270,000.
(2) Wages and salaries payable at 31 December 2013 were Rs.426,000.
(3) Rent paid in advance at 31 December 2013 amounted to Rs.100,000.
(4) The allowance for doubtful debts is to be increased to Rs.260,000.
(5) Depreciation is to be charged as follows: motor vans at 25% per year on cost, fixtures and fittings 5% per year on cost.
(6) During 2013, the owner of SWAN withdrew goods valued at Rs.180,000 for his own use. No entry has been made in the accounts for the withdrawal of these goods.
(7) One quarter of the motor vehicle expenses is the cost of the owner's private motoring, as distinct from expenses for business purposes.

Required:

Prepare a statement of comprehensive income for the year ending on 31 December 2013 and a statement of financial position as at that date.

Q.4 BRADBURY AND CO
The following trial balance has been extracted from the ledger of Bradbury and Co, as at 31 December 2013, the end of its most recent financial year.

Bradbury and Co: Trial balance as at 31 December 2013

	DR Rs.	CR Rs.
Plant and machinery at cost	920,000	
Allowance for depreciation (as at 1 January 2013)		215,000
Inventory as at 1 January 2013	39,000	
Sales		1,292,000
Purchases	550,000	
Capital		173,000
Distribution expenses	116,000	
Administrative expenses	241,000	
Bad debts	23,500	
Loan (charging interest at 6%)		400,000
Receivables control account	200,000	
Payables control account		73,500
Allowance for doubtful debts		6,000
Interest paid on loan	12,000	
Bank	58,000	
	2,159,500	**2,159,500**

The following additional information as at 31 December 2013 is available:

(a) Inventory as at 31 December 2013 was valued at Rs.35,000.

(b) Depreciation on plant and machinery for the year ended 31 December 2013 is to be provided at the rate of 10% of cost.

(c) There are accrued distribution expenses of Rs.7,500 and prepaid administrative expenses of Rs.4,000.

(d) The allowance for doubtful debts should be adjusted to 2% of trade receivables as at 31 December 2013

(e) No interest has been accrued on the loan.

Required:
Prepare the statement of comprehensive income of Bradbury and Co for the year ended 31 December 2013 and its statement of financial position as at that date in a format suitable for publication.

Q.5 MARS
The following information relates to the business of Mars for the year ended 31 December 2012.

	Rs.	Rs.
Capital account, 1 January 2012		13,640
Freehold properties at cost	7,500	
Furniture and fittings at cost	2,000	
Motor cars at cost	6,300	
Accumulated depreciation to 1 January		
Freehold properties		450
Furniture and fittings		800
Motor cars		2,370
Inventory 1 January	6,740	
Purchases	54,520	
Sales		79,060
Salaries	8,760	
Rates	1,170	
Office expenses	3,950	
Motor expenses	3,790	
Drawings	4,800	
Allowance for doubtful debts 1 January		600
Loan		4,000
Trade receivables	9,240	
Trade payables		10,040
Bank balance	2,190	
	110,960	**110,960**

You are also supplied with the following information.

(1) Inventory at 31 December 2012 was Rs.7,330.
(2) Rates paid in advance at 31 December 2012 amounted to Rs.250.
(3) Allowance for doubtful debts is to be made equal to 5% of accounts receivable at 31 December 2012.
(4) Depreciation is to be provided for the year at the following annual rates calculated on cost at the year end

Freehold properties	1%
Furniture and fittings	10%
Motor cars	20%

(5) Interest on the loan at 5% per annum is to be provided.

Required:
Prepare a statement of comprehensive income for the year ended 31 December 2012 and a statement of financial position at that date. **(20)**

Q.6 BOWIE [After suspense account]
Mr Bowie is a sole trader and prepares his accounts to 30 September each year. At 30 September 2013, his trial balance is as follows:

	Dr Rs.	Cr Rs.
Plant and machinery		
- Cost	125,000	
- depreciation at 1 October 2012		28,000
Office equipment		
- Cost	45,000	
- depreciation at 1 October 2012		15,000
Inventory at 1 October 2012	31,000	
Purchases and sales	123,000	194,000
Selling expenses	12,000	
Heat and light	8,000	
Wages and salaries	19,000	
Printing and stationery	6,000	
Telephone and fax	6,000	
Rent, rates and insurances	4,000	
Trade receivables and payables	35,000	33,000
Allowance for doubtful debts at 1 October 2012		4,000
Bank	3,000	
Petty cash	1,000	
Drawings	22,000	
Capital at 1 October 2012		169,000
Suspense account	3,000	
	443,000	**443,000**

The following additional information at 30 September 2013 is available:

(i) Closing Inventory goods for resale Rs.53,000

(ii) Prepayments:
- telephone and fax rental Rs.1,000
- rates and insurance Rs.1,000

(iii) Accruals:
- wages and salaries Rs.5,000

(iv) Specific bad debts to be written off amount to Rs.3,000.

(v) Allowance for doubtful debts to be amended to 5% of debtors, after adjusting for bad debts written off.

(vi) The following book-keeping errors are discovered:
- the purchase of an item of inventory has been debited to the office equipment account, cost Rs.1,200.
- the payment of Rs.1,300 to a trade payable has been recorded by debiting the bank account and crediting the trade payable's account
- a payment of rent of Rs.1,500 has been credited to the bank and credited to the rent account.

(vii) The figure in the trial balance for the bank balance is the balance appearing in the cash book, prior to the reconciliation with the bank statement. Upon reconciliation, it is discovered that:
- unpresented cheques amount to Rs.3,000; and
- bank charges not entered in the ledgers amount to Rs.4,000.

(viii) Depreciation of non-current assets is to be provided as follows:

plant and machinery	10% on cost
office equipment	33.33 % on the reducing balance at the end of the year

Required:

(a) Show the journal entries and suspense account to correct the bookkeeping errors identified in note (vi). (Narrative descriptions are not required)

(b) Prepare a statement of comprehensive income for the year ended 30 September 2013.

(c) Prepare a statement of financial position at 30 September 2013

Discounts

Trade Discount
(Negotiation Discount)

Treatment Sale and purchase
Is recorded net of trade discount

Settlement Discount
(Early payment Discount)

Related to credit transactions

Discount Allowed

Discount Allowed (Dr.)
Debtor (Cr.)

Discount Received

Creditor (Dr.)
Discount Received(Cr.)

Cash Sale

Good sold for Rs.100,000 on cash after negotiation Rs.5,000 is allowed as a discount

Seller			**Buyer**		
Cash	95,000		Purchase	95,000	
Sale		95,000	Cash		95,000

Credit Sale

Goods sold for Rs.700,000 on credit to All after negotiation Rs.10,000 is allowed as a discount .It is further agreed that if payment is made within 10Days Rs.20,000 will also be allowed as a discount . Date Of sale is 1-7-2015 (and assume amount is received on 8-7-2015)

Seller				**Buyer**		
1-7-2015	Debtor	690,000		Purchase	690,000	
	Sale		690,000	Creditor		690,000
8-7-2015	Cash	670,000		Creditor	670,000	
	Debtor		670,000	Cash		670,000
	Discount Allowed	20,000		Creditor	20,000	
	Debtor		20,000	Discount Allowed		20,000

Debtor

Sale	690,000	Cash	670,000
		Discount Allowed	20,000

Creditor

Cash	670,000	Purchases	690,000
Discount Received	20,000		

Q.7

Following is the trial balance of Salman for the year ended 30 June 2014:

	Rs. in '000' Debit		Rs. in '000' Credit
Drawings	30,500	Salman's capital	300,000
Trade debtors	109,420	Creditors	104,724
Goodwill	20,000	Loan taken from bank	40,000
Interest on bank loan	800	Bad debts provision as on 1 July, 2013	900
Cash in hand	728	Sales	353,300
Plant & machinery - WDV	45,000	Interest received	11,930
Factory building – WDV	42,400	Bills payable	23,150
Sales return	10,000	Accrued expenses	3,460
Cash at bank	13,512	Other income	3,100
Power and utility charges	6,500		
Trade discount	2,432		
Purchases less retunes	330,530		
Salaries and wages	40,400		
Rent and rates	6,992		
Insurance	2,000		
Advertisement	4,512		
Opening stock	127,762		
Carriage inward	10,420		
Bills receivable	32,526		
Miscellaneous expenses	4,130		
	840,564		**840,564**

Additional information:

(i) On 1 July 2013 a machine was purchased for Rs. 500 thousand. However, this cost has wrongly been posted to the purchases account.

(ii) Salman's son works as the head of administration and received a salary of Rs. 150 thousand per month, which has been included in drawings.

(iii) Insurance premium was paid in advance to the extend of Rs. 650 thousand.

(iv) Depreciation is to be charged on written down value (WDV) as follows:

Plant & machinery	10%
Factory building	5%

(v) Provision for bad debts is maintained at 2% of trade debtors.

(vi) Closing stock as on 30 June 2014 amounted to Rs. 237,500 thousand.

Required:

Prepare statement of comprehensive income (Trading and Profit and Loss account) for the year ended 30 June 2014 and statement of financial position (Balance Sheet) as at 30 June, 2014. **(20)**

"SUSPENSE ACCOUNT"

(i) If a transaction is completely omitted from the books even then, trial balance will be reconciled.

(ii) If there is no violation of debit/credit rule even then, trial balance will be reconciled even though entry is wrong.

(iii) If there is a violation of debit/credit rule then trial balance will not be reconciled.

If trial balance is not reconciled then:

(i) If sum of debit column of trial balance is more than sum of credit column of trial balance then suspense account will appear on credit column of trial balance unless corrected.

(ii) If sum of credit column of trial balance is more than the sum of debit column of trial balance then the suspense account will appear on debit column of trial balance unless corrected.

Q.8 Following is the summarised trial balance of **Fortune Traders (FT)** for the year ended 30 June 2016:

	Debit	**Credit**
	-------- Rs. in '000'--------	
Buildings – Cost	3,700	
Buildings – accumulated depreciation as at 1 July 2015		1,436
Plant and machinery – cost	6,650	
Plant and machinery – accumulated depreciation as at 1 July 2015		2,414
Stock-in-trade as at 1 July 2015	1,045	
Purchases	16,000	
Purchase returns		220
Sales		28,900
Sales returns	90	
Capital as at 1 July 2015		3,000
Selling and administration expenses	5,855	
12% loan payable		5,000
Trade receivables	3,600	
Provision for doubtful debts as at 1 July 2015		180
Prepayments and other receivables	380	
Trade and other payables		2,080
Cash and bank balances	5,850	
Suspense account	60	
	43,230	**43,230**

Additional information:

(i) FT depreciates its fixed assets from the month of addition. Depreciation is to be charged on written-down value (WDV) as follows:

Buildings	5%
Plant & machinery	10%

(ii) On 1 March 2016, FT paid an advance of Rs. 330,000 for purchase of a machine and debited it to plant and machinery. The machine was delivered on 1 September 2016.

(iii) Closing inventory was valued at Rs; 1,560,000. This included goods costing 35,000 returned by a customer on 30 June 2016 but not yet accounted for. These goods were earlier sold at cost plus 40%.

(iv) The loan was acquired on 1 January 2016 and the principal amount is repayable in eight equal half yearly instalments commencing from 1 January 2017. Interest is payable half yearly on 1 January and 1 July each year.

(v) Selling and administration expenses include fire insurance premium amounting to Rs. 430,000 and Rs. 240,000 paid for office and owner's personal premises respectively. The policies are valid upto 31 December 2016.

(vi) Rent and salaries amounting to Rs. 137,000 and Rs. 89,000 respectively are to be accrued at 30 June 2016.

(vii) At 30 June 2016, the provision for doubtful debts is to be reduced by Rs. 30,000.

(viii) Suspense account represents an error which occurred when a credit note of Rs. 30,000 received for goods returned to a supplier was mistakenly posted as credit to trade payable account.

Required:

(a) Prepare a statement of comprehensive income for the year ended 30 June 2016. **(08)**

(b) Prepare a statement of financial position as at 30 June 2016. **(09)**

Q.9 Following summarized trial balance as at 31 December 2015 pertains to **Moon Trading (MT)** who deals in office machines:

	Debit	Credit
	-------- Rs. in Millions ------	
Fixed assets at cost	150	
Accumulated depreciation		45
Trade debtors	200	
Provision for doubtful debts		6
Inventory	410	
Prepayments, advances and other receivables	9	
Cash and bank balances	5	
Capital		50
Bank loan		160
Trade creditors		320
Accruals and other payables		25
Sales revenue		2,840
Purchases	2,141	
Selling and administration expenses	540	
Interest on bank loan	8	
Bank charges	2	
Other income		15
Suspense account		4
	3,465	**3,465**

Additional information:

(i) Inventory is valued under the FIFO method. Value of physical inventory as at 31 December 2015 amounted to Rs. 530 million.

(ii) During stock taking, it was noted that:

- A photocopy machine appearing in inventory is being used in the office since 1 October 2015. The cost of the machine is Rs. 0.78 million.
- Four computers were found to be short. It was discovered that these computers costing Rs.0.32 million had been issued for use by the proprietor's family members.
- Items costing Rs. 4.5 million were returned to a supplier on 31 December 2015.The return was recorded in January 2016.
- Items having invoice value of Rs. 2.4 million sold on credit were returned by a customer on 31 December 2015. A credit note was issued and recorded by MT on 12 January 2016. The profit margin on these items was 20% of cost.

(iii) Depreciation for the year has already been charged on all fixed assets at 20% per annum under the straight line method, except for the effect of any errors,

(iv) A recovery of Rs. 3.5 million against debts written off in prior years was credited to trade debtors. MT's policy is to provide doubtful debts at 3% on year-end balance.

(v) Review of other income revealed the following information:

- Services for certain contracts amounting to Rs. 1.2 million were rendered in December 2015 but invoices thereof were processed in January 2016.
- On 1 August 2015, MT received an amount of Rs. 1.8 million as 50% advance against a maintenance contract covering the period from 1 September 2015 to 31 May 2016 and was credited to other income. The balance amount would be paid on completion of the contract.

(vi) Office supplies purchased during the year are directly debited to expenses. Unused office supplies at close of the year amounted to Rs. 0.15 million.

(vii) The bank loan was acquired on 1 April 2015. The principal amount is repayable in five equal annual instalments on 31 March each year. Interest is payable at 10% per annum on six monthly basis and is recorded at the time of payment

(viii) Suspense account represents a commission (net of bank charges amounting to Rs. 0.25 million) received on 1 September 2015.

Required:

(a) Prepare a statement of comprehensive income for the year ended 31 December 2015. **(11)**

(b) Prepare a statement of financial position as at 31 December 2015. **(09)**

Q.10 Following is the summarised trial balance of **Rainbow Lights (RL)** for the year ended 31 December 2016:

	Debit	Credit
	Rs. in million	
Capital – 1 January 2016		100
Profit and loss account – 1 January 2016	30	
Drawings	50	
Fixed assets – cost	270	
Accumulated depreciation		150
Closing inventory	170	
Trade debtors	400	
Provision for doubtful debts		12
Prepayments and other receivables	45	
Cash and bank	20	
10% Long-term loan		120
Trade creditors		240
Accruals and other payables		28
Sales		750
Cost of sales	304	
Selling and administration expenses	146	
Financial charges	10	
Miscellaneous income		45
	1,445	**1,445**

Additional information:

(i) RL uses perpetual inventory method to record its inventory. During the physical inventory count carried out on 31 December 2016, following matters were noted:

- Inventory shortages amounted to Rs. 2 million which is considered to be normal. Goods costing Rs. 15 million were damaged in fire and have no sales value.
- Goods costing Rs. 1 million were withdrawn by the owner for his personal use but no adjustment was made in the books.

- Goods sold on credit for Rs. 7 million were returned but have not been accounted for. These goods were sold at cost plus 40%.

(ii) Goods sold on credit at a trade discount of 5% were recorded at gross amount of Rs. 20 million.

(iii) Rs. 2 million were recovered in full and final settlement of an old outstanding balance of Rs. 3 million which had been written-off last year. The amount recovered was credited to trade debtors account.

(iv) RL maintains a provision for doubtful debts at 3% of the year-end balance.

(v) Miscellaneous income includes Rs. 12 million received against an annual maintenance contract expiring on 30 April 2017.

(vi) Annual rent amounting to Rs. 24 million was paid in advance on 1 October 2016 and charged as an expense.

(vii) Long-term loan was acquired on 1 February 2016 and is repayable in 2020. Interest thereon is due semi-annually on 1 August and 1 February each year. Interest is charged to expenses at the time of payment.

(viii) An equipment costing Rs. 8 million was purchased on 1 September 2016 against advance payment. The equipment was not used and returned on 31 December 2016. The supplier agreed to set-off the cost of the equipment against the amount payable by RL. The return as well as reversal of depreciation is yet to be recorded in the books.

(ix) Depreciation on fixed assets is charged at 15% per annum from the month of addition to the month prior to disposal using reducing balance method. Assume depreciation for the year has already been charged except for the effect of any errors.

Required:

(a) A statement of comprehensive income for the year ended 31 December 2016. **(10)**

(b) A statement of financial position as at 31 December 2016. **(11)**

Start practice questions

Q.11 Following is the summarised trial balance of **Home Appliances (HA)** for the year ended 30 June 2017:

	Debit	**Credit**
	Rs. in '000	
Fixed assets- cost	35,000	
Accumulated depreciation- 1 July 2016		8,000
Inventory- 1 July 2016	8,200	
Trade receivables	12,500	
Provision for doubtful receivables- 1 July 2016		750
Prepayments and other receivables	2,350	
Cash and bank balances	1,300	
Capital		25,500
Drawings	4,500	
Trade payables		10,200
Accruals and other payables		5,310
Sales		101,120
Return inwards	3,000	
Purchases	70,000	
Wages and salaries	5,900	
Discounts	1,600	
Utility charges	2,350	
Carriage inwards	1,360	
Running and maintenance expenses	3,290	
Financial charges	580	
Miscellaneous income		110
Suspense account		940
	151,930	**151,930**

Additional information:

(i) Cost of closing physical inventory was Rs. 9,000,000. However, goods returned by a credit customer on 30 June 2017 were received after completion of the count, therefore not included in the inventory. These goods had been sold for Rs. 400,000 at cost plus 25%. However, the goods are damaged and can be sold at normal price after a repair cost of Rs. 90,000. The return has not yet been accounted for.

(ii) Suspense account represents an online transfer of funds by a customer who availed 5% discount on settlement of the pending amount by 30 June 2017. The amount was credited by the bank net of its charges of Rs. 10,000.

(iii) HA maintains a 5% provision against trade receivables.

(iv) Running and maintenance expenses totalling Rs. 110,000 were incurred in June 2017. Related invoices were received and accounted for in July 2017.

(v) A machine was rented-out to Zee Trader (ZT) on 1 October 2016. Annual rent of Rs. 120,000 received in advance is included in 'Accruals and other payables'. However, on 16 June 2017, the machine was sold to ZT for Rs, 450,000. The sale proceed net of rent adjustment was received in July 2017. The disposal has not yet been accounted for.

The machine had been purchased on 1 January 2016 and had written down value of Rs. 540,000 as at 1 July 2016.

(vi) HA depreciates its fixed assets at 20% per annum from the month of addition to the month prior to disposal using reducing balance method. There were no additions/disposals during the year except as mentioned above.

Required:

(a) Prepare statement of profit or loss for the year ended 30 June 2017. **(11)**

(b) Prepaid statement of financial position as at 30 June 2017. **(09)**

Important points to remember

- If trial balance contains opening balance of stock and purchases then closing stock will be in additional information whish needs to be adjusted.
- If trial balance contains cost of sales and closing stock then closing stock will have only one effect in SOFP as an asset.
- If gain or loss on disposal is in the trail balance then no further accounting entry, instead only place the figure once in other income
- If gain or loss on disposal is not appearing in the trial balance then calculate the gain or loss from additional information (if any) and pass necessary entries.
- Trail balance contains income and expenses of current period only. Effects of previous period's incomes and expenses should have been included in the opening balance of capital.

Effect of stocks on profit:

- Closing stock has direct relationship with profit (means inverse relationship with cost of sale)
- Opening stock has inverse relationship with profit (means direct relationship with cost of sale)

When it is assumed that depreciation/amortization has already been charged in trial balance:

- If depreciation expense is appearing on the debit side of the trial balance
- If closing date is mentioned against accumulated depreciation in trial balance or closing date is mentioned against WDV of asset in the trial balance.

Answers:

A.1

HERBERT
Statement of Comprehensive Income
For the year ended 31-05-2013

	Notes	'000'
Sales		405,000
Cost of Sales	N-1	(260,060)
Gross Profit		144,940
Other Income (discount received)		4,420
Admin and selling Expenses:	N-2	(112,955)
Finance cost (loan interest)		(1,560)
Net Profit		**34,845**

HERBERT
Statement of financial position
As on 31-05-2013

	'000'	'000'
Non-Current Assets:		
Land & Building (90,000 – 12,500 – 900)		76,600
Equipment (57,500 – 32,500 – 8,625)		16,375
Current Assets:		
Inventories		25,900
Trade Receivables	46,200	
Less: Allowance	(2,310)	43,890
Prepaid Operating Expenses		500
Cash		151
Total Assets		163,416
Capital & Liabilities:		
Capital	94,501	
Add Net Profit	34,845	
Less Drawings (28,930 + 1,040)	(29,970)	99,376
Non-Current Liabilities:		
10% Loan		15,600
Current Liabilities:		
Trade Payable		33,600
Bank Overdraft		14,500
Wages & Salaries Payable		140
Operating Expenses Payable		200
		163,416

Notes:

N-1: Cost of sales

Opening Stock	27,400
Add Purchases (259,600 – 1,040)	258,560
Less Closing Stock	(25,900)
Total	**260,060**

N-2: Admin and selling expenses

Discount Allowed	(3,370)
Wages & Salaries (52,360 + 140)	(52,500)
Bad debts (1,720 + 2,030)	(3,750)
Other Operating Expenses (38,800 – 500 + 200)	(38,500)
Carriage Outwards	(5,310)
Depreciation (900 + 8,625)	(9,525)
Total	**(112,955)**

Workings:

Property:

90,000 x 1% = 900

Equipment:

57,500 x 15% = 8,625

	Dr	Cr
Depreciation	9,525	
Acc. Depreciation – Property		900
Acc. Depreciation – Equipment		8,625
Wages and Salaries	140	
Wages and Salaries Payable		140
Prepaid Operating Expense (presented in current assets)	500	
Other Operating Expense		500
Other Operating Expense	200	
Payable		200
Drawings	1,040	
Purchases		1,040

Allowance

		Unadjusted bal	280
		Bad debts (bal)	2,030
c/d	2,310		

46,200 × 5% = 2,310

	Dr	Cr
Bad debts	2,030	
Allowance		2,030

A.2

STEVEN CHEE
Statement of Comprehensive Income
For the year ended 31-05-2013

	Notes	'000'
Sales		402,200
Cost of Sales:	N-1	(243,000)
Gross Profit		159,200
Other Income (Discount Received)		4,800
Admin and selling expenses	N-2	(115,160)
Finance cost (loan interest)		(2,100)
Net Profit		**46,740**

STEVEN CHEE
Statement of financial position
For the year ended 31-05-2013

	'000'	'000'
Non-current Assets:		
Land & Building (120,000 – 20,000 – 1,800)		98,200
Equipment (80,000 – 38,000 – 10,500)		31,500
Current Assets:		
Inventory		42,000
Trade Receivables	38,000	
Less: Allowance	(760)	37,240
Cash		300
Bank		1,300
Prepaid Operating Expense		300
		210,840
Capital & Liabilities:		
Capital	121,300	
Add Net Profit	46,740	
Less Drawings	(24,000)	144,040
Non-current Liabilities:		
7% Long-Term Loan		30,000
Current Liabilities:		
Trade payables		36,000
Wages & Salaries Payable		800
Capital & Liabilities:		210,840

Notes:

N-1: Cost of sales

Opening Stock	50,000
Add Purchases (250,000 – 15,000)	235,000
Less Closing Stock	(42,000)
Total	**243,000**

N-2: Admin and selling expenses

Discount Allowed	(18,000)
Wages & Salaries (61,800 + 800)	(62,600)
Bad debts (4,600 + 200)	(4,860)
Other Operating Expense (17,700 – 300)	(17,400)
Depreciation (10,500 + 1,800)	(12,300)
Total	**(115,160)**

Workings:

(b)	Wages & Salaries	800,000	
	Payable		800,000
(c)	Prepaid Operating Expense	300,000	
	Other Operating Expense		300,000

(d) **Allowance Account**

		Un-adjusted bal	500
		Bad debts (bal)	260
c/d	760		

Bad debts 250
Allowance 260

(e) Land ⇒ 120,000 × 1.5% 1,800
Equipment ⇒ (80,000 – 38,000) × 25% 10,500 } 12,300

A.3

SWAN
Statement of Comprehensive Income
For the year ended 31-12-2013

	Notes	**'000'**
Sales		50,021
Cost of Sales:	**N-1**	(32,132)
Gross Profit		17,889
Other Income (Discount Received)		59
Admin and selling Expenses:	**N-2**	(8,691)
Finance cost (loan interest)		(56)
Net Profit		**9,201**

SWAN
Statement of Financial Position
As on 31-12-2013

	'000'	'000'
Non-current Assets:		
Freehold Land		10,300
Motor Van (1,500 – 500)		1,000
Furniture & Fittings (3,800 – 200)		3,600
Current Assets:		
Inventory		4,270
Receivables (7,009 – 260)		6,749
Prepaid Rent		100
Cash in hand		55
Total Assets		26,074
Capital & Liabilities:		
Capital	10,059	
Add Net Profit	9,201	
Less Drawings (2,459+180+230)	(2,869)	16,391
Non-current Liabilities:		
Current Liabilities:		
Bank overdraft	2,522	
Sundry payables	6,735	
Accrued wages	426	9,683
Capital & Liabilities		26,074

Notes:

N-1: Cost of sales

Opening Stock	2,720
Add Purchases (33,436 – 120 - 180)	33,136
Add Carriage Inwards	546
Less Closing Stock	(4,270)
Total	**32,132**

N-2: Admin and selling expenses

Rent (626 – 100)	(526)
Carriage Outwards	(720)
Salaries & Wages (5,226 + 426)	(5,652)
Motor Vehicle Expense (920 – 230)	(690)
Discount Allowed	(65)
Bad debts (240 + 98)	(338)
Depreciation (500 + 200)	(700)
Total	**(8,691)**

Workings:

(2)	Wages & Salaries	426,000	
	Payable		426,000
(3)	Prepaid Rent	100,000	
	Rent		100,000

(4) **Allowance**

		Un-adjust	162
		Bad debts	98
c/d	260		

Bad debts	98	
Allowance		98

(5)	**Depreciation** Van 2,000 × 25%	500	700
	Fixtures 4,000 × 5%	200	
(6)	Drawings	180,000	
	Purchases		180,000
(7)	Drawings	230	
	Motor Vehicle Expenses		230

A.4

BRADBURY & CO
Statement of Comprehensive Income
For the year ended 31-12-2013

	Notes	'000'
Sales		1,292,000
Cost of Sales:	N-1	(554,000)
Gross Profit		738,000
Admin and selling Expenses:	N-2	(474,000)
Finance cost (loan interest 400,000 x 6%)		(24,000)
Net Profit		240,000

BRADBURY & CO
Statement of financial position
As on 31-12-2013

	'000'	'000'
Non-current Assets:		
Plant & Machinery (920,000 – 215,000 – 92,000)		613,000
Current Assets:		
Receivables Control Account	200,000	
Less: Allowance	(4,000)	196,000
Inventory		35,000
Bank		58,000
Prepaid Expense		4,000
Total Assets		906,000

Capital & Liabilities:		
Capital	173,000	
Add Net Profit	240,000	413,000
Non-current Liabilities:		
Loan		400,000
Current Liabilities:		
Payables	73,500	
Accruals (12,000+7,500)	19,500	93,000
		906,000

Notes:

N-1: Cost of sales

Opening Stock	39,000
Add Purchases	550,000
Less Closing Stock	(35,000)
Total	**554,000**

N-2: Admin and selling expenses

Distribution Expense (116,000 + 7,500)	(123,500)
Administrative Expense (241,000 – 4,000)	(237,000)
Bad debts (23,500 – 2,000)	(21,500)
Depreciation	(92,000)
Total	**(474,000)**

Workings:

		Dr	Cr
(b)	Plant & Machinery 920,000 × 10% ⇒	92,000	
(c)	Distribution Expense	7,500	
	Payable		7,500
	Prepaid Administrative Expense	4,000	
	Administrative Expense		4,000

(d) **Allowance Account**

Bad debts (bal)	2,000	Un-adjusted bal	6,000
c/d (200,000 x 2%)	4,000		

Allowance	2,000	
Bad debts		2,000

A.5

MARS
Statement of Comprehensive Income
For the year ended 31-12-2012

	Notes	'000'
Sales		79,060
Cost of Sales	N-1	(53,930)
Gross Profit		25,130
Admin and selling expenses	N-2	(18,817)
Finance cost (interest on loan)		(200)
Net profit		6,113

MARS
Statement of financial position
As on 31-12-2012

	'000'	'000'
Non-current Assets:		
Freehold Property (7,500 – 450 – 75)		6,975
Furniture & Fittings (2,000 – 800 – 200)		1,000
Motor Van (6,300 – 2,370 – 1,260)		2,670
Current Assets:		
Receivables	9,240	
Less: Allowance	(462)	8,778
Bank		2,190
Prepaid Rates		250
Inventory		7,330
Total Assets		29,193
Capital & Liabilities:		
Capital	13,640	
Add Net Profit	6,113	
Drawings	(4,800)	14,953
Non-current Liabilities:		
Loan		4,000
Current Liabilities:		
Payables		10,040
Accrued Expense		200
Capital & Liabilities		29,193

Notes:

N-1: Cost of Sales

Opening Stock	6,740
Add Purchases	54,520
Less Closing Stock	(7,330)
Total	**53,930**

N-2: Admin and selling expenses

Salaries	(8,760)
Rates (1,170 – 250)	(920)
Office Expenses	(3,950)
Motor Expenses	(3,790)
Bad debts	138
Depreciation	(1,535)
Total	**(18,817)**

(2) Prepaid Rate 250

Rate Expense 250

(3) **Allowance**

Bad debts (bal)	138	c/d	600
c/d (9,240 x 5%)	462		

(4) **Depreciation:**

Property	= 7,500 × 1%	⇒	75	
Furniture	= 2,000 × 10%	⇒	200	1,535
Motor Car	= 6,300 × 20%	⇒	1,260	

(5) Interest on Loan = 4,000 × 5% = 200

Expense 200

Expense payable 200

Ans.6 **BOWIE**

(a)

		Dr	Cr
(i)	Purchases	1,200	
	Office Equipment		1,200
	(Purchases wrongly debited to office equipment now rectified)		
(ii)	Trade Payable	2,600	
	Bank		2,600
	(Payment wrongly recorded now rectified)		
(iii)	Rent	3,000	
	Suspense		3,000
	(Rent wrongly credited now rectified)		

(b)

BOWIE
Statement of Comprehensive Income
For the year ended 30-09-2013

	Notes	'000'
Sales		194,000
Cost of Sales:	N-1	(102,200)
Gross Profit		91,800
Admin and selling Expenses:	N-2	(83,700)
Finance cost (bank charges)		(4,000)
Net Profit		4,100

BOWIE
Statement of Financial Position
As on 30-09-2013

	'000'	'000'
Non-current Assets:		
Plant & Machinery (125,000 – 12,500 – 28,000)		84,500
Office Equipment (45,000 – 15,000 – 9,600 – 1,200)		19,200
Current Assets:		
Stock		53,000
Trade Receivables (35,000 – 3,000)	32,000	
Allowance	(1,600)	30,400
Prepaid Payments (1,000 + 1,000)		2,000
Cash		1,000
Bank		--
Total Assets		190,000
Capital & Liabilities:		
Capital	169,000	
Add Net Profit	4,100	
Less Drawings	(22,000)	151,100
Non-current Liabilities:		
		--
Current Liabilities:		
Bank overdraft (3,000 – 4,000 – 2,600)		3,600
Trade Payables (33,000 – 2,600)		30,400
Accrued Expenses		5,000
		190,100

Notes:

N-1: Cost of sales

Opening Stock	31,000
Add Purchases (123,000 + 1,200)	124,200
Less Closing Stock	(53,000)
Total	**102,200**

N-2: Admin and selling expenses

Selling Expenses	(12,000)
Heat & Light	(8,000)
Wages & Salaries (19,000 + 5,000)	(24,000)
Printing & Stationery	(6,000)
Telephone & Fax (6,000 – 1,000)	(5,000)
Rent rates and taxes (4,000+3,000-1,000)	(6,000)
Bad debts (3,000 – 2,400)	(600)
Depreciation (W-1)	(22,100)
Total	**(83,700)**

W-1 Depreciation:

Plant & Machinery = 125,000 × 10% = 12,500

Office Equipment: (45,000 – 1,200 – 35,000) × 33.33% = 9,600

Bank

Cheques	3,000	Bank charges	4,000
		Overdraft (Liability)	(2,600)
c/d	3,600		

Allowance Account

Bad debts (bal)	2,400	Un-adjusted	4,000
c/d (35,000 – 3,000) × 5%	1,600		

vi (b)

Bank 1,300		Payable 1,300		Payable 2,600	
Payable	1,300	Bank	1,300	Bank	2,600
(Recorded)		(Required)		(Rectifying)	

vi (c)

Suspense	3,000		
Rent		1,500	(Recorded)
Bank		1,500	
Rent Expense	1,500		
Bank		1,500	(Required)
Rent Expense	3,000		
Suspense Account		3,000	(Correction)

A.7

Salman
Statement of Comprehensive Income
For the year ended 30-06-2014

	Notes	Rs.
Sales (353,300 – 10,000 – 2,432)		340,868
Cost of sales	N-1	(230,712)
Gross Profit		110,156
Other Income	N-2	15,030
Admin and selling expenses	N-3	(73,642)
Finance cost (loan interest)		(800)
Net Profit		**50,744**

Salman
Statement of Financial Position
As on June 30, 2014

	Rs.	Rs.	Rs.
Non-Current Assets:			
Goodwill		20,000	
Plant & Machinery (45,000 – 4,550 + 500)		40,950	
Factory Building (42,400 – 2,120)		40,280	
Current Assets:			
Stock		237,500	
Trade Receivable	109,420		
Allowance for bad debts	(2,188)	107,232	
Bills Receivable		32,526	
Prepaid Insurance		650	
Cash at Bank		13,512	
Cash in Hand		728	
			493,378
Capital & Liabilities:			
Capital	300,000		
Add: Net Profit	50,744		
Less: Drawings (30,500 – 1,800)	(28,700)	322,044	
Non-Current Liabilities:			
Loan from Bank		40,000	
Current Liabilities:			
Bills Payable		23,150	
Accrued Expenses		3,460	
Creditors		104,724	
			493,378

Notes:

N-1: Cost of Sales

Opening Stock	127,762
Add: Purchases (330,530 – 500)	330,030
Add: Carriage Inwards	10,420
Less: Closing Stock	(237,500)
Total	**230,712**

N-2: Other Income

Interest received	11,930
Other income	3,100
Total	**15,030**

N-3: Admin and selling expenses

Power and utilities	(6,500)
Salaries (40,400 + 1,800)	(42,200)
Rent	(6,992)
Insurance (2,000 – 650)	(1,350)
Advertisement	(4,512)
Miscellaneous Expenses	(4,130)
Depreciation (4,550 + 2,120)	(6,670)
Bad debts	(1,288)
Total	**(73,642)**

Working and adjusments:

		Rs.	Rs.
(i)	Machine	500	
	Purchases		500
(ii)	Salary (150 × 12)	1,800	
	Drawings		1,800
(iii)	Prepaid Insurance	650	
	Insurance Expense		650

(iv) **Calculation of Depreciation:**

Plant & Machinery = 45,000 × 10%	4,500
Add: 500 × 10%	50
	4,550
Factory Building = 42,400 × 5%	2,120

(v) **Allowance for bad debts**

	Rs.		Rs.
		b/d	900
		Bad debts (balance)	1,288
c/d (109,420 × 5%)	2,188		

Answer 8

Fortune traders
Income Statement
For the year ended June 30, 2016

	Notes	Rs. '000'
Sales (28,900 – 90 – 49)		28,761
Less: Cost of sales	N-1	(15,265)
Gross Profit		13,496
Admin and selling expenses	N-2	(6,100)
Finance cost (loan interest)		(300)
Net Profit		7,096

Fortune Traders
Statement of Financial Position
On June 30, 2016

	Rs. '000'	Rs. '000'
Building [3,700 – 1,436 – 113]		2,151
Plant & Machinery [6,650 – 330 – 2,414 – 391]		3,515
Current Assets:		
Trade receivables [3,600 – 49]	3,551	
Allowance (180 – 30)	(150)	3,401
Closing Stock		1,560
Prepayment and other receivables		380
Prepaid selling expense		215
Advance to supplier		330
Cash and bank		5,850
		17,402
Capital & Liabilities:		
Capital	3,000	
Add Profit	7,096	
Less Drawings	(240)	9,856
Non-Current Liabilities:		
Long term loan (5,000 – 625)		4,375
Current Liabilities:		
Current Portion of loan		625
Trade payables (2,080 – 60)		2,020
Rent payable		137
Salaries payable		89
Interest payable		300
		17,402

Notes:

N-1: Cost of Sales

Opening Stock	1,045
Add Purchases (16,000 – 220)	15,780
Less Closing Stock	(1,560)
Total	**15,265**

N-2: Admin and selling expenses

Selling & Admin expenses (5,855 – 215 – 240)	(5,400)
Depreciation – building (W)	(113)
Depreciation –Plant & Machinery (W)	(391)
Office rent	(137)
Salaries	(89)
Bad debts(Reversal of bad debts)	30
Total	**(6,100)**

Workings:

Depreciation:

(3,700 – 1,436) × 5% = 113

(6,650 – 330 – 2,414) × 10% = 391

(i)	Advance Plant & Machinery	330	 330
(ii)	Sale Return Debtor $\frac{35,000}{100} \times 140 = 49,000$	49	 49
(iii)	Interest expense Interest payable 5,000 × 12% × 6/12 = 300 5,000 ÷ 8 = 625 will in current liabilities	300	 300
(iv)	(a) Prepaid selling expense Selling expenses 430,000 ÷ 2 = 215,000 (b) Drawing Selling expenses	215 240	 215 240
(v)	Rent Rent payable Salaries Salaries payable	137 89	 137 89
(vi)	Allowance Bad debts	30	 30
(vii)	(a) Trade payable Purchase Return (Required) (b) Suspense Trade payable Purchase Return (Recorded) (c) Trade payable Suspense (Rectifying)	30 60 60	 30 30 30 60

Answer 9 (a)

Moon Trading

Statement of Comprehensive Income

For the year ended 31-12-2015

	Notes	Rs. In Millions
Sales (2,840 – 2.4)		2,837.60
Less: Cost of sales	N-1	(2,015.4)
Gross Profit		822.2
Other Income	N-2	20.25
Admin and selling expenses	N-3	(536.42)
Finance cost	N-4	(14.25)
Net Profit		291.78

Answer 9 (b)

Moon Trading
Statement of Financial Position
As on 31-12-2015

Non-Current Assets:		**Rs. In Millions**
Fixed Assets (150 + 0.78)		150.78
Accumulated depreciation (45 + 0.04)		(45.04)
		105.74
Current Assets:		
Trade debtors (200 + 3.5 – 2.4)	201.1	
Allowance for doubtful debts	(6.03)	195.07
Closing stock		530
Office supplies		0.15
Prepayments and advances (9 + 1.2)		10.2
Cash and bank balances		5.00
		846.16
Equity & Liabilities:		
Equity:		
Capital	50.00	
Profit for the year	291.78	
Drawings	(0.32)	341.46
Non-Current Liabilities:		
Long term loan (160 – 32)		128.00
Current liabilities:		
Current portion of loan (160 ÷ 5)		32.00
Creditors (320 – 4.5)		315.50
Accruals (25 + 4)		29.00
Advance/Unearned income (workings)		0.20
		846.16

Notes:

N-1: Cost of Sales

Opening stock	410
Purchases (2,141 – 0.78 – 0.32 – 4.5)	2,135.4
Closing stock	(530)
Total	**2,015.40**

N-2: Other Income

Other income	14.8
Service income	1.2
Commission income	4.25
Total	**20.25**

N-3: Admin and selling expenses

Selling and admin expenses	540
Office supplies	(0.15)
Bad debts (0.033-3.5)[Bad debt recovered]	(3.47)
Depreciation	0.04
Total	**536.42**

N-4: Finance cost

Interest on Bank loan (8 + 4)	12
Bank charges (2+0.25)	2.25
Total	**14.25**

Workings:

(1) Closing stock is 530 million.

(2)	(a) Fixed Assets	0.78	
	Purchases		0.78
	Depreciation	0.04	
	Accumulated depreciation		0.04

$0.78 \times 20\% \times 3/12 = 0.04$ (depreciation for three months to be charged)

	(b) Drawings	0.32	
	Purchases		0.32
	(c) Creditors	4.5	
	Purchases Returns		4.5
	(d) Sales Return	2.4	
	Debtors		2.4
(iv)	Debtor	3.5	
	Bad debts		3.5

Adjustment for Allowance

		Unadjusted	6
		Bad debts	0.033
c/d	6.033		

[200 + 3.5 – 2.4 = 201.1 × 3% = 6.033]

(v)	(a) Income receivable	1.2	
	Other income		1.2

(b) $\frac{1.8}{50\%}$ = 3.6 ÷ 9 × 4 = 1.6 is income for the period, remaining 0.2 (1.8 – 1.6) is advance. So

	Other Income	0.2	
	Advance Income		0.2
(vi)	It means now 0.15 asset is increased ; so		
	Stock of Office supplies	0.15	
	Expense		0.15
(vii)	160 × 10% × 3/12 = 4		
	Interest expense	4	
	Interest payable		4

(viii)

(Posted)			**(Required)**			**(Rectification)**		
Bank	4		Bank	4		Suspense	4	
Suspense		4	Bank Charges	0.25		Bank Charges	0.25	
			Commission		4.25	Commission		4.25

Answer 10 (a)

Rainbow Lights
Statement of Comprehensive Income
For the year ended 31-12-2016

	Note	Rs. in million
Sales [750 – 1 – 7]		742.00
Cost of Sales [304 + 2 - 5]		(301.00)
Gross Profit		441.00
Other Income (45 – 4)		41
Admin and selling expenses	N-1	(140.42)
Finance cost (10 + 5)		(15)
Net Profit		326.58

Answer 10 (b)

Rainbow Lights
Statement of Financial Position
As on 31-12-2016

Assets:		
Non-current Assets:		
Property, Plant & Equipment [270 – 8]	262.0	
Accumulated Depreciation [150 – 0.4]	(149.6)	
		112.4
Current Assets:		
Closing Stock [170 – 2 – 15 – 1 + 5]		157
Debtors (400 – 7 – 1 + 3)	394.0	
Less: provision (12 – 0.18)	(11.82)	382.18
Prepayments and other receivables		45
Advance Rent		18
Cash and bank		20
		734.58
Capital & Liabilities:		
Capital [100 – 30]	70	
Add net profit	326.58	
Less Drawings [50 + 1]	(51)	345.58
Non-current Liabilities:		
Long term loan		120.00
Current Liabilities:		
Trade payables [240 – 8]		232.00
Accruals and other payables		28.00
Unearned Income		4.00
Interest payable		5.00
		734.58

Notes:

N-1: Admin and selling expenses

Selling & Admin	(146)
Decrease in bad debts	2.18
Rent in advance	18
Reversal of depreciation on equipment	0.4
Loss of Inventory	(15)
Total	**(140.42)**

Accounting Entries: (Workings)

		Dr	Cr
(a)	Cost of Sales	2	
	Stock		2
(b)	Loss by fire	15	
	Stock		15
(c)	Drawings	1	
	Stock		1
(d)	Sales Return	7	
	Debtor		7
	Stock	5	
	Cost of Sales		5
	(7/140 × 100)		

(ii)	Sales Debtors (20 × 5%)	1	1
(iii)	Debtors Bad debts (bad debts recovered)	2	2
(iv)	Provision Bad debts [7 + 1 – 2 = 6] (debtors are decreased so does provision = 6 × 3% = 0.18	0.18	0.18
(v)	Misc. Income Unearned Income $\left[12 \times \frac{4}{12} = 4\right]$	4	4
(vi)	Advance Rent Rent Expense $\left[24 \times \frac{9}{12} = 18\right]$	18	18
(vii)	Interest Expense Interest Payable $\left[120 \times 10\% \times \frac{5}{12} = 5\right]$ [From August to December]	5	5
(viii)	Payable Equipment Or	8	8

	Receivable	8	
	Equipment		8
	Payable	8	
	Receivable		8
	Accumulated Depreciation	0.4	
	Depreciation		0.4
	[8 × 15% × 4/12]		

Answer 11 (a)

Home Appliances
Statement of Profit or Loss
For the year ended 30-6-2017

	Note	Rs. '000'
Sales		101,120
Less: Sales return (3,000 + 400)		(3,400)
Net sales		97,720
Less: Cost of sales	N-1	(70,250)
Gross Profit		27,470
Add: Other Income	N-2	204
Admin and selling expenses	N-3	(18,496)
Finance cost (580+10)		(590)
Net Profit		8,588

Home Appliances
Statement of Financial Position
As on 30-6-2017

	Rs. '000'	Rs. '000'
Assets:		
Non-Current Assets:		
Fixed Assets – Cost	34,400	
Accumulated Depreciation	(13,232)	21,168
Current Assets:		
Trade receivables [12,500 – 400 – 1,000]	11,100	
Less Allowance for bad debts	(555)	10,545
Stock (workings)		9,310
Prepayments and other receivables		2,350
Receivable against sale of machine		415
Cash and bank		1,300
Total Assets		45,088
Equity and Liabilities:		
Capital	25,500	
Profit	8,588	
Drawings	(4,500)	29,588
Current Liabilities:		
Trade payables		10,200
Accruals and other payables [5,310 – 85 – 35 + 110]		5,300
		45,088

Notes:

N-1: Cost of Sales

Opening Stock	8,200
Add Purchase	70,000
Add Carriage Inwards	1,360
Less Closing Stock [9,000 + 310]	(9,310)
Total	**70,250**

N-2: Other Income

Machine rent income	85
Gain on disposal	9
Misalliance Income	110
Total	**204**

N-3: Admin and selling expenses

Wages and salaries	(5,900)
Discount Allowed (1,600 + 50)	(1,650)
Utility Charges	(2,350)
Running Charges (3,290 + 110)	(3,400)
Depreciation	(5,391)
Bad debts reversed	195
Total	**(18,496)**

Workings:

(i) Sales Return 400

Debtors 400

Stock – Given =	9,000
Add: Damaged Stock [At lower of cost & NRV]	310

$$\text{Cost} = \frac{400}{120} \times 100 = 320$$

NRV = 400 – 90 = 310

	9,310

(ii)

Suspense A/c	940	
Bank charges	10	
Discount allowed (bal.)	50	
Debtors [950 ÷ 95%]		1,000

Recorded			Required		
Bank	940		Bank	940	
Suspense		940	Bank charges	10	
			Discount allowed (bal.)	50	
			Debtor		1,000

(iii) **Allowance A/c**

Bad debts	195	b/d	750
c/d	555		

[12,500 – 400 – 1,000] × 5% = 555

Allowance	195	
Bad debts		195
(iv) Running Expense	110	
Running Expenses payable		110

(v) Entry already recorded:

Cash 120

Accruals and payables 120

$\frac{120,000}{12} \times 8.5 = 85,000$ [from 1-10 to 15-6]

Accruals and payables	85,000	
Rent Income		85,000

Remaining Advance rent is 120,000 – 85,000 = 35,000

Fixed Assets

Unadjusted balance	35,000	Disposal (540 ÷ 90%)	600
		c/d	34,400

Accumulated Depreciation

Disposal (60 + 99)	159	b/d	8,000
		Depreciation (W)	5,391
c/d	13,232		

Depreciation for the year:

35,000 – 8,000 =	27,000	
Less: WDV of disposal (600 – 60)	540	
	26,460	
× 20%	5,292	
Add on disposal [540 × 20% × 11/12]	99	5,391

Depreciation	5,391	
Accumulated depreciation		5,391

Entry of Disposal:

Receivable (450 – 35)	415	
Accrual and other payable	35	
Accumulated depreciation (60 + 99)	159	
Fixed Assets		600
Gain (balance)		9

FINAL ACCOUNTS
PRACTICE QUESTIONS

Question-1

The following is the Trial Balance of Mr. Faisal on 31st December 2002 :

Particulars	Dr.(Rs)	Cr. (Rs)
Capital		4,000
Sundry creditors		5,200
Plant & Machinery	8,000	
Accumulated depreciation		3,000
Office furniture and fittings	460	
Accumulated depreciation		200
Stock as on 1st January, 2002	4,800	
Motor van	1,200	
Sundry debtors	4,570	
Cash in hand	40	
Cash at bank	650	
Wages	15,000	
Salaries	1,400	
Purchases	21,350	
Sales		48,000
Bills payable		560
Bills Receivable	720	
Returns inwards	930	
Provision for doubtful debts		250
Drawings	700	
Returns outwards		550
Rent	600	
Factory lighting and heating	80	
Insurance	630	
General expenses	100	
Bad debts	250	
Discount	650	370
Total	**62,130**	**62,130**

The following adjustments are to be made :

(i) Stock on 31st December, 2002 Rs 5,200:

(ii) 3 months lighting and heating is due, but not paid Rs 30;

(iii) 5% depreciation to be written-off on furniture and plant and machinery using WDV method;

(iv) Write-off further bad debts Rs 70;

(v) The provision for doubtful debts to be increased to Rs 300

(vi) During the year machinery purchased on 1.1.2002 for Rs 2,000, but it was debited to Purchases Account.

Required: Prepare statement of profit or loss and statement of financial position as on December 31, 2002.

Question-2

Following is the Trial Balance of Mr. Asif as at 31.12.1993. You are required to prepare statement of profit or loss for the year ended 31.12.1993 and a statement of financial position as on that date after making necessary adjustments:

Debit Balances	Rs	Credit Balances	Rs
Purchases	60,000	Sales	100,000
Sales Ledger Balances (debtors)	30,400	Purchases Ledger Balances (creditors)	23,912
Returns Inward	2,000	Discount Received	1,088
Discount Allowed	2,000	Returns Outward	7,400
Building	44,000	Capital	53,200
Sundry expenses	2,000	Suspense Account	2,000
Repair expense	2,000	Rental Income	1,000
Wages	4,000	Provision for Bad Debts	2,000
Salaries	6,000	Commission	4,000
Prepaid expense	1,200		
Stock-in-Trade (1.1.1993)	20,000		

Trade Expenses	4,000		
Insurance	400		
Cash at Bank	12,600		
Deposit with Bank of Punjab – long term	4,000		
	194,600		**194,600**

Adjustments:

(i) Stock-in-trade on 31.12.1993 was valued at Rs 20,000.

(ii) Interest receivable from Bank of Punjab is @ 10% pa not yet recorded.

(iii) Out of purchases, goods of Rs 4,000 was distributed as free samples

(iv) Suspense Account represents a cheque received from Amjad a customer, in settlement of Rs 2,400 due from him. The cheque was duly deposited and credited by the Bank.

(v) Maintain provision for bad debts @ 5% on Debtors.

Question-3

Prepare a statement of profit or loss and statement of financial position as on December 31, 2002, from the following Trial Balance and the adjustment items:

Particulars	Dr. (Rs)	Cr. (Rs)
Opening stock	46,000	
Purchases and Sales	442,000	820,000
Sales returns and Purchases returns	8,000	12,000
Discount received		2,200
Wages	43,500	
Salaries	66,000	
Carriage inwards	39,100	
Advertising expenses	10,200	
Bills receivable	9,000	
12% Bank loan (taken on 1st November 2002)		150,000
Office equipment	199,700	
Land and building	336,000	
Provision for doubtful debts		3,200
Sundry Debtors and Sundry Creditors	45,000	48,300
Rates and taxes	5,300	
Office electricity expenses	9,400	
Telephone charges	4,400	
Cash at Bank	18,000	
Printing and Stationery	11,200	
Postage stamps	1,090	
Furniture	200,000	
Petty cash	210	
Prepaid printing	1,200	
Insurance premium	3,000	
Carriage outwards	12,000	
Bad debts	800	
Interest on Bank loan paid	1,500	
Capital Account		476,900
Total	**1,512,600**	**1,512,600**

Adjustment items:

(a) Closing stock was valued at Rs. 38,000 on 31st December 2002.

(b) Goods worth Rs.2,500 were distributed by salesmen as free samples, but no entry has been made for this.

(c) Depreciate furniture by 7-1/2% p.a and office equipment by 10% p.a.

(d) Provision for doubtful debts to be maintained at 5% on debtors.

(e) Commission of Rs 1,300 was earned but not yet received.

(f) Rates and taxes of Rs 800 was paid in advance for 2003.

(g) Creditors include a debt of Rs 4,000 to Mr. Nayak who is also included in the list of debtors for Rs. 5,000 and therefore, to be set off before calculating the provision.

Question-4

Mr. Taimoor has extracted the following Trial Balance from his books as on March 31, 2003:

Particulars	Dr. (Rs)	Cr. (Rs)
Drawings	16,000	
Cash	6,760	
Petty cash	1,000	
Equipment	20,000	
Opening stock	50,000	
Salary	12,000	
Sundry debtors	50,000	
Wages	40,000	
Bank	21,000	
Capital		34,000
Rent	9,000	
Electricity	6,000	
Motorcar	10,240	
Advertising	9,000	
Sundry creditors		35,000
Purchases / Sales	400,000	600,000
Postage and telephone	3,000	
Discount	11,400	
General charges	4,000	
Petty cash expenses	9,600	
Suspense		10,000
TOTAL	**679,000**	**679,000**

You are required to prepare a statement of profit or loss and a statement of financial position using the following information:

(a) Closing stock as on 31st March, 2003 amounted to Rs 75,000 at cost.

(b) Petty cash expenses of Rs. 400 have been completely omitted from books.
(c) Discounts allowed amounting to Rs 1,000 had been posted to the debit of Sundry Debtors.
(d) Cash withdrawn from bank Rs 4,000 had not been entered in the bank column of the cash book.
(e) Sales Account had been under casted on the credit side by Rs 4,000.
(f) The motor car is depreciated at 10%.
(g) Equipment was purchased at start of year. On the date of purchase the life was 5 years.
(h) No entry had been passed in the books for stock withdrawn from the business by the proprietor Rs 10,000.
(i) Telephone bills amounting to Rs 1,000 remained unpaid.

Question-5

Mr. Syed Aamir Ali, a trader has extracted the following Trial Balance from his books as on 31st March, 2003:

Particulars	Dr. (Rs)	Cr. (Rs)
Purchases	400,000	
Sundry debtors	150,000	
Cash in hand	12,000	
Cash at bank	8,000	
Rent, rates and taxes	3,000	
Insurance premium	9,000	
Salaries	45,000	
Carriage outwards	21,000	
Carriage inwards	18,000	
Sundry creditors		50,000
Research and Development expense	9,000	
Furniture and fittings	30,000	
Accumulated depreciation		7,000
Deposit with supplier (advance to supplier)	6,000	
Office equipment	15,000	
Accumulated depreciation		5,000
Bad debts	4,000	

Sales		700,000
Opening stock	30,000	
Electricity expenses	2,000	
Total	**762,000**	**762,000**

The following further information is provided:

1. A purchase invoice for Rs 15,000 received from a creditor has not been entered through oversight.
2. Depreciation is to be provided on straight-line method on furniture and fittings and office equipment at 5%.
3. Goods costing Rs 5,000 were dispatched out on 29th March. The sale, however, was recorded on 2nd April 2003, when an invoice for Rs 7,500 was raised against the customer.
4. Insurance premium includes a prepaid amount of Rs 1,000.
5. Two cheques from customers of Rs 700 and Rs 1,300, were dishonored on 30th March. These had earlier been deposited with the bank.
6. Provide 2% on sundry debtors for doubtful debts.
7. Physical stock of goods on hand on 31st March, 2003 at cost was Rs 100,000.

Required: Prepare statement of profit or loss and statement of financial position from the above information.

SOLUTIONS
PRACTICE QUESTIONS

Answer No. 1

Mr. Faisal
Income Statement
For the year ended December 31, 2002

	Notes	Rs.
Sales (48,000 – 930)		47,070
Cost of Sales	N-1	(18,400)
Gross Profit		**28,670**
Other Income (Discount received)		370
Admin and selling Expenses	N-2	(19,223)
Net Profit		**9,817**

Mr. Faisal
Statement of Financial Position
As on December 30, 2002

	Rs.	Rs.	Rs.
Assets:			
Non-Current Assets:			
Plant & Machinery (8,000 – 2,000)		10,000	
Less: Account Depreciation (3,000 + 350)		(3,350)	6,650
Furniture		460	
Less: Account Depreciation (200 + 13)		(213)	247
Motor Van			1,200
Current Assets:			
Debtors (4,570 – 70)	4,500		
Less: Allowance for Doubtful Debts (W-1)	(300)	4,200	
Bills Receivable		720	
Stock		5,200	
Cash in Hand		40	
Cash at Bank		650	10,810
			18,907
Capital & Liabilities:			
Capital	4,000		
Add: Net Profit	9,817		
Drawings	(700)	13,117	
Current Liabilities:			
Trade Creditors	5,200		
Lighting & Heating Payable	30		
Bills Payable	560	5,790	
			18,907

Notes:

N-1: Cost of sales

Opening Stock	4,800
Purchases (21,350 – 550 – 2,000)	18,800
Closing Stock	(5,200)
Total	**18,400**

N-2: Admin and selling expenses

Wages	(15,000)
Salaries	(1,400)
Rent	(600)
Lighting and Heating	(110)
Insurance	(630)
General Expenses	(100)
Bad Debts (250 + 70 + 50)	(370)
Discount Allowed	(650)
Depreciation – Furniture (460 – 200) × 5%	(13)
Depreciation – Plant & Machinery	(350)
Total	**(19,223)**

WORKINGS:

(W-1) **Allowance Account**

	Rs.		Rs.
		Unadjusted b/d	250
		Bad debts	50
c/d	300		
	300		**300**

Depreciation Expense:

On Opening Assets (8,000 – 3,000) × 5%	250
On Additions (2,000 × 5%)	100
	350

Answer No. 2

Mr. Asif
Statement of Comprehensive Income
For the year ended December 31, 1993

		Rs.
Sales (100,000 – 2,000)		98,000
Cost of Sales	N-1	(48,600)
Gross Profit		**49,400**
Other Income	N-2	6,488
Admin & selling expenses	N-3	(24,200)
Net Profit		**31,688**

Mr. Asif
Statement of Financial Position
As on December 31, 1993

	Rs.	Rs.	Rs.
Assets:			
Non-Current Assets:			
Building		44,000	
Deposits with Bank of Punjab		4,000	48,000
Current Assets:			
Debtors (30,400 – 2,400)		28,000	

Less: Allowance		(1,400)	26,600
Prepaid Expenses			1,200
Interest Receivable			400
Stock			20,000
Cash at Bank			12,600
			108,800
Capital & Liabilities:			
Capital	53,200		
Profit	31,688	84,888	
Current Liabilities:			
Trade Creditors		23,912	
			108,800

Notes:

N-1: Cost of sales

Opening Stock	20,000
Purchases (60,000 – 4,000)	56,000
Less: Purchase Return	(7,400)
Closing Stock	(20,000)
Total	**48,600**

N-2: Other income

Interest Income	400
Rental Income	1,000
Commission Income	4,000
Discount Received	1,088
Total	**6,488**

N-3: Admin and selling expenses

Wages	(4,000)
Repairs	(2,000)
Salaries	(6,000)
Trade Expenses	(4,000)
Insurance	(400)
Advertisement (free samples)	(4,000)
Discount Allowed (2,000 + 400)	(2,400)
Bad debts reversed	600
Sundry Expenses	(2,000)
Total	**(24,200)**

WORKINGS:

(i) Entry for Point (iv)

Posted	**Required**	**Rectifying**
Bank 2,000 Suspense 2,000	Bank 2,000 Discount Allowed 400 Debtor 2,400	Suspense 2,000 Discount Allowed 400 Debtor 2,400

(ii) **Debtor Account**

	Rs.		Rs.
Un-adjusted balance	30,400	Suspense	2,000
		Discount allowed	400
		c/d	28,000
	30,400		**30,400**

Allowance Account

	Rs.		Rs.
Bad Debt (bal)	600	Unadjusted balance	2,000
c/d (28,000 × 5%)	1,400		28,000
	2,000		**2,000**

Answer No. 3

Mr. XYZ
Statement of Comprehensive Income
For the year ended December 31, 2002

	Notes	Rs.
Sales (820,000 – 8,000)		812,000
Cost of Sales	N-1	(474,600)
Gross Profit		**337,400**
Other Income	N-2	3500
Admin and selling Expenses	N-3	(202,410)
Finance cost (1,500 + 1,500) **(W-2)**		(3,000)
Net Profit		**135,490**

Mr. XYZ
Statement of Financial Position
As on December 31, 2002

	Rs.	Rs.	Rs.
Assets:			
Non-Current Assets:			
Land & Building		336,000	
Furniture (200,000 – 15,000)		185,000	
Office Equipment (199,700 – 19,970)		179,730	700,730
Current Assets:			
Debtors (45,000 – 4,000)		41,000	
Less: Allowance for Doubtful Debts		(2,050)	38,950
Bills Receivable			91,000
Commission Receivable			1,300
Prepaid Rates			800
Prepaid Printing			1,200
Stock			38,000
Petty Cash			210
Cash at Bank			18,000
			808,190
Capital & Liabilities:			
Capital	476,900		
Add: Profit	135,490	612,390	
Non-Current Liabilities:			
Bank Loan		15,000	
Current Liabilities:			
Trade Creditors (48,300 – 4,000)		44,300	
Interest Payable (W-2)		1,500	
			808,190

Notes:

N-1: Cost of sales

Opening Stock		46,000
Purchases (442,000 – 2,500)	439,500	
Less: Purchase Return	(12,000)	427,500
Carriage Inwards		39,100
Closing Stock		(38,000)
Total		**474,600**

N-2 Other income

Discount Received	2,200
Commission Income	1,300
Total	**3,500**

N-3: Admin and selling expenses

Wages	(43,500)
Salaries	(66,000)
Advertisement (10,200 + 2,500)	(12,700)
Rate & Taxes (5,300 - 800)	(4,500)
Office Electricity	(9,400)
Telephone	(4,400)
Printing & Stationery	(11,200)
Postage Stamp	(1,090)
Insurance	(3,000)
Carriage outwards	(12,000)
Bad debts (800-1150)	350
Depreciation – Furniture (200,000 × 75%)	(15,000)
Depreciation – Office Equipment (199,700 × 10%)	(19,970)
Total	**(202,410)**

WORKINGS:

(i) **Allowance Account**

	Rs.		Rs.
Bad debts (bal)	1,150	Unadjusted	3,200
c/d (41,000 x 5%)	2,050		
	3,200		**3,200**

(ii)

Interest expense in Trial balance	1,500
Loan taken on 1st November, 2002	
150,000@ 12% × $\frac{2}{12}$	3,000
Interest payable not yet recorded	1,500

Answer No. 4

Mr. Taimoor
Statement of Comprehensive Income
For the year ended March 31, 2003

		Rs.	Rs.
Sales (600,000 + 4,000)			604,000
Cost of Sales		N-1	(365,000)
Gross Profit			**239,000**
Admin and selling expenses		N-2	(110,424)
Net Profit			**128,576**

Mr. Taimoor
Balance Sheet
As on March 31, 2003

	Rs.	Rs.	Rs.
Assets:			
Non-Current Assets:			
Equipment (20,000 – 4,000)		16,000	
Motor Car (10,240 – 1,024)		9,216	25,126
Current Assets:			
Debtors (50,000 – 2,000)		48,000	
Stock		75,000	
Petty Cash (1,000 – 400)		600	
Cash		6,760	
Bank (21,000 – 4,000)		17,000	147,360
			172,576
Capital & Liabilities:			
Capital	34,000		
Profit	128,576		
Drawings (16,000 + 10,000)	(26,000)	136,576	
Non-Current Liabilities:			
Trade Creditors		35,000	
Telephone Payable		1,000	36,000
			172,576

Notes:

N-1: Cost of sales

Opening Stock	50,000
Purchases (400,000 – 10,000)	390,000
Closing Stock	(75,000)
Total	**365,000**

N-2: Admin and selling expenses

Wages	(40,000)
Salaries	(12,000)
Rent	(9,000)
Electricity	(6,000)
Advertising	(9,000)
Discount Allowed	(11,400)
General Charges	(4,000)
Petty Cash Expenses (9,600 + 400)	(10,000)

Postage and Telephone (3,000 + 1,000)	(4,000)
Depreciation – Motor Car (10,240 × 10%)	(1,024)
Depreciation – Equipment	(4,000)
Total	**(110,424)**

WORKINGS:

(i)

Suspense Account

	Rs.		Rs.
Debtors (1,000 × 2)	2,000	Unadjusted balance	10,000
Bank A/c	4,000		
Sales	4,000		
	10,000		**10,000**

(ii)

Debtor Account

	Rs.		Rs.
Unadjusted balance	50,000	Suspense	2,000
		c/d	48,000
	50,000		**50,000**

Answer No. 5

Mr. Syed Aamir Ali
Statement of Comprehensive Income
For the year ended March 31, 2003

	Rs.	Rs.
Sales (700,000 + 7,500)		707,500
Cost of Sales	**N-1**	(363,000)
Gross Profit		**344,500**
Admin and selling expenses	**N-2**	(97,440)
Net Profit		**247,060**

Mr. Syed Aamir Ali
Statement of Financial Position
As on March 31, 2003

	Rs.	Rs.	Rs.
Assets:			
Non-Current Assets:			
Furniture and Fittings		30,000	
Less: Accumulated Depreciation (7,000 + 1,500)		(8,500)	21,500
Office Equipment		15,000	
Less: Accumulated Depreciation (5,000 + 750)		(5,750)	9,250
Current Assets:			
Debtors (150,000 + 7,500 + 2,000)		159,500	
Less: allowance for bad debts		(3,190)	156,310
Prepaid Insurance			1,000
Deposit with Suppliers			6,000
Stock			100,000
Cash in Hand			12,000
Cash at Bank (8,000 – 700 -1,300)			6,000
			312,060
Capital & Liabilities:			
Capital	--		
Add Net Profit	247,060	247,060	
Current Liabilities:			
Trade Creditors (50,000 + 15,000)		65,000	
			312,060

Note

N-1: Cost of sales

Opening Stock	30,000
Purchases (400,000 + 15,000)	415,000
Carriage Inwards	18,000
Closing Stock	(100,000)
Total	**363,000**

N-2: Admin and selling expenses

Rent, Rates and Taxes	(3,000)
Salaries	(45,000)
Carriage Outwards	(21,000)
Insurance (9,000 – 1,000)	(8,000)
Electricity	(2,000)
Bad Debts (4,000 + 3,190)	(7,190)
Research & Development Expense	(9,000)
Depreciation – Furniture (30,000 × 5%)	(1,500)
Depreciation – Office Equipment (15,000 × 5%)	(750)
Total	**(97,440)**

WORKINGS:

(i) As the goods are despatched on 29th March, so sale should be recorded in the current period. It is wrongly recorded in the next accounting period, which is now rectified.

(ii) **Debtors Account**

	Rs.		**Rs.**
Unadjusted balance	150,000		
Bank (700 + 1,300)	2,000		
Sales	7,500	c/d	159,500
	159,500		**159,500**

(iii) **Allowance Account**

	Rs.		**Rs.**
		Unadjusted balance	--
		Bad Debts (bal)	3,190
Closing (159,500 × 2%)	3,190		
	3,190		**3,190**

Extra practice questions:

Q. Following is the trial balance of **Sofia Trader (ST)** for the year ended 30 June 2018:

	Debit	Credit
	---------- Rs.'000 ----------	
Equipment - cost	17,000	
Equipment - accumulated depreciation - 1 Jul 2017		4,800
Vehicles - cost	3,000	
Vehicles - accumulated depreciation - 1 Jul 2017		1,200
Inventory - 1 Jul 2017	5,500	
Trade receivables	5,350	
Provision for doubtful receivables		220
Prepaid insurance - 1 Jul 2017	140	
Advance	384	
Bank deposit (invested on 1 Feb 2017 at 7%)	1,400	
Cash and bank balances	620	
Capital		16,000
Drawings	352	
Trade payables		3,500
Accruals and other payables		1,520
Sales		32,350
Purchases	21,000	
Returns	950	700
Salaries and utilities	2,790	
Rent	1,000	
Discounts	270	220
Other expenses	480	
Insurance	300	
Bad debts	106	
Interest income on bank deposit		82
Suspense account		50
	60,642	**60,642**

Following further information is available:

(i) Cost of closing physical inventory was Rs. 7,400,000. Inventory included goods costing Rs. 240,000 which were damaged in the warehouse. These goods can be sold for Rs. 250,000 after incurring a cost of Rs. 16,000.

(ii) Rent includes payment of annual rent of Rs. 240,000 expiring on 30 November 2018 for owner's residence.

(iii) Prepaid insurance represents premium which expired on 31 January 2018 while insurance represents annual premium which is expiring on 31 January 2019.

(iv) Suspense account represents goods returned by ST which were debited to supplier's account.

(v) On 29 June 2018, dishonoured cheque of Rs. 285,000 was returned by a bank. No entry has been made in the books for this return. This cheque was received from a customer net of 5% settlement discount.

(vi) ST maintains a 4% provision against trade receivables.

(vii) ST paid Rs. 388,000 (net of 3% settlement discount) which was debited to supplier's account with the same amount.

(viii) On 1 March 2018, an equipment was sold for Rs. 400,000 and its sale proceeds were credited to the equipment account. This equipment had been purchased at a cost of Rs. 500,000 and on 1 July 2017 its book value was Rs. 360,000.

(ix) Advance represents 40% payment made for purchase of vehicle. Remaining balance would be paid in September 2018. No entry was passed when the vehicle was delivered on 1 June 2018.

(x) ST depreciates equipment and vehicles at 15% and 25% respectively using reducing balance method.

Required:

(a) Prepare statement of profit or loss for the year ended 30 June 2018

(b) Prepare statement of financial position as at 30 June 201

Ans.

Sofia Traders
Statement of Profit or Loss
For the year ended 30-06-2018

	Note	Rs "000"
Sales (32,350-950)		31,400
Cost of sales	N-1	(18,356)
Gross Profit		13,044
Other Income	N-2	406
Admin and selling expenses	N-3	(7,004)
Net Profit		**6,446**

Sofia Traders
Statement of Financial Position
As on June 30, 2018

		---------- Rs. in "000" ----------	
Assets:			
Non Current Assets:			
Equipment (16,900-6,496)		10,404	
Vehicle (3,960-1,670)		2,290	12,694
Current Assets:			
Stock (7,400-6)		7,394	
Trade Receivable	5,650		
Allowance for bad debts	(226)	5,424	
Prepayments (140-140+175)		175	
Interest Receivable		16	
Bank Deposit		1,400	
Cash and Bank Balances (620-285)		335	14,744
			27,438
Equity & Liabilities:			
Capital	16,000		
Add: Net Profit	6,446		
Less: Drawings (352+240)	(592)	21,854	
Current Liabilities:			
Creditors (3,500-12)		3,488	
Accruals and other payables		1,520	
Vehicle payable		576	
			27,438

Notes:

N-1: Cost of Sales

Opening Stock	5,500
Add: Purchases (21,000-700-50)	20,250
Less: Closing Stock (7,400 – 6)	(7,394)
Total	**18,356**

N-2: Other Income

Gain on disposal	76
Discount received (220+12)	232
Interest Income (82+16)	98
Total	**406**

N-3: Admin and selling expenses

Salaries	(2,790)
Rent (1,000-240)	(760)
Discount Allowed (270-15)	(255)
Insurance (300-175+140)	(265)
Bad debts (106+6)	(112)
Depreciation – Equipment	(1,872)
– Vehicle	(470)
Other Expenses	(480)
Total	**(7,004)**

Working & Adjustments

			Rs.	Rs.
(i)	Cost of damaged goods NRV of damaged goods (250,000-16,000) 7,400,000 – 6,000 = 7,394,000		240,000 234,000	
(ii)	Drawings Rent		240	240
(iii)	Insurance Expense Prepaid Insurance (300 / 12 x 7)		140	140
(iv)	Creditor 50 Purchase return 50 **(Required)**	Creditor 50 Suspense 50 **(Posted)**	Suspense 50 Purchase return 50 **(Rectifying)**	
(v)	Debtor Bank Discount allowed		300	285 15
(vi)	Creditor 400 Discount Received 12 Cash 388 388,000 / 97 x 100 **(Required)**	Creditor 388 Cash 388 **(Posted)**	Creditor 12 Discount received 12 **(Rectifying)**	
(vii)	Cash 400 Acc. Dep 176 [(500-360)+36] Equipment 500 Gain 76 360,000 x 15% x 8/12 =36 **(Required)**	Cash 400 Equipment 400 **(Posted)**	Equipment 400 Accumulated depreciation 176 Equipment 500 Gain 76 **(Rectifying)**	
(viii)	Vehicle (384 / 40%) Advance Payable		960	384 576

Debtors

	Rs.		Rs.
b/d	5,350		
Bank	285		
Discount allowed	15	c/d	5,650

Allowance for bad debts

	Rs.		Rs.
		b/d	220
		Bad debts	6
c/d (5,650 x 4%)	226		

Bad Debt	6	
Allowance		6

Equipment

	Rs.		Rs.
b/d (unadjusted)	17,000	Disposal	500
Cash	400		
		c/d	16,900

Accumulate depreciation

	Rs.		Rs.
Disposal	176	b/d	4,800
		depreciation	1,872
c/d	6,496		

Depreciation of Equipment:

Opening WDV [17,400 – 4,800]	12,600
Less: Opening WDV of disposal (500 - 140)	(360)
	12,240
X 15%	1,836
360 x 15% x 9/12	36
Depreciation	1,872

Vehicle

	Rs.		Rs.
b/d	3,000		
Addition	960		
		c/d	3,960

Accumulate depreciation

	Rs.		Rs.
		b/d	1,200
		depreciation	470
c/d	1,670		

Depreciation of Vehicle:

[3,000 – 1,200] x 25%	450
960 x 25% x 1/12	20
	470

Interest Receivable	16	
Interest Income		16
(1,400 x 7% - 82)		

Q. Following is the trial balance of **Tulip Enterprises (TE)** for the year ended 31 December 2017:

Rs. in '000

	Debit		Credit
Cash and bank balances	2,320	Trade payables	3,250
Trade receivables	4,400	Accruals and other payables	1,320
Stock-in-trade 31-12-2017	3,900	Provision for doubtful receivables	220
Prepayments and advances	1,740	Accumulated depreciation	4,630
Property, plant & equipment – cost	12,500	12% Long-term loan	5,150
Drawings	490	Capital	6,000
Cost of sales	23,580	Sales	35,230
Salaries and wages	2,610	Miscellaneous income	940
Fuel and power	450		
Bad debt expense	230		
Rent and insurance	2,900		
Repair and maintenance	920		
Financial charges	700		
	56,740		**56,740**

Additional information:

(i) While carrying out the physical inventory count at year-end, following matters were identified:
- Goods costing Rs. 1,000,000 were slightly defective. These can be sold for Rs. 1,130,000 after incurring a cost of Rs. 200,000.
- Goods costing Rs. 670,000 purchased on credit were returned to a supplier on 28 December 2017 but the return was not recorded in the books.

(ii) A machine costing Rs. 450,000 was received on 1 October 2017 against 100% advance payment. The advance has not yet been adjusted due to non-receipt of the invoice.

(iii) On 1 October 2017, 50% advance received for an annual maintenance contract of Rs. 480,000 was credited to miscellaneous income. Remaining amount would be received at the end of the contract. Services are rendered evenly throughout the contract period.

(iv) Maintenance services for Rs. 150,000 were rendered in December 2017 but income has been recorded in January 2018 on receipt of the amount.

(v) Interest on the loan is paid in arrears on 1 April and 1 October each year. Interest accrued for the quarter ended 31 December 2017 has been credited to loan account.

(vi) Rent and insurance include:
- annual insurance premium of Rs. 800,000 for the health policy arranged by TE for the department heads and the owner's family members. Premium pertaining to the owner's family members is Rs. 200,000. The policy is valid up to 30 June 2018.
- Rs. 1,200,000 paid against the annual rent agreement expiring on 31 August 2018. According to the rent agreement, the rent paid would not be refunded in case the building is vacated earlier.

(vii) TE maintains provision for doubtful receivables according to the age analysis of the outstanding balances. Relevant details are as under:

	Trade receivables as on 31 December 2017				
	Less than 3 months	**4-6 months**	**7-12 months**	**More than 1 year**	**Total**
Outstanding balances (Rs. in '000)	1,970	1,000	900	530	4,400
Required provision	-	5%	10%	20%	

(viii) TE depreciates property, plant & equipment at 15% per annum on reducing balance method.

Required:

Prepare the followings:

a. Statement of profit or loss for the year ended 31 December 2017

b. Statement of financial position as at 31 December 2017

Tulip Enterprises
Statement of Profit or Loss
For the year ended 31-12-2017

		Rs. '000'
Sales		35,230
Cost of sales (23,580 +70)		(23,650)
Gross Profit		11,580
Add: Other income (940 - 120 + 150)		970
Admin and selling expenses	N-1	(7,033)
Finance cost		(700)
Net Profit		4,817

Tulip Enterprises:
Statement of Financial Position
As on 30-06-2017

ASSETS:		
Non-Current Assets:		
Property, Plant & Equipment [12,500 + 450]		12,950
Less: Accumulated Depreciation [4,630 + 1,197]		(5,827)
		7,123
Current assets:		
Stock in trade (3,900 -70 -670)		3,160
Trade Receivables	4,400	
Less: Allowance (W)	(246)	4,154
Prepayments & Advances [1,740 – 450]		1,290
Prepaid Insurance		300
Prepaid Rent		800
Maintenance services receivable		150
Cash and bank		2,320
Total Assets		19,297
Equity & Liabilities:		
Capital	6,000	
Add Net Profit	4,817	
Less: Drawings [490 + 200]	(690)	10,127
Non-Current Liabilities:		
Long term loan [5,150 – 150 (W)]		5,000
Current Liabilities:		
Trade Payables [3,250 – 670]		2,580
Accruals and other payables		1,320
Unearned Rent Income		120
Interest payable		150
Total Equity & Liabilities		19,297

Notes:

N-1: Admin and selling expenses

Salaries and wages	(2,610)
Fuel and power	(450)
Bad debts expense [230 + 26]	(256)
Rent and Insurance [2,900 – 200 – 300 – 800]	(1,600)
Depreciation [working]	(1,197)
Repair and Maintenance	(920)
Total	**7,033**

Workings:

(i) (a)

Cost of goods	=	1,000,000
NRV [1,130,000 – 200,000]	=	930,000
Loss	=	70,000

	Dr	Cr
Cost of Sales	70,000	
Stock		70,000

(b)

	Dr	Cr
Creditor	670,000	
Stock		670,000

(ii)

	Dr	Cr
Machine	450,000	
Advance		450,000

(iii) 480,000 × 3/12 = 120,000 [Rent Income]

Required:

	Dr	Cr
Cash (480,000 × 50%)	240,000	
Unearned Income		120,000
Rent Income		120,000

Posted

	Dr	Cr
Cash	240,000	
Rent Income		240,000

Rectifying:

	Dr	Cr
Rent Income	120,000	
Unearned Income		120,000

(iv)

	Dr	Cr
Receivable	150,000	
Maintenance Income (other Income)		150,000

(v) Lets x is the amount of loan without including interest.

x + x × 12% × 3/12 = 5,150

x + 0.03x = 5,150

1.03x = 5,150

x = 5,000

	Dr	Cr
Loan	150	
Interest payable		150

(vi) (a)

	Dr	Cr
Drawings	200,000	
Rent and Insurance	200,000	

[800,000 – 200,000] × 6/12 = 300,000

	Dr	Cr
Prepaid Insurance	300,000	
Rent and Insurance		300,000

(b)

	Dr	Cr
Prepaid Rent	800,000	
Rent and Insurance		800,000

[1,200,000 × 8/12]

(vii)

Provision

		b/d	220
		Bad debts	$\boxed{26}$
c/d (working below)	246		

	Dr	Cr
Bad debts	26	
Allowance		26

Workings:

1,000 × 5%	=	50
900 × 10%	=	90
530 × 20%	=	106
		246

(viii) **Depreciation for the year:**

[12,500 – 4,630] × 15%	=	1,180.50
+ 450 × 15% × 3/12	=	16.875
		1,197.375

Q. Following is the summarised trial balance of **Qambar Enterprises (QE)** for the year ended 31 December 2018:

Rs. in '000'

	Debit		Credit
Furniture – cost	2,535	Accumulated dep. at 1 Jan 2018:	
Vehicles – cost at 1 Jan 2018	4,500	– Furniture	975
Inventories at 1 Jan 2018	4,450	– Vehicles	1,450
Trade receivables	2,970	Capital at 1 Jan 2018	5,223
Office and sales supplies	210	12% Bank loan	1,500
Cash and bank balances	746	(obtained on 1 April 2018)	
Purchases	12,364	Trade payables	3,943
Returns	826	Sales	18,184
Salaries and commission	1,295	Other income	275
Rent and insurance	545		
Utilities and repairs	420		
Goods withdrawn	644		
Provision for doubtful receivables	45		
	31,550		**31,550**

Additional information:

(i) Inventories as at 31 December 2018 were valued at Rs. 3,860,000. Office and sales supplies costing Rs. 90,000 are still unused. However, 30% of these supplies are not usable due to deterioration in quality.

(ii) Rent and insurance includes Rs. 75,000 paid for a photocopying machine. The machine was obtained on 1 November 2018 at a fixed rent of Rs. 75,000 per quarter and an additional Re. 0.40 for each copy. 40,000 copies have been made by QE up to 31 December 2018.

(iii) QE received 5% discount on list price of goods purchased for cash which was credited to other income. List price of such purchases was Rs. 2,500,000.

(iv) Cost of office repairs amounting to Rs. 85,000 was paid by the owner from personal cash.

(v) On 1 November 2018, a vehicle was completely destroyed in an accident. In December 2018, insurance company agreed to pay Rs. 500,000 in January 2019. The vehicle was purchased for Rs. 600,000 on 1 January 2016.

(vi) On 1 September 2018, a vehicle was invested into the business by the owner. The vehicle was purchased by the owner on 1 July 2015 for Rs. 1,050,000 and had a fair value of Rs. 960,000 on 1 September 2018.

(vii) QE depreciates vehicles at 10% using straight line method while furniture is depreciated at 15% using reducing balance method. Cost of furniture includes an item of furniture purchased for Rs. 400,000 on 1 May 2018.

(viii) Sales include Rs. 335,000 received from a customer though the related goods were dispatched on 5 January 2019.

(ix) Trade receivables include Salman's balance of Rs. 370,000. It has been decided to set-off Rs. 100,000 payable by QE to Salman and make a specific provision of 30% against the remaining balance.

(x) A general provision of 4% of remaining trade receivables is maintained. Trade receivables amounting to Rs. 131,000 were written off and debited to provision for doubtful receivables during 2018.

Required:

(a) Prepare statement of profit or loss for the year ended 31 December 2018. (12)

(b) Prepare statement of financial position as at 31 December 2018. (11)

Ans. **Qambar Enterprises**

a) Statement of profit or loss for the year ended 31 December 2018

	Note	Rs
Sales (18,184 - 335)		17,849
Return inward		(826)
Net sales		**17,023**
Cost of sales	N-1	(12,829)
Gross Profit		4,194
Add: Other income	N-2	220
Admin and selling expenses	N-3	(3,399)
Finance cost		(135)
Net profit		**880**

(b) Statement of financial position as at 31 December 2018

		Rs. in '000
Assets		
Non-current assets:		
Vehicle - cost		4,860
Accumulated depreciation		(1,752)
		3,108
Furniture - cost		2,535
Accumulated depreciation		(1,189)
		1,346
		4,454
Current assets		
Trade receivables	(2,970 –100)	2,870
Provision of doubtful receivables		(185)
		2,685
Inventories		3,860
Office and sales supplies	(90 - 27)	63
Prepaid rent		9
Insurance claim		500
Cash and bank balances		746
		7,863
		12,317
Equity and liabilities:		
Equity		
Capital	(5,223+85+960)	6,268
Profit for the year		880
Drawings		(644)
		6,504
Non-current liability		
Bank loan		1,500
Current liabilities		
Trade payables	(3,943–100)	3,843
Advances from customers (Unearned Income)		335
Accrued interest		135
		4,313
		12,317

Notes:

N-1: Cost of sales

Opening inventory	4,450
Purchases 12,364 –125)	12,239
Closing inventory	(3,860)
Total	**12,829**

N-2: Other income

Gain on disposal	70
Other income (275-125)	150
Total:	**220**

N-3: Admin and selling expenses

Salaries and commission		(1,295)
Rent and insurance	(549 - 9)	(536)
Utilities and repairs	420+85	(505)
Office and sales supplies	(210 – 90 +27)	(147)
Bad debts	131+99	(230)
Depreciation - vehicle		(472)
Depreciation- furniture		(214)
Total		**(3,399)**

Working;

i. Unused office and sales supplies 90
   Office and sale supplies 90
   Office supplies loss 27
   Unused office and sale supplies 27

ii. Total rent expense : 75,000/3 x 2 = 50,000 + 40,000 x 0.4 = 66,000
   Amount for which benefits is to be obtained = 75,000 – 66,000 = 9,000
   Repaid rent 9
   Rent and insurance 9

iii. Other income 125
   Purchases 125
   2,500,000 x 5% = 125,000

iv. Repair expense 85
   Capital 85

v. Claim receivable 500
   Accumulated depreciation 170
   (600 x 10% = 60 x 2 + 60 x 10/12)
   Vehicle 600
   Gain (I.S) 70

vi. Vehicle 960
   Capital 960

vii. Sales 335
   Advance from customers (Unearned income) 335

viii. Creditor 100
   Debtors 100

ix. Bad debts 131
   Provision 131

Depreciation :

Vehicles

b/d	4,500	Disposal (1-11-2018)	600
Capital 1-9-18	960		
		c/d	4,860

Accumulated depreciation

Disposal	170	b/d	1,450
		Expense	472
c/d	1,752		

Depreciation :

(4,500 – 600)	= 3,900
X 10%	= 390
+ 600 x 10% 10/12	= 50
+960 x 10% x 4/12	= 32
	472

Depreciation 472
Accumulated depreciation 472

Furniture

Furniture A/C

b/d	2,135 (2,535 – 400)		
(1-5-2018) Cash	4500		
		c/d	2,535

Accumulated depreciation

		b/d	975
		Dep Exp	214
c/d	1,189		

Depreciation :

(2,135 -975)	1,160
X 15%	174
400 x 15 % x 8/12	40
	214

Depreciation 214
Accumulated depreciation 214

Allowance

1. 270 x 30%	= 81
2. Debtor (2,970 – 100)	= 2,870
Less: balance on which specific allowance is created	= 270
	= 2,600
3. X 4%	= 104
4. (81 + 108)	= 185

Provision

Unadjusted Allowance	45	Bad debts	131
		Bad debts	99
c/d	185		

Bad debts 99
Allowance 99
Interest Expense 135
Interest Payable 135
(1,500 x 12% x 9/12)

Test question:

Q.1 Following is the summarised trial balance of Delta Enterprises (DE), for the year ended 30 June 2019:

Rs. in '000

Description	Debit	Description	Credit
Property, plant and equipment	230,600	Capital	145,000
Inventory – 30 June 2019	67,800	Profit or loss – 1 July 2018	34,500
Cash and bank balances	4,600	12% Bank loan	90,000
Trade receivables	94,800	Accumulated depreciation	44,300
Prepayments	3,000	Trade payables	41,400
Other receivables	5,300	Sales revenue	487,800
Cost of sales	354,700	Other income	2,600
Selling expenses	29,400		
Administration expenses	25,900		
Depreciation	19,800		
Interest on bank loan	9,000		
Bank charges	700		
	845,600		845,600

Additional information:

(i) Goods returned by a customer on 30 June 2019 were recorded on 1 July 2019. These goods had been sold on credit for Rs. 1,950,000 at cost plus 30%.

(ii) On 1 October 2018, a printer was acquired on rent from Qazi & Co. The annual rent of Rs. 480,000 was paid in advance and debited to prepayments. However, the printer was purchased by DE on 1 April 2019 for Rs. 1,240,000. The payment net of rent adjustment was made in July 2019. The purchase has not been accounted for. DE depreciates office equipment at 20% using reducing balance method. Depreciation for the year has already been recorded except for the effect of any errors.

(iii) Annual fire insurance premium of Rs. 4,500,000 was paid in advance on 1 January 2019 and debited to administration expenses. The payment also includes Rs. 1,350,000 pertaining to the owner's personal property.

(iv) Other income includes Rs. 900,000 collected on 1 April 2019 in respect of a service agreement for the six months ending 30 September 2019.

(v) An amount of Rs. 960,000 receivable on 1 August 2019 on completion of a service agreement for the six months ended 31 July 2019 has not been accounted for.

(vi) 12% bank loan was acquired on 1 April 2018. The principal is repayable in ten equal yearly installments commencing from 1 April 2019. Interest is payable on 1 October and 1 April each year.

Required:

(a) Prepare statement of profit or loss for the year ended 30 June 2019 (09)

(b) Prepare statement of financial position as at 30 June 2019. (09)

A.1 (a) **Delta Enterprises**

Statement of profit or loss for the year ended 30 June 2019

		Rs. in '000'
Sales	487,800-1,950	485,850
Cost of sales	354,700-1,500	(353,200)
Gross profit		**132,650**
Other income	2,600-450+800	2,950
Selling & Admin expenses	W-1	(72,477)
Financial charges	9,000+2,700+700	(12,400)
Net profit		**50,723**

(b) **Statement of financial position as at 30 June 2019**

		Rs. In '000'
Assets		
Non-current assets		
Property, plant and equipment	(230,600+1,240)-(44,300+62)	187,478
Current assets		
Inventory	67,800+1,500	69,300
Trade receivables	94,800-1,950	92,850
Prepayments	3,000+1,575-240-240	4,095
Other receivables	5,300+800	6,100
Cash and bank balances		4,600
		176,945
		364,423
Equity and liabilities		
Equity		
Capital		145,000
Profit or loss	34,500+50,723	85,223
Drawings		(1,350)
		228,873
Long-term loan		**80,000**
Current liabilities		
Trade payable		41,400
Unearned revenue		450
Interest payable		2,700
Current maturity of long-term loan		10,000
Printer payable		1,000
		55,550

W-1: Selling and administration expenses

As given	(29,400+25,900)	55,300
Depreciation	(19,800+62)	19,862
Printer's rent	480×6÷12	240
Insurance pertaining to the owner's property		(1,350)
Prepaid insurance	[(4,500-1,350)÷2]	(1,575)
		72,477

Workings

(i)	Sale Return	1,950	
	Debtor		1,950
	Stock	1,500	
	Cost of Sales		1,500
	1,950 /130 X 100 = 1,500		
(ii)	Rent (Admin)	240	
	Prepayment		240
	480,000 / 12 X 6 = 240		
	Remaining repayment = 480 -240 = 240		
	Printer	1,240	
	Prepayment		240
	Payable		1,000
	Depreciation	62	
	Acc . dep		62
	1,240 X 20% X 3/12 = 62		
(iii)	Drawings	1,350	
	Admin Exp		1,350
	Prepaid Insurance	1,575	
	Admin Exp		1,575
	(4,500-1,350)/12 X 6 = 1,575		
(iv)	Other Income	450	
	Unearned Service Income		450
	900/6 X 3 = 450		
(v)	Receivable	800	
	Other Income		800
	960/6 X 5 = 800		

(vi) Loan [90,000/9 X 10 = 100,000]

100,000X12% X 9/12 + 90,000 X 12% X 3/12

= <u>11,700</u>

Already Recorded	To be Recorded
9,000	2,700

Interest Exp	2,700	
Payable		2,700

Current portion of loan
[90,000/9 X 1] = 10,000

Non-Current portion of loan
[90,000-10,000] = 80,000

Accounting Equation

Question:1

The effect of certain transactions is summarised below in equation form:

Description	Assets					=	Liabilities	+	Owner's Equity
	Cash	Debtors	Land	Stocks	Machine		Creditors		Capital
Opening balance	118,600	177,800	500,000	206,800	164,200		191,500		975,900
(i)	-14,600	-	-	-	+14,600		-		-
(ii)	+4,100	-4,100	-	-	-		-		-
(iii)	-16,000	-	-	-	+61,600		+45,600		-
(iv)	-	-	-	-66,100	-		-66,100		-
(v)	+68,400	-	-	-	-		-		+68,400
(vi)	-	-	-	-	+9,600		+9,600		-
(vii)	-22,000	-	-	-	-		-		-22,000
(viii)	-	-15,000	-	-	-		-15,000		-
Closing balance	138,500	158,700	500,000	140,700	250,000		165,600		1,022,300

Required:

Give brief narrative/description of each of the above transactions. **(08)**

Q. 2 The following table depicts the effects of certain transactions in accounting equation form:

	Transaction date							
	3-Jan	5-Jan	8-Jan	12-Jan	16-Jan	20-Jan	25-Jan	28-Jan
	---------------------------- Rs. in million ----------------------------							
ASSETS:								
Fixed assets - cost					–5.00			
Accumulated depreciation					+2.40*			
Account receivables – Gross			– 6.00					
Prepayments & other receivables						–4.80		
Inventory	+17.00	– 20.00		–2.00		+8.00	–8.00	
Cash & bank	–4.25	+22.50	+3.00	–1.50	+3.00	–3.20	+9.50	–3.80
Total	**+12.75**	**+2.50**	**–3**	**–3.50**	**+0.40**	**-**	**+1.50**	**–3.80**

EQUITY:								
Capital				–3.50				
Profit and loss		+5.00	–3		+0.40		+1.50	–0.80
LIABILITIES:								
Long term loan								-3.00
Account payable	+12.75							
Accruals and other payables		–2.50						
Total	**+12.75**	**+2.50**	**–3**	**–3.50**	**+0.40**	**-**	**+1.50**	**–3.80**

***Note:** This is +ve according to fixed asset that when accumulated depreciation is decreased fixed asset will increase.

Required:

Give brief narration/description of each of the above transactions. **(08)**

Q 3. The following table depicts the effects of certain transactions of Ben Ten Trader in accounting equation form:

	Assets					Owner's
	Cash	Debtors	Inventory	Equipment =	Liabilities +	equity
(i)	+50,000	+50,000	-75,000			+25,000
(ii)	+20,000	-50,000				-30,000
(iii)			-23,000		-23,000	
(iv)	-15,000			+65,000	+50,000	
(v)			-15,000			-15,000
(vi)	+60,000			-55,000		+5,000
(vii)	-2,500	-17,500			-20,000	
(viii)					-17,000	+17,000
(ix)		-35,000	+28,000			-7,000
(x)	-39,200				-40,000	+800

Required:
Give brief narrative/description of each of the above transactions. (10)

Q 4. Following information pertains to Paracha Enterprises, a sole proprietorship:

(i) A machine costing Rs. 450,000 and having book value of Rs. 120,000 was sold for Rs. 150,000.

(ii) A purchase order for supply of goods amounting to Rs. 1,500,000 was issued to ABC & Co. Payment would be made on delivery of the goods. ABC & Co. accepted the purchase order immediately.

(iii) Goods costing Rs. 200,000 were sold at 40% above cost. 20% of the sales amount had been received in advance and the remaining amount is to be received within60 days

(iv) Rent amounting to Rs. 600,000 was paid for offices premises. 40% of the rent paid had already been accrued in the books.

(v) A loan instalment of Rs. 545,000 including interest expense amounting to Rs. 45,000 was paid.

Required:
Show the effects of the above information in the form of accounting equation. **(08)**

Q 5. Following information pertains to Swat Enterprises (SE):

(i) A machine was purchased for Rs. 3,500,000 against which 100% advance had already been paid. SE also paid transportation and installation costs of Rs. 60,000 and Rs. 125,000 respectively on this machine.

(ii) Insurance premium amounting to Rs. 180,000 was paid which included an amount of Rs. 30,000 for the proprietor's personal vehicle.

(iii) Office equipment having cost and carrying value of Rs. 265,000 and Rs. 89,000 respectively was sold for Rs. 95,000.

(iv) SE entered into rent agreement with the owner of a shop for annual rent of Rs. 300,000.

(v) Stock amounting to Rs. 75,000 was destroyed in fire in the warehouse. The stock was insured and insurance company agreed to pay Rs. 65,000.

(vi) SE incurred costs of Rs. 1,200,000 on extension of warehouse and Rs. 250,000 on miscellaneous repairs.

Required:
Show the effects, if any, of each of the above information in the form of accounting equation.

Question 6

Following information pertains to Arish Enterprises (AE) for the month of August 2016:

(i) Goods purchased on credit for Rs. 842,000 were returned to the supplier.

(ii) A customer bought goods amounting to Rs. 96,000. 40% payment was made in cash and the balance amount was set off against amount payable by AE to the customer.

(iii) An unidentified amount of Rs. 11,000 received in the bank account was credited to the suspense account. At month end, it was found that the amount received represents a direct transfer into AE's bank account by a foreign customer. The bank had credited AE's account net of bank charges of Rs. 1,000.

(iv) A customer owes Rs. 348,000 to AE. It is expected that AE would be able to recover 60% and a provision for doubtful debts is to be made for the remaining amount.

(v) The owner withdrew cash of Rs. 35,000 and goods costing Rs. 65,000 for his own use.

Required:

Show the effect of the above in the form of accounting equations. **(08)**

Answers:

A.1

(i) Purchased machine for cash at a cost of Rs. 14,600.
(ii) Received Rs. 4,100 cash from debtors.
(iii) Purchased machine at a cost of Rs. 61,600; paid Rs. 16,000 cash and incurred a liability for the remaining balance.
(iv) Returned stock of Rs. 66,100 to supplier/creditor.
(v) The owner invested Rs. 68,400 cash in business.
(vi) Purchased machine on credit for Rs. 9,600.
(vii) Amount of Rs. 22,000 drawn by the owner from business.
(viii) Contra settlement of Rs. 15,000 between debit and credit balances of the same party.

A.2

Date	Description	Debit	Credit
3 - Jan	Inventory	17	
	Cash		4.25
	Payable		12.75
	Goods costing Rs. 17 million purchased against cash payment of 4.25 million and balance on credit.		
5 – Jan	Cash	22.5	
	Advance from customer	2.5	
	Sales		25
	Cost of sale	20	
	Stock		20
	Goods costing Rs. 20 million sold for Rs. 25 million. 10% amount was received in advance and balance has been collected on delivery.		
8 – Jan	Cash	3	
	Bad debts	3	
	Debtor		6
	Against the balance receivables of Rs. 6 million, Rs. 3 million were recovered and balance of 3 million is written off in income statement.		
12 – Jan	Drawings	3.5	
	Inventory		2
	Cash		1.5
	Goods costing 2 million and cash of Rs. 1.5 million were withdrawn by the owner for his personal use.		
16 – Jan	Cash	3	
	Accumulated depreciation	2.4	
	Fixed Asset		5
	Gain		0.4
	Fixed assets having WDV of 2.6 million were sold for Rs. 3 million.		
20 – Jan	Inventory	8	
	Cash		3.2
	Advance to supplier		4.8
	Goods costing 8 million were purchased. Amount of Rs.4.8 Million had been paid in advance previously whereas balance of Rs. 3.2 million was paid on delivery.		
25 – Jan	Cash	9.5	
	Sales		9.5
	Cost of sale	8	
	Stock		8
	Goods costing 8 million sold for Rs. 9.5 million.		
28 – Jan	Loan	3	
	Interest	0.8	
	Cash		3.8
	Repayment of long term loan comprising of principal amount of Rs. 3 million and interest of Rs. 0.8 million.		

A. 3

(i) Goods costing Rs. 75,000 were sold for Rs. 100,000 and part payment of Rs. 50,000 received in cash.

(ii) An amount of Rs. 20,000 was received from a debtor and remaining Rs. 30,000 were written off.

(iii) Goods purchased on credit for Rs. 23,000 were returned.

(iv) Equipment was purchased for Rs. 65,000 against part payment of Rs. 15,000.

(v) Inventory costing Rs. 15,000 was destroyed/lost/used in office/distributed as sample/withdrawn by owner.

(vi) Equipment having a net book value of Rs. 55,000 were sold for cash of Rs. 60,000.

(vii) A liability of Rs. 20,000 was settled by adjusting receivable from same party of Rs. 17,500 and cash payment of Rs. 2,500.

(viii) Owner paid to supplier Rs. 17,000 from personal cash. / A liability of Rs. 17,000 was written back as it was no more payable.

(ix) Goods costing Rs. 28,000 and sold on credit for Rs. 35,000 were returned by a customer.

(x) Payment of Rs. 39,200 was made to a supplier in settlement of Rs. 40,000.

Ans 4.

(i)	Cash	150,000	
	Acc. Dep	330,000	
	Machinery		450,000
	Gain		30,000
(ii)	Unearned Income (20%)	56,000	
	Debtor (80%)	224,000	
	Sales		280,000
	Cost of Sale	200,000	
	Inventory		200,000
(iv)	Rent payable	240,000	
	Rent expense	360,000	
	Cash		600,000
(v)	Loan	500,000	
	Interest Expense	45,000	
	Cash		545,000

		Capital	=	Asset	-	Liabilities
(i)	Cash			150,000		
	Acc.dep			330,000		
	Machine			(450,000)		
	Gain	30,000				
		30,000	=	30,000	-	0
(ii)	Unearned income					(56,000)
	Debtor			224000		
	Sale	280,000				
		310,000	=	254,000	-	0
	Cost of sale	(200,000)	=	(200,000)	-	(56000)
		110,000	=	54,000	-	(56,000)
(iv)	Rent Payable					(240,000)
	Rent Expense	(360,000)				
	Cash			(600,000)		
		(250,000)	=	(546,000)	-	(296,000)

(v)	(45,000)	=	(545,000)	-	(500,000)
	(295,000)	=	(1,091,000)	-	(796,000)

Ans.5 **Swat Enterprises**

S. No.	Head of account	Assets	=	Equity	+	Liabilities
		Rupees [Increase/(Decrease)]				
(i)	Machinery (3,500+60+125)	3,685,000				
	Cash/Bank	(185,000)				
	Advance	(3,500,000)				
(ii)	Cash/Bank	(180,000)				
	Drawings			(30,000)		
	Insurance			(150,000)		
(iii)	Cash/Receivables	95,000				
	Office equipment - cost	(265,000)				
	Office equipment – accumulated dep.	176,000				
	Book value	**(89,000)**				
	Gain on disposal			6,000		
(iv)	No business transaction takes place by entering into rent agreement.					
(v)	Stock	(75,000)				
	Insurance claim receivable	65,000				
	Loss of stock			(10,000)		
(vi)	Warehouse	1,200,000				
	Repairs and maintenance			(250,000)		
	Cash/Bank	(1,450,000)				

A.6
Arish Enterprises

S. No.	Head of account	Assets	=	Equity	+	Liabilities
		--------- Rupees [Increase/(Decrease)] ---------				
(i)	Account payable	-		-		(842,000)
	Purchase return / inventories	(842,000)				-
(ii)	Sales	-		96,000		-
	Cash	38,400		-		-
	Account payable	-		-		(57,600)
(iii)	Bank charges	-		(1,000)		-
	Trade debtors	(12,000)				-
	Suspense	-		-		(11,000)
(iv)	Bad debt expense	-		(139,200)		-
	Provision for doubtful debts	(139,200)		-		-
(v)	Drawings	-		(100,000)		-
	Purchases / inventories	(65,000)				-
	Cash	(35,000)		-		-

Journal Entries [not required for extra information]

(i)	Creditors	842,000	
	Purchase returns / inventories		842,000
(ii)	Cash	38,400	
	Debtor	57,600	
	Sales		96,000
	Creditor	57,600	
	Debtor		57,600
(iii)	Suspense	11,000	
	Bank Charges	1,000	
	Debtor		12,000
(iv)	Bad Debts	139,200	
	Provision		139,200
(v)	Drawing	100,000	
	Cash		35,000
	Purchases		65,000

Control Accounts and day books

Book of Original Entry:

Journal

↓

Ledger

↓

Trial Balance

Statement of comprehensive income | **Statement of financial position**

In large organization Journal is subdivided into **Sub-Journals also called as day books:**

- ⇒ Sales Journal (Sales day book) → to record Credit Sales.
- ⇒ Purchase Journal (Purchase day book) → to record Credit purchases.
- ⇒ Sales Return Journal (Sale return day book) → to record Credit sale return.
- ⇒ Purchase Return Journal (purchase return day book) → to record Credit purchase return
- ⇒ Cash book (Three column book)

	Discount Allowed	Cash	Bank		Discount Received	Cash	Bank

- ⇒ General Journal: (is used to record all other transactions e.g; Depreciation, bad debts, credit expense etc).

Point to remember:

These above books are also called as Books of original entry or books of prime entry.

For Example: 1st year of Business

Sales day book

A	1	10,000
B	2	15,000
C	3	5,000
D	4	25,000
		55,000

Sales Return day book:

A	2,000
D	3,000
	5,000

Cash Book

	Discount Allowed	Cash	Bank		Discount Received	Cash	Bank
A		3,000					
B			6,000				
E		4,000		c/d		7,000	6,000

Posting of entries:

Debtor's Control Account (Also called as Total Debtor's Account)

Sales (From SDB)	55,000	Sales return (From SRDB)	5,000
		Cash (From cash book)	7,000
		Bank (From cash book)	6,000
c/d Closing advance from customers	4,000	c/d Closing receivable	41,000
	59,000		59,000

Sales

		Debtors	55,000
c/d	55,000		

Sales Return

Debtors	5,000		
		c/d	5,000

Trial balance:

Accounting Heads	Dr.	Cr.
Debtor's Control Account	41,000	4,000
Sales		55,000
Sales Return	5,000	
Cash	7,000	
Bank	6,000	
Total	59,000	59,000

Subsidiary ledgers (If control accounts are prepared then Subsidiary ledgers are not part of double entry system. These are prepared for additional information about individual balances of customers)

A

Sale	10,000	Sale Return	2,000
		Cash	3,000
		c/d	5,000

B

Sale	15,000	Sale Return	---
		Bank	6,000
		c/d	9,000

C

Sale	5,000	Sale Return	---
		c/d	5,000

D

Sale	25,000	Sale Return	3,000
		c/d	22,000

E

Sale	---	Sale Return	---
		Cash	4,000
c/d	4,000		

List of balances extracted from subsidiary ledgers:

A =	5,000 Dr.	
B =	9,000 Dr.	
C =	5,000 Dr.	
D =	22,000 Dr.	
E =	4,000 Cr.	Advance from Customer
Total	**37,000 Dr.**	

2nd year of Business

Debtors Control Account

b/d (Receivable)	41,000	b/d (Advance)	4,000
c/d (Advance)	--	c/d (Receivable)	--

Similarly:
1st year of Business

Creditors Control Account (Also called as Total Creditors Account)

P/Return	25,000	Purchase	500,000
Cash	150,000		
Bank	50,000		
c/d (Payable to Supplier)	300,000	c/d (Advance to supplier)	25,000

2nd year of Business

Creditors Control Account

b/d	25,000	b/d	300,000
c/d	--	c/d	--

CONTROL ACCOUNTS

Debtors Control Account
[Total Debtors Account]
- Receivables Control Account
- Sales Ledger Control Account

Creditors Control Account
[Total Creditors Account]
- Payables Control Account
- Purchase Ledger Control Account

Contra Entry:

If a person is simultaneously our customer as well as supplier, his respective balances can be adjusted against each other by making a set – off or contra entry.e.g.

1. Ali

~~50,000~~ Dr.	**~~10,000~~ Cr.**
40,000 Dr.	**Cr.**

Contra Entry

Creditor Ali	10,000	
Debtor Ali		10,000

2. Shahid

~~5,000~~ Dr.	**~~60,000~~ Cr.**
-- Dr.	**55,000 Cr.**

Contra Entry

Creditor Shahid	5,000	
Debtor Shahid		5,000

3. Naveed

~~1,000~~ Dr.	**5,000 Cr.**
Dr.	**4,000 Cr.**

Creditor Naveed	1,000	
Debtor Naveed		1,000

Contra entry is always same and it is made at lower of the amount of two balances.

Q.1 Prepare the total accounts from the following particulars in the 2015.

			Rupees
1 Jan	Balance on Bought Ledger Control Account	Dr	870
1 Jan	Balance on Bought Ledger Control Account	Cr	11,940
1 Jan	Balance on Sales Ledger Control Account	Dr	14,620
1 Jan	Balance on Sales Ledger Control Account	Cr	240
	Transaction during the period:		
	Purchases		66,180
	Purchase returns		2,560
	Sales		87,490
	Sales Return		1,170
	Cash received from customers		76,210
	Discount allowed thereon		2,820
	Cash paid to the suppliers		58,430
	Discount received thereon		1,660
	Cash paid to customers		130
	Cheque received from debtors		4,120
	Cheque received dishonored		2,250
31 Jan	Bought Ledger Control Account Balance (Dr)		770
31 Jan	Sales Ledger Control Account Balance (Cr)		420

Q. 2 Abid who was appointed at ABC & Company on January 1, 2009 had changed the method of recording debtors and creditors, to save time. Under the new method, he made all entries related to debtors and creditors in the subsidiary ledgers but did not maintain the related control accounts. Although the company's trial balance does agree but the management is not satisfied with the method adopted by Abid and wants you to draw the related control account

On reviewing various records, you have extracted the following information:

	Rupees
Debtors as on December 31, 2008	2,600,000
Creditors as on December 31,2008	4,100,000
Cheques issued to suppliers in settlement of Rs. 23,600,000	23,350,000
Cash sales memos issued	14,360,000
Goods returned to suppliers	550,000
Cheques received from debtors in settlement of Rs. 32,000,000	31,650,000
Cheque received from suppliers against return of goods	180,000
Credit sales invoices issued	35,900,000
Returns by customers: from cash sales	320,000
from credit sales	980,000
Goods purchased on credit	27,700,000
Cash refund to a debtor who had paid the amount due twice	120,000
Cheque issued by a debtor on Dec. 28,2008 was dishonoured on May 13,2009	200,000
Increase in provision for doubtful debts (from Rs. 1,750,000 to Rs. 2,250,000)	500,000
Bad debts written off	430,000
Contra settlement between creditors and debtors accounts	1,660,000
Credit balances included in debtors' accounts as on December 31,2009	75,000
A supplier's invoice received on December 30,2009 relating to goods supplied	
on December 28,2009 has not been entered in the books	350,000

Required:

Prepare the debtors and creditors control accounts from the above information for the year ended December 31,2009.

Introduction

1) A control account is a ledger account that appears in the main/general ledger. It summarizes large volumes of transactions.
2) The debtors control account (sales ledger control a/c or total debtors account)
   - Is used to record all transactions with credit customers
   - Balance shows the total amount currently owed by all credit customers. This balance should agree with the list of individual balances extracted from the Sales Ledger (a memorandum ledger containing ledger accounts of individual debtors).
3) The creditors control account (purchase ledger control a/c or total creditors, account).
   - Is used to record all transactions with credit suppliers
   - Balance shows the total amount currently owed to all credit suppliers. This balance should agree with list of individual balances extracted from the Purchase Ledger (a memorandum ledger containing ledger accounts of individual creditors)
4) Balance on the debtors/creditors control account may not agree with total of the list of individual balances extracted from the debtor's ledger.
   a) Any difference, must be investigated and corrections made
   b) This may involve adjustments:
      - to the Control account and/or
      - to the list of balances
5) Debtors Control a/c might produce two balances i.e. Dr. and Cr. in this case the account will look like;

Debtors Control Account	
Opening Dr. Balance Closing Cr. Balance(i.e. Advance From Customers)	Opening Cr. Balance(i.e. Advance From Customers) Closing Dr Balance

6) Creditors Control a/c might produce two balances i.e. Dr. and Cr. in this case the account will look like

Creditors Control Account	
Opening Dr Balance (i.e. Advance to Suppliers) Closing Cr Balance	Opening Cr Balance Closing Dr Balance(i.e. Advance to Suppliers)

7) Whatever the nature of ledger account, opening Dr Balance would always appear on debit side of respective ledger and opening Cr balance would always appear on credit side of respective ledger.
8) Closing balances always appear on opposite side. i.e. closing Dr balance will appear on credit side and dosing Cr balance will appear on Dr side.
9) There might be the chance that a person who is a debtor is also a Creditor of the entity with different amount e.g. Mohsin is a debtor with a balance of Rs. 700 and he also a creditor of Rs. 500, contra entry will always be recorded at lower amount.

Day books (Question bank)

Q.3 MAY TRANSACTIONS REVISITED

The following transactions in May 2013 are those of a new business entity, Home Oak Garden Traders.

May 2013

Date	
1	Set up the entity with capital in cash: Rs.2,500,000.
2	Bought goods on credit from the following suppliers: The Bushes Company Rs.540,000, Flower City Rs.870,000, D Gibson Rs.250,000, Weedkill Rs.760,000, T Greenery Rs.640,000. (Total Rs.3,060,000).
4	Sold goods on credit to: The Office Company Rs.430,000, V Cork Rs.640,000, Texas Chain Stores Rs.1,760,000. (Total Rs.2,830,000).
6	Paid rent Rs.120,000.
9	The Office Company paid the Rs.430,000 that it owed.
10	Texas Chain Stores paid Rs.1,500,000.
12	The following payments were made: to D Gibson Rs.250,000 and to The Bushes Company Rs.540,000. (Total Rs.790,000).
15	Advertising costs of Rs.230,000 were paid to the local newspaper publisher.
18	Bought goods on credit from the following suppliers: The Bushes Company Rs.430,000, Landscape Rs.1,100,000. (Total Rs.1,530,000).
21	Sold goods on credit to Public Parks Rs.670,000
31	Paid rent Rs.180,000.

Required:

(a) Prepare extracts of the sales day book and purchase day book for the relevant transactions above.

(b) Use T accounts to show how these transactions should be recorded in the main ledger accounts of the entity. The accounting system contains a receivables ledger and a payables ledger for individual accounts, and there are control accounts (total accounts) for receivables and payables in the main ledger.

(c) Post the transactions to individuals' accounts in the receivables ledger and the payables ledger and extract a list of balances from these. (The total of each list should agree with the balance on the receivables control account and payables control account respectively).

(d) Prepare a trial balance as at 31 May 2013.

Note: Main ledger is also called as General ledger

Q.4 JUNE TRANSACTIONS

The following transactions in June 2013 are those of a new business entity, Parakeet.

June 2013

Date	
1	Set up the entity with capital in cash of Rs.6,500,000 paid into a bank account.
2	Bought goods on credit from C Jones Rs.1,800,000
3	Credit sales: J Bird Rs.660,000, D Swann Rs.250,000, Swallow Company Rs.430,000. (Total Rs.1,340,000).
4	Purchased goods for cash (by cheque) Rs.230,000.
5	Bought second-hand motor van for Rs.2,560,000, paying by cheque.
7	Paid motor expenses Rs.120,000.
9	Credit sales: M Parrott Rs.240,000, Canary Company Rs.260,000, G Finch Rs.680,000. (Total Rs.1,180,000).
11	Purchased goods on credit: C Jones Rs.2,400,000, E Davies Rs.620,000, A Evans Rs.460,000. (Total Rs.3,480,000).
13	Purchases returned to C Jones Rs.250,000.
19	Sales returns from D Swann Rs.110,000.
20	Cash drawings taken by owner: Rs.440,000 by cheque.
21	Payments made to E Davies Rs.620,000, A Evans Rs.460,000. (Total Rs.1,080,000). All payments were made by cheque.
23	Received payment from J Bird: Rs.660,000 by cheque.
25	Received payment from Swallow Company: Rs.430,000 in cash which was kept in the office.
28	Purchases returned to C Jones: Rs.420,000.
29	Purchased stationery Rs.40,000 (record as a sundry expense) using cash.
30	Credit sales: D Swann Rs.420,000, Canary Company Rs.540,000. (Total Rs.960,000).

Required:

(a) Prepare journal entries to show how the following transactions in June 2013 should be recorded in the main ledger accounts of Parakeet, a newly-established business entity.

The accounting system contains a receivables ledger and a payables ledger for individual accounts, and there are control accounts (total accounts) for receivables and payables in the main ledger.

You are not required to include any narrative in the journal entries.

(b) List the transactions that will be entered in the receivables ledger accounts for the month.

(c) List the transactions that will be entered in the payables ledger accounts for the month.

Q.5 KWARK

The following are transactions of Kwark, a new business, during May 2013.

May 2013

Transaction	
1	Started the business with capital of Rs.2,500,000, paid into a business bank account.
2	Bought goods on credit from the following entities: Ellis Rs.810,000; Mendez Trading Rs.1,305,000; Gibson Rs.375,000; Dynasty Rs.1,140,000; Liners Rs.960,000. (Total Rs.4,590,000).
3	Sold goods on credit to: Bailey Stores Rs.753,000; Fastshop Rs.1,120,000; Spencers Rs.3,080,000. (Total Rs.4,953,000).
4	Bailey Stores paid by cheque Rs.723,000. A discount of Rs.30,000 was allowed for early payment.
5	Spencers paid Rs.1,500,000 by cheque
6	The following payment was made: Ellis Rs.700,000
7	The following payment was made Gibson: Rs.350,000. A discount of Rs.25,000 was received for early payment.
8	Paid carriage outwards: Rs.345,000
9	Purchase returns to Dynasty Rs.400,000
10	Sales returns from Spencers: Rs.270,000
11	Purchases on credit from Mendez Trading Rs.753,000; Dynasty Rs.1,650,000. (Total Rs.2,403,000).
12	Sold goods on credit to Fastshop Rs.1,005,000.

Kwark maintains control accounts for receivables and payables in the main ledger, and accounts for individual customers and suppliers in a receivables ledger and a payables ledger respectively.

Required:

(a) Use T accounts to show how the relevant transactions will be recorded in the receivables control account and the payables control account in the main ledger of Kwark in May. (You are not required to prepare T accounts for any of the other main ledger accounts.)

(b) Show the list of balances in the receivables ledger after recording the above transactions.

(c) Show the list of balances in the payables ledger after recording the above transactions.

Question 6

Lotus Pharma (LP) was established on 1 January 2016. Following transactions pertain to the first month of business:

1-Jan-2016 Bought medicines on credit from the following suppliers:

	Rs. In million
Shan Traders	8.50
Rahat Stores	12.50
Quality Medicos	15.00

12-Jan-2016 Bought medicines on cash for Rs. 3.8 million.

20-Jan-2016 Medicines worth Rs. 2.5 million were returned to Rahat Stores.

24-Jan-2016 A part payment of Rs. 5.8 million was made to Shah Traders.

28-Jan-2016 Amount payable to quality Medicos was fully settled to avail an early payment discount of 2%.

31-Jan-2016 Rahat Stores was paid in full after adjusting Rs. 1.2 million against its account receivable balance.

Required:

(a) Prepare extracts of purchase day book for the above transactions. **(02)**

(b) Prepare subsidiary and control accounts for trade payables. **(08)**

Question 7

In August 2015, Ali established a stationery store named as Ali Baba Stationers. The transactions during the month are listed below:

Date	**Transactions**
3 August	A bank account was opened with cash Rs. 5,000,000.
3 August	Purchase shop furniture worth Rs. 170,000 on credit.
3 August	Bought stationery on credit from The Pen Store: Rs. 450,000 less trade discount of Rs. 25,000, The School Shop; Rs. 200,000, Galaxy Stationers; Rs. 350,000. The Stationery Store: Rs. 400,000, The Office Store; Rs. 800,000.
5 August	Supplied stationery on credit to Murjeena Traders: Rs. 200,000, Qasim and Company: Rs. 550,000 less trade discount of Rs. 50,000, Chiragh Limited: Rs. 250,000, Sameer Enterprises: Rs. 400,000. Hamid and Company: Rs. 800,000.
6 August	Purchase returns to Galaxy Stationers: Rs. 10,000 and the Stationery Store: Rs. 40,000.
7 August	Paid shop rent amounting to Rs. 300,000.
7 August	Recovered Rs. 150,000 from Murjeena Traders, Rs. 250,000 from Qasim and company, Rs. 200,000 from Chiragh Limited, Rs. 300,000 from Sameer Enterprises, Rs. 400,000 from Hamid and Company.
10 August	Paid Rs. 300,000 to The Stationery Store, Rs. 290,000 to the Office Store and Rs. 250,000 to The Pen Store after availing early payment discount of Rs. 25,000.
11 August	Paid Rs. 60,000 for shop repairs.
12 August	Sold stationery on cash amounting to Rs. 250,000.
15 August	Sales return from Murjeena Traders: Rs. 25,000 and Chiragh Limited: Rs. 30,000.
18 August	Bought stationery for cash Rs. 150,000.
21 August	Supplied stationery on credit to Murjeena Traders: Rs. 300,000, Qasim and Company: Rs. 200,000, Chiragh Limited: Rs. 550,000, Sameer Enterprises: Rs. 200,000.
25 August	Following amounts were received from debtors: Murjeena Traders: Rs. 150,000, Qasim and Company: Rs. 150,000 after allowing early payment discount of Rs. 25,000, Chiragh Limited: Rs. 300,000 after allowing early payment discount of Rs. 50,000.

Required:

(a) Enter the purchase and sale transactions in the related books of prime entry other than cash book and journal.

(b) Prepare the following:
- (i) Receivables Control Account
- (ii) Payables Control Account
- (iii) Cash and Bank Account **(16)**

Question:8

The following information is available in respect of debtors and creditors of Saarim Limited:

(i) The control accounts of debtors and creditors had balances of Rs. 1,744,500 and Rs. 1,366,000 respectively on 1 July 2013.

(ii) Summary of transactions that took place during the year ended 30 June 2014 is as follows:

	Rs.
Credit purchases	8,166,600
Purchase returns	315,900
Credit sales	10,796,300
Sale returns	144,400
Cash received from customers	9,404,300
Discount allowed to customers	348,000
Cash paid to the suppliers	7,210,300
Debtor's balance written off	16,000
Discount received from vendors	204,800
Bill of exchange received from customers	508,400
Contra settlement between creditors and debtors accounts	35,000

Bill of exchange given to suppliers	277,700
Bill of exchange dishonoured by a customer	30,900

(iii) The following discrepancies have been discovered in the recording of transactions:

- a payment of Rs. 26,000 on 18 December 2013 against a purchase was wrongly recorded as salaries expenses.
- the sales return book had been overcast by Rs. 22,000.
- suspense account of Rs. 30,000 (Dr.) is appearing in the trial balance which represents posting errors in creditors control account.

Required:

Prepare the debtors and creditors control accounts from the above information for the year ended 30 June 2014. **(12)**

Q.9 Following transactions pertain to Gul Brothers (GB) for the month of February 2017:

3-Feb	Bought goods on credit from QT Stores for Rs. 295,000.
3-Feb	Purchased goods in bulk on 15 days credit from Bana & Co. at a price of Rs. 190,000 (net of 5% trade discount).
8-Feb	Sold goods on cash for Rs. 300,000.
15-Feb	Issued a cheque of Rs. 90,000 to XYZ in full and final settlement of an old outstanding balance of Rs. 100,000.
18-Feb	Sold goods on 15 days credit to Qavi for Rs. 275,000. Qavi would be entitled to 2% discount if payment is made on the due date.
18-Feb	Sold goods on credit to Child Care Centre at a concessional price of cost plus 10%. The cost of goods was Rs. 158,000.
23-Feb	Johar & Sons, a debtor owing a balance of Rs. 65,000 was declared bankrupt. The balance due was written-off. GB maintains adequate provision against its debtors.
25-Feb	Received cheques from debtors – Chenab Rs. 68,000 and Ameen Stores Rs. 32,000.

Required:

(a) Enter the above transactions in the related books of prime entry.

(b) Post the entries to Receivables Control Account and Payables Control Account. (Balancing of control accounts is not required)

Q.10 Following information pertains to Alpha Traders (AT):

Balances as at 1 August 2017:

	Rupees
Cash in hand	178,000
Bank overdraft	769,000

Transactions for the month of August 2017:

Date	**Transactions**
02-Aug	Office furniture purchased from RABBIT for cash and on credit for Rs. 38,000 and Rs. 129,000 respectively.
03-Aug	Goods purchased for cash from Bena & Co. for Rs. 85,000.
05-Aug	Goods purchased on credit in bulk (net of 5% trade discount) from Moon & Co. and Shan Traders for Rs. 475,000 and Rs. 513,000 respectively.
08-Aug	Goods sold on credit for Rs. 236,000 and Rs. 198,000 to A-Z Super Store and Apollo Center respectively.
10-Aug	Goods costing Rs. 68,000 were returned to Moon & Co.
12-Aug	Cash sales to Danish & Sons for Rs. 40,000.
16-Aug	Cheques (net of 5% discount) amounting to Rs. 194,750 and Rs. 243,200 were received from A-Z Super Store and Bright & Co. respectively.
20-Aug	It was agreed with Columbus Traders to adjust Rs. 200,000 payable to AT against receivables from AT.
25-Aug	Payment of Rs. 225,000 (net of 10% discount) to Al-Shams.

Required

Record the above transactions in relevant books of prime entry in a proper format. **(13)**

Q.11 Quality Services (QS) was established on 1 April 2017 to provide various maintenance services to textile industry. A summarized bank book of QS for the quarter ended 30 June 2017 is as follows:

	Receipts	**Payments**
	----- **Rs. in '000** -----	
Opening of a bank account in the name of QS by its owner	5,000	
Purchase of a vehicle on commencement of the business		1,200
Supplies		650
Maintenance services	4,500	
Cash given for petty office expenses		300
Utility bills (electricity, gas, telephone, etc.)		250
Wages and salaries		1,450
Owner's personal expenses		390
Office rent for the nine months ending 31 December 2017		900
Bank charges		10
Total	**9,500**	**5,150**

Additional information:

i. On 1 April 2017, a machine costing Rs. 240,000 was purchased for business use. The owner paid the amount from his personal bank account in May 2017.
ii. Supplies costing Rs. 850,000 were purchased during the quarter.
iii. Unused supplies as at 30 June 2017 amounted to Rs. 350,000.
iv. Payment of utility bills includes refundable deposits of Rs. 20,000.
v. Electricity bill of Rs. 45,000 for June 2017 was received in July 2017.
vi. Vouchers of Rs. 250,000 for petty office expenses were submitted during the quarter.

vii. Wages and salaries include payment of supervisor's salary for July 2017 amounting to Rs. 150,000.
viii. A bank advice of Rs. 5,000 dated 30 June 2017 for bank charges was received on 4 July 2017.
ix. Maintenance services for Rs. 700,000 have been rendered during the quarter but the amount due has not yet been received.
x. Maintenance services against collections of Rs. 1,250,000 will be rendered in the next quarter.
xi. QS has adopted the policy of charging depreciation on fixed assets @ 20% per annum on a straight line basis. Depreciation is to be charged from the month the assets are available for use.

Required:

Prepare a Trial Balance for the quarter ended 30 June 2017 incorporating all the adjustments necessary for accrual basis of accounting. ***(Ledger accounts are not required)*** **(15)**

Q.12 Ravi Traders (RT) commenced its business on 1 January 2018. The books of prime entry as maintained by RT for the month of January 2018 are reproduced below:

CASH BOOK - RECEIPTS				
Date	Description	Discount	Cash	Bank
		------------- Rupees -------------		
1-Jan	Capital	-	1,000	8,000
10-Jan	Return outward	-	50	-
11-Jan	Trade debtors - Quality Traders	150	-	6,100
14-Jan	Sales	-	-	1,250
20-Jan	Trade debtors - Himalaya Super Store	90	300	1,410
26-Jan	Bank	-	500	-
		240	1,850	16,760

CASH BOOK - PAYMENTS				
Date	Description	Discount	Cash	Bank
		------------- Rupees -------------		
4-Jan	Office rent	-	200	300
5-Jan	Fixed assets (Office equipment)	-	-	1,500
7-Jan	Purchases	-	-	650
14-Jan	Trade debtors - Quality Traders	-	-	6,100
15-Jan	Trade creditors - Zee Traders	100	500	3,400
20-Jan	Return inward	-	60	-
21-Jan	Fixed assets (Computers)	-	250	-
24-Jan	Drawings	-	100	180
25-Jan	Utility bills	-	120	140
26-Jan	Cash	-	-	500
		100	1,230	12,770

PURCHASES DAY BOOK		
Date	Suppliers' name	Rupees
2-Jan	ABC & Co.	4,500
10-Jan	Zee Traders	6,000
28-Jan	Unity Enterprises	7,500
		18,000

PURCHASES RETURNS DAY BOOK		
Date	**Suppliers' name**	**Rupees**
12-Jan	Zee Traders	900

Sales DAY BOOK		
Date	**Customers' name**	**Rupees**
8-Jan	Quality Traders	6,250
19-Jan	Himalaya Super Store	2,350
24-Jan	ABC & Co.	8,000
		16,600

GENERAL JOURNAL			
Date	**Particulars**	**Debit**	**Credit**
1-Jan	Fixed assets (Furniture)	300	
	Capital		300
14-Jan	Drawings	100	
	Purchases		100
14-Jan	Trade debtors - Quality Traders	150	
	Discount allowed		150
31-Jan	Drawings	50	
	Fixed assets (Computers)		50
31-Jan	Trade creditors - ABC & Co.	4,500	
	Trade debtors - ABC & Co.		4,500

Required:

Prepare trial balance for the month ended 31 January 2018.

(Preparation of ledger accounts is not necessary) **(15)**

Rectification of errors:

Q. While reviewing the draft financial statements of Sky Electronics (SE) for the year ended 31 December 2017, following errors have been identified:

I. Computers costing Rs.240,000 purchased on 1 September 2017 for office use were debited to purchases account. SE depreciates computers at 20% per annum using straight line method.

II. Furniture costing Rs. 1,200,000 and having a book value of Rs. 670,000 as on 31 December 2017 had already been sold on 1 November 2017. The proceeds of Rs. 700,000 were credited to sales. SE depreciates furniture at 10% per annum using straight line method.

III. On 1 April 2017, SE rented-out one of its premises at an annual rent of Rs. 900,000 payable in advance. The rent received was credited to income.

IV. Trade receivables include a balance of Rs. 180,000 which is irrecoverable but has not been written-off. Further, a recovery of Rs. 96,000 against receivables written off in prior years was credited to trade receivables. As per SE's policy, provision for doubtful receivables has already been made at 5% on year-end balance.

V. A cheque of Rs. 192,000 was received after a discount of 4% from a customer. However, in the cash book, the amount received was entered in the discount allowed column and the amount of discount was entered in the bank column.

Required:

a. Prepare rectification entries to correct the above errors. **(Narrations are not required)**

b. Post the effect of rectification entries in accounting equation

A. (a)

Sky Electronics

Accounting entries for correction of the errors

Date	Description		Debit	Credit
			Rupees	
(i)	Fixed assets (Computers)		240,000	
	Purchases			240,000
	Depreciation expense	**[240,000×0.2÷12×4]**	16,000	
	Accumulated depreciation			16,000
(ii)	Accumulated depreciation	**(1,200,000×0.1×2÷12)**	20,000	
	Depreciation expense			20,000
	Sales		700,000	
	Accumulated depreciation	**[(1,200,000-670,000) - 20,000]**	510,000	
	Fixed assets-Furniture			1,200,000
	Gain on disposal (Balancing figure)			10,000
(iii)	Rent income	**(900,000÷12×3)**	225,000	
	Advance rent			225,000
(iv)	Bad debt expense		180,000	
	Trade receivables			180,000
	Trade receivable		96,000	
	Bad debt expense/Bad debt recovered			96,000
	Provision for doubtful	**(180,000-96,000)×5%**	4,200	
	Bad debt expense (Reversal of allowance)			4,200
*(v)	Bank	**192,000- (192,000÷0.96×0.04)**	184,000	
	Discount allowed			184,000

* **Required**		**Posted**	
Bank	192,000	Bank	8,000
Disc. Allowed	8,000	Disc. Allowed	192,000
(192,000/96 x 4)		Debtor	200,000
Debtor	200,000		

(b) effect of correction of errors in Accounting equation:

Sr. No	Description	Assets	=	Capital	+	Liabilities
1	Fixed assets	240,000				
	Purchases	(240,000)				
		-		-		-
	Depreciation			(16,000)		
	Acc. Depreciation	(16,000)				
		(16,000)		**(16,000)**		
2	Acc. Depreciation	20,000				
	Depreciation			20,000		
	Sales			(700,000)		
	Acc. depreciation	510,000				
	Fixed asset	(1,200,000)				
	Gain			10,000		
		(670,000)		**(670,000)**		
3	Rent income			(225,000)		
	Advance rent					225,000
				(225,000)		**225,000**
4	Bad debts			(180,000)		
	Trade debtors	(180,000)				
	Trade debtors	96,000				
	Bad debts			96,000		
	Provision	4,200				
	Bad debts			4,200		
		(79,800)		**(79,800)**		
5	Bank	184,000				
	Disc. Allowed			184,000		
		184,000		**184,000**		

Q.13 **Henry Brothers (HB)** is engaged in trading of textile products. As at 1 July 2018, HB had cash and bank balances of Rs. 76,000 and Rs. 286,000 respectively. Following transactions pertain to the month of July 2018:

4 July	Purchased goods on credit amounting to Rs. 250,000 and Rs. 180,000 from Alpha Enterprises (AE) and Bravo Traders respectively. AE offered 3% discount if payment was made within 15 days.
6 July	Purchased office furniture costing Rs. 90,000 from Lavish Designs and paid Rs. 50,000 through cheque. Rs. 40,000 had already been paid in June 2018 and debited to Advances.
8 July	Sold goods to HRS Garments and received a cheque of Rs. 300,000. Also sold goods on cash to Shan Garments having list price of Rs. 250,000 and offered discount of 2%.
14 July	20% goods sold to Shan Garments on 8 July were returned and the amount was refunded in cash. These goods were sold on mark up of 25% of cost.
16 July	Sold old office furniture on cash for Rs. 12,000. The cost of furniture was Rs. 75,000 and its book value was nil.
17 July	Goods costing Rs. 35,000 were returned to AE and the remaining amount was

	paid through cheque.
23 July	Sold goods on cash to Salim Sons for Rs. 236,500.
26 July	Saleh & Co. offered discount of 5% on list price of Rs. 500 per unit if at least 250 units are purchased. HB purchased 300 units to avail the discount and paid through cheque.
28 July	Paid loan instalment of Rs. 150,000 including interest of Rs. 35,000 in cash.
30 July	Deposited cash into bank Rs. 200,000.

Required:

Record the above transactions in the relevant books of prime entry in a proper format.
(Narrations are not required) (15)

Q.14 **Chaman Stores** commenced its business on 1 January 2019. The following books of prime entry are available for the month of January 2019:

CASH BOOK

------------------ Receipts ------------------				------------------ Payments ------------------			
		Cash	**Bank**			**Cash**	**Bank**
Date	**Description**	**Rs. in '000**		**Date**	**Description**	**Rs. in '000**	
1-Jan	Capital		500	2-Jan	Cash		140
2-Jan	Bank	140		5-Jan	Security deposit – shop		45
10-Jan	Sales	19	36	10-Jan	Furniture	40	35
15-Jan	Bank loan		200	11-Jan	Insurance		15
27-Jan	Rafiq Limited - net		95	12-Jan	Shabbir & Sons - net	44	100
				15-Jan	Purchases	35	43
				21-Jan	Returns	4	
				27-Jan	Salaries to staff		76
				30-Jan	Utilities		18
				31-Jan	Balance c/f	36	359
		159	831			159	831

SALES DAY BOOK		
Date	**Name of customer**	**Rs. in '000**
9-Jan	Arif Sons	65
17-Jan	Rafiq Limited	130
24-Jan	Zubair Brothers	72
		267

SALES RETURN DAY BOOK		
Date	**Name of customer**	**Rs. in '000**
22-Jan	Rafiq Limited	30

PURCHASES DAY BOOK		
Date	Name of supplier	Rs. in '000
3-Jan	Shabbir & Sons	150
19-Jan	Ameer & Sons	220
		370

Additional information:

- Utilities paid on 30 January 2019 include Rs. 6,000 against bills of owner's residence.
- Shop rent of Rs. 22,000 for the month of January 2019 was paid on 3 February 2019.
- Goods costing Rs. 30,000 were withdrawn by owner for personal use.
- Furniture purchased on 10 January 2019 had a total cost of Rs. 130,000. Remaining amount is due to be paid within 30 days.
- Goods costing Rs. 13,000 were returned to Ameer & Sons on 31 January 2019.
- Rafiq Limited and Shabbir & Sons had no balance at month end.

Required:

Prepare trial balance for the month ended 31 January 2019. (Preparation of ledger accounts is not necessary)

The role of books of prime entry

Books of prime entry include the following:

Books of prime entry	Function
Sales day book, Sales returns day Book	Records sales on credit (receivables) from sales invoices. Records items returned by credit customers (credit notes issued to customers).
Purchases day book Purchases returns day book	Records purchases on credit from suppliers (trade payables) from purchase invoices. Records returns of purchases on credit.
Cash book	Records cash received into the bank account and cash paid out of the bank account. Cash receipts and payments are very much a part Of the sales and purchases cycles.
Journal	Records transactions that are not recorded in any of the other books of original entry.

Documents in the sales cycle

A business tries to make a profit by selling goods or services to customers. This creates revenue or income for the business.

Sales might be for cash or (coin, by debit card, credit card, cheque or by some less common method such as banker's draft) or on credit.

The following documents might be used in a system designed to account for sales.

Document	Purpose	Impacts double entry?
Sales quotation	Before ordering, customers often require a sales quotation for review in their company. You create it as a proposal of your goods and services to a customer	No
Sales order	From the customer placing an order.	No
Goods despatched note	A notice to the customer to inform them that the goods have been despatched and are on their way.	No
Delivery note	A note that accompanies the goods. (A customer will check this to make sure that it agrees with his order and that it is consistent with what has actually been delivered.	No
Sales invoice	A request for payment from the customer for goods delivered. Invoices normally show a date, details of transaction and payment terms.	**Yes**
Statement of balances	A document to show the customer the amount still owed at a point in time. It will be the net amount of all invoices issued less cash received by the business up to a point in time.	No
Credit note	Issued when a customer returns goods and the business agrees to this. The business issues a credit note to acknowledge that the amount specified is no longer owed to them by the customer.	**Yes**

Documents in the purchases cycle

Businesses make purchases from suppliers. Purchases are similar in many respects to sales, except that the business is buying from a supplier rather than selling to a customer.

The following documents might be used in a system designed to account for purchases.

Document	Purpose	Impacts double entry?
Purchase requisition	An item should be requisitioned first if not lying in the stock	No
Quotation and approval	Where value of goods exceeds certain limit, quotations will be obtained from at least three suppliers. After all quotations have been received and examined for completeness, a dated summary sheet will be prepared enlisting all the necessary details. Contract should ideally be awarded to the lowest bidder after an evaluation of the quotations submitted by them. However, besides financial concerns, weight age should also be given to non-financial and other qualitative factors before a final decision.	No
Purchase order	After selection and finalization of quotation and approval of purchase requisitions, a Purchase Order (PO) will be issued in the name of selected supplier.	No
Goods received note	A document produced when goods are received. It is produced after the goods have been checked against the delivery note and what has actually been received. The GRN is sent to accounts staff who will check that what has been received is what was ordered and that the invoice agrees with what was received.	No
Purchase invoice	A request for payment from the supplier for goods delivered.	Yes
Statement of balances	A document from the supplier to show the amount still owed at a point in time.	No

Terminology

This chapter uses certain terminology to explain how sales might be accounted for. This is an area where you may see different terms used to describe what has been described above.

Used in this chapter	Common alternative
Sales day book	Sales journal
Receivables ledger	Debtors ledger, Sales ledger
Receivables control account	Receivables ledger control account Sales ledger control account Total sales control account Debtor control account Account receivable control account

Terminology

This chapter uses certain terminology to explain how purchases might be accounted for. This is an area where you may see different terms used to describe what has been described above.

Used in this chapter	Common alternative
Purchases day book	Purchases journal
Payables ledger	Creditors ledger, Purchases ledger
Payables control account	Payables ledger control account Purchases ledger control account Total purchases control account Creditor control account Account payable control account Bought ledger adjustment account

Answers

A. 1

Creditor Control Account

b/d	870	b/d	11,940
Purchase return	2,560	Purchase	66,180
Cash	58,430		
Discount received	1,660		
c/d	15,370	c/d	770
	78,890		78,890

Debtor Control Account

b/d	14,620	b/d	240
Sales	87,490	Sale return	1,170
Cash	130	Cash	76,210
Bank	2,250	Discount allowed	2,820
c/d	420	Bank	4,120
		c/d	20,350
	104,910		104,910

A. 2

Debtors Control Account

	Rs.'000'		Rs.'000'
Balance b/d	2,600	Cash received from debtors	31,650
Credit sales	35,900	Discount allowed	350
Bank - refund to customer	120	Returns	980
Cheque dishonored	200	Bad debts written off	430
Credit balances c/d	75	Creditors Control Account-contra	1,660
		Balance c/d	3,825
	38,895		38,895

Creditors Control Account

	Rs.'000'		Rs.'000'
Bank - payment to suppliers	23,350	Balance b/d	4,100
Discount received	250	Purchases	27,700
Purchases returns	550	Purchases - not recorded	350
Debtors Control Account-contra	1,660		
Balance c/d	6,340		

A.3 MAY TRANSACTIONS REVISITED

(a) **Day books**

Purchases day book

Date	Supplier	Rs.
2 May	The Bushes Company	540,000
	Flower City	870,000
	D Gibson	250,000
	Weedkill	760,000
	T Greenery	640,000
		3,060,000

Date	Supplier	Rs.
18 May	The Bushes Company	430,000
	Landscape	1,100,000
		1,530,000

Sales day book

Date	Customer	Rs.
4 May	The Office Company	430,000
	V Cork	640,000
	Texas Chain Stores	1,760,000
		2,830,000

Date	Customer	Rs.
21 May	Public Parks	670,000
		670,000

(b) **Accounts in the main ledger**

Capital

31	Balance c/f	2,500,000	1	Bank	2,500,000
		2,500,000			2,500,000
			1 June	Balance b/f	2,500,000

Cash at bank

1	Capital	2,500,000	6	Rent	120,000
9	The Office Company	430,000	12	D Gibson	250,000
10	Texas Chain Stores	1,500,000	12	The Bushes Company	540,000
			15	Advertising	230,000
			31	Rent	180,000
			31	Balance c/f	3,110,000
		4,430,000			**4,430,000**
1 June	Balance b/f	3,110,000			

Purchases

2	Payables	3,060,000			
18	Payables	1,530,000	31	Balance c/f	4,590,000
		4,590,000			4,590,000
1 June	Balance b/f	4,590,000			

Sales

			4	Receivables	2,830,000
31	Balance c/f	3,500,000	21	Receivables	670,000
		3,500,000			3,500,000
			1 June	Balance b/f	3,500,000

Payables control account

12	Cash at bank	790,000	2	Purchases	3,060,000
31	Balance c/f	3,800,000	18	Purchases	1,530,000
		4,590,000			4,590,000
			1 June	Balance b/f	3,800,000

Receivables control account

4	Sales	2,830,000	9	Cash at bank	430,000
21	Sales	670,000	10	Cash at bank	1,500,000
			31	Balance c/f	1,570,000
		3,500,000			3,500,000
1 June	Balance b/f	1,570,000			

Rent (expense)

6	Bank	120,000			
31	Bank	180,000	31	Balance c/f	300,000
		300,000			300,000
1 June	Balance b/f	300,000			

Advertising expenses

15	Bank	230,000	31	Balance c/f	230,000
		230,000			230,000
1 June	Balance b/f	230,000			

(c) **Accounts in receivables and payables ledgers Payables ledger**

Payables - The Bushes Company

12	Cash at bank	540,000	2	Purchases	540,000
31	Balance c/f	430,000	18	Purchases	430,000
		970,000			970,000
			1 June	Balance b/f	430,000

Payables - Flower City

31	Balance c/f	870,000	2	Purchases	870,000
		870,000			870,000
			1 June	Balance b/f	870,000

Payables - D Gibson

12	Cash at bank	250,000	2	Purchases	250,000
		250,000			250,000

Payables - Weedkill

31	Balance c/f	760,000	2	Purchases	760,000
		760,000			760,000
			1 June	Balance b/f	760,000

Payables - T Greenery

31	Balance c/f	640,000	2	Purchases	640,000
		640,000			640,000
			1 June	Balance b/f	640,000

Payables - Landscape

31	Balance c/f	1,100,000		Purchases	1,100,000
		1,100,000			1,100,000
			1 June	Balance b/f	1,100,000

List of balances in the payables ledger

	Rs.
The Bushes Company	430,000
Flower City	870,000
D Gibson	
Weedkill	760,000
T Greenery	640,000
Landscape	1,100,000
	3,800,000

Receivables ledger

Receivables – The Office Company

4	Sales	430,000	9	Cash at bank	430,000
		430,000			430,000

Receivables – V Cork

4	Sales	640,000		Balance c/f	640,000
		640,000			640,000
1 June	Balance b/f	640,000			

Receivables – Texas Chain Stores

4	Sales	1,760,000	10	Cash at bank	1,500,000
				Balance c/f	260,000
		1,760,000			1,760,000
1 June	Balance b/f	260,000			

Receivables – Public Parks

21	Sales	670,000		Balance c/f	670,000
		670,000			670,000
1 June	Balance b/f	670,000			

List of balances in the receivables ledger:

	Rs.
The Office Company	nil
V Cork	640,000
Texas Chain Stores	260,000
Public Parks	670,000
	1,570,000

(d) **Trial Balance as at 31 May 2013**

Home Oak Garden Traders: Trial balance as at 31 May

	Debit Rs.	Credit Rs.
Capital		2,500,000
Bank	3,110,000	
Purchases	4,590,000	
Sales		3,500,000
Payables conrol account		3,800,000
Receivables control account	1,570,000	
Rent	300,000	
Advertising	230,000	
	9,800,000	9,800,000

A.4 JUNE TRANSACTIONS

(a) Main ledger transactions

Date		Debit	Credit
June		Rs.(000)	Rs.(000)
1	Bank	6,500	
	Capital		6,500
2	Purchases	1,800	
	Payables control account		1,800
3	Receivables control account	1,340	
	Sales		1,340
4	Purchases	230	
	Bank		230
5	Motor van (asset account)	2,560	
	Bank		2,560
7	Motor expenses	120	
	Bank		120
9	Receivables control account	1,180	
	Sales		1,180
11	Purchases	3,480	
	Payables control account		3,480
13	Payables control account	250	
	Purchase returns		250
19	Sales returns	110	
	Receivables control account		110
20	Drawings	440	
	Bank		440
21	Payables control account	1,080	
	Bank		1,080
23	Bank	660	
	Receivables control account		660
25	Cash in hand	430	
	Receivables control account		430
28	Payables control account	420	
	Purchase returns		420
29	Sundry expenses	40	
	Cash in hand		40
30	Receivables control account	960	
	Sales		960

(b) Receivables ledger entries

Date		Debit	Credit
June		Rs.(000)	Rs.(000)
3	J Bird	660	
3	D Swann	250	
3	Swallow Company	430	
9	M Parrott	240	
9	Canary Company	260	
9	G Finch	680	
19	D Swann		110
23	J Bird		660
25	Swallow Company		430
30	D Swann	420	
	Canary Company	540	

(c) Payables ledger entries

Date		Debit	Credit
June		Rs.(000)	Rs.(000)
2	C Jones		1,800
11	C Jones		2,400
	E Davies		620
	A Evans		460
13	C Jones	250	
21	E Davies	620	
	A Evans	460	
28	C Jones	420	

A.5 KWARK

(a)

Payables control account

		Rs.(000)			Rs.(000)
6	Bank	700	2	Purchases	4,590
7	Bank	350	9	Purchases	2,403
7	Discount received	25			
9	Purchase returns	400			
	Balance c/d	5,518			
		6,993			**6,993**
				Balance b/d	5,518

Receivables control account

		Rs.(000)			Rs.(000)
3	Sales	4,953	4	Bank	723
12	Sales	1,005	4	Discounts allowed	30
			5	Bank	1,500
			10	Sales returns	270
				Balance c/d	3,435
		5,958			5,958
	Balance b/d	3,435			

(b)

Receivables ledger balances at 31 May	Rs.(000)
Bailey Stores (753 – 723 – 30)	0
Fastshop (1,120 + 1,005)	2,125
Spencers (3,080 – 1,500 – 270)	1,310
Total balances	3,435

= Receivables control account balance: main ledger

(c)

Payables ledger balances at 31 May	Rs.(000)
Ellis (810 – 700)	110
Mendez Trading (1,305 + 753)	2,058
Gibson (375 – 350 – 25)	0
Dynasty (1,140 + 1,650 – 400)	2,390
Liners	960
Total balances	5,518

= Trade payables control account balance: main ledger

Answer 6

(a)

Lotus Pharma
Purchase Day Book

Date	Suppliers	Rs. In million
1-Jan-2016	Shan trader	8.50
	Rahat Store	12.50
	Quality Medicos	15.00
		36.00

(b) Subsidary purchase ledger accounts

Shan Traders

Date	Particulars	Rs. In million	Date	Particulars	Rs. In million
24-Jan	Bank	5.80	1-Jan	Purchases	8.50
31-Jan	Balance c/f	2.70			
		8.50			8.50

Rahat Store

Date	Particulars	Rs. In million	Date	Particulars	Rs. In million
20-Jan	Purchase return	2.50	1-Jan	Purchases	12.50
31-Jan	Account receivable	1.20			
31-Jan	Bank	8.80			
		12.50			12.50

Quality Medicos

Date	Particulars	Rs. In million	Date	Particulars	Rs. In million
28-Jan	Bank (15×98%)	14.70	1-Jan	Purchases	15.00
28-Jan	Discount received (15×2%)	0.30			
		15.00			15.00

Trade Payables Control Account

Date	Particulars	Rs. In million	Date	Particulars	Rs. In million
20-Jan	Purchase return-Rahat	2.50	1-Jan	Purchases 8.5+12.5+15	36.00
24-Jan	Bank-Shan Traders	5.80			
28-Jan	Bank-Quality Medicos	14.70			
28-Jan	Discount received	0.30			
31-Jan	Account receivable.-Rahat	1.20			
31-Jan	Bank-Rahat	8.8			
	c/d	2.7			
		36.00			36.00

Answer: 7

(a) Ali Baba Stationers Day Books

Purchase Day Book

Date	Supplier	Rupees
3-Aug-15	The pen store (450,000 – 25,000)	425,000
	The School Shop	200,000
	Galaxy Stationers	350,000
	The Stationary Store	400,000
	The Office Store	800,000
		2,175,000

Sales Day Book

Date	Customer	Rupees
5-Aug-15	Murjeena Traders	200,000
	Qasim and Company (550,000 – 50,000)	500,000
	Chiragh Limited	250,000
	Sameer Enterprises	400,000
	Hamid and Company	800,000
		2,150,000

21-Aug-15	Murjeena Traders	300,000
	Qasim and Company	200,000
	Chiragh Limited	550,000
	Sameer Enterprises	200,000
		1,250,000

Purchase Return Book

Date	Supplier	Rupees
6-Aug-15	Galaxy Stationers	10,000
	Stationary Store	40,000
		50,000

Sales Return Book

Date	Customer	Rupees
15-Aug-15	Murjeena Traders	25,000
	Chiragh Limited	30,000
		55,000

(b) Receivable Control Account

		Rupees			Rupees
5-Aug-15	Sales	2,150,000	7-Aug-15	Cash & bank (150+250+200+300+400)	1,300,000
21-Aug-15	Sales	1,250,000	15-Aug-15	Sales return (25+30)	55,000
			25-Aug-15	Cash and bank (150+150+300)	600,000
			25-Aug-15	Discount allowed (25+50)	75,000
			31-Aug-15	Balance c/d	1,370,000
		3,400,000			3,400,000

Payable Control Account

		Rupees			Rupees
6-Aug-15	Purchase return	50,000	3-Aug-15	Purchases	2,175,000
10-aug-15	Cash (300+290+250)	840,000			
10-Aug-15	Discount received	25,000			
31-Aug-15	Balance c/d	1,260,000			
		2,175,000			2,175,000

Cash and Bank

		Rupees			Rupees
3-Aug-15	Capital	5,000,000	7-Aug-15	Shop rent	300,000
7-Aug-15	Receivable control a/c	1,300,000	10-Aug-15	Payable control a/c	840,000
12-Aug-15	Sales	250,000	11-Aug-15	Shop repairs	60,000
25-Aug-15	Receivable control a/c	600,000	18-Aug-15	Purchases	150,000
			31-Aug-15	Balance c/d	5,800,000
		7,150,000			7,150,000

Answer: 8

Debtors Control Account

Dr.	Rs.		Cr. Rs.
Balance b/d	1,744,500	Sales returns	144,400
Sales	10,796,300	Cash	9,404,300
Bills R/able dishonoured	30,900	Discount	348,000
Sales return overcast	22,000	Bad debts	16,000
		Bills receivable	508,400
		Creditors control a/c	35,000
		Balance c/d	2,137,600
	12,593,700		12,593,700

Creditors Control Account

Dr.	Rs.		Cr. Rs.
Purchase returns	315,900	Balance b/d	1,366,000
Cash paid	7,210,300	Purchases	8,166,600
Discount received	204,800		
Debtors control a/c	35,000		
Bills payable	277,700		
Salaries expense	26,000		
Suspense account	30,000		
Balance c/d	1,432,900		
	9,532,600		9,532,600

Ans. 9 Gul Brothers

(a) Books of prime entry

Purchase Day Book		
Date	**Supplier**	**Rupees**
3-Feb	QT Stores	295,000
3-Feb	Bana & Co.	190,000
	Total	**485,000**

Sales Day Book			
Date	**Customer**		**Rupees**
18-Feb	Qavi		275,000
18-Feb	Child Care Centre	(158,000×100/110)	173,800
	Total		**448,800**

Cash book							
Date	Description	Cash (Rs.)	Bank (Rs.)	Date	Description	Cash (Rs.)	Bank (Rs.)
8-Feb	Cash sales	300,000	-	15-Feb	XYZ	-	90,000
25-Feb	Chenab	-	68,000				
25-Feb	Ameen Stores	-	32,000				

General Journal			
Date	Description	Debit	Credit
		------ Rupees -----	
23-Feb	Bad debts	65,000	
	Receivables control account - Johar & Sons		65,000

(b) Control accounts

Payables control account					
Date	Description	Rupees	Date	Description	Rupees
15-Feb	Bank – XYZ	90,000	3-Feb	Purchases (295,000+190,000)	485,000
15-Feb	Discount income - XYZ	10,000			

Receivables control account					
Date	Description	Rupees	Date	Description	Rupees
18-Feb	Sales [275,000+(158,000×1.1)]	448,800	23-Feb	Bad debts (Johar & Sons)	65,000
			25-Feb	Bank (68,000+32,000)	100,000

A.10 **Alpha Traders**

Recording of transactions in relevant books of prime entry

Purchases day book

Date	Supplier	Rupees
05-Aug-17	Moon & Co.	475,000
05-Aug-17	Shan Traders	513,000
		988,000

Purchases returns day book		
Date	**Supplier**	**Rupees**
10-Aug-17	Moon & Co.	68,000

Sales day book		
Date	**Customer**	**Rupees**
08-Aug-17	A-Z Super Store	236,000
08-Aug-17	Apollo Center	198,000
		434,000

Cash book

Receipts					Payments				
Date	Description	Discount allowed memo	Cash	Bank	Date	Description	Discount received memo	Cash	Bank
		--------- Rupees ---------					--------- Rupees ---------		
01-08-17	Opening balance	-	178,000	-	01-08-17	Opening balance	-	-	769,000
12-08-17	Sales	-	40,000	-	02-08-17	Office furniture	-	38,000	-
16-08-17	A-Z Super Store	10,250	-	194,750	03-08-17	Purchases	-	85,000	-
16-08-17	Bright & Co.	12,800	-	243,200	25-08-17	Al-Shams	25,000	-	225,000
31-08-17	Closing balance	-	-	556,050	31-08-17	Closing balance	-	95,000	-
		23,050	**218,000**	**994,000**			**25,000**	**218,000**	**994,000**

General Journal

Date	Description	Debit	Credit
		Rupees	
02-Aug-17	Office furniture	129,000	
	Payables control account		129,000
	(Purchased office furniture on credit)		
20-Aug-17	Payables control account	200,000	
	Receivables control account		200,000
	(Adjustments of inter-company balances with Columbus Traders)		

A.11 (a)

Quality services

Trial balance for the quarter ended 30 june2017

S. No	Description		Debit	Credit
			Rs. In '000'	
1	Cash at bank	(9,500 – 5,150) – 5	4,345	
2	Capital	5,000 +240		5,240
3	Fixed assets - Vehicle		1,200	
4	Supplies	650 + 200 – 500	350	
5	Maintenance service revenue	4,500 + 700 – 1,250		3,950
6	Petty cash balance	300 – 250	50	
7	Utility expenses	250 – 20 + 45	275	
8	Wages and salaries	1,450 – 150	1,300	
9	Drawings		390	
10	Office rent expense	900 – 600	300	
11	Bank charges	10 + 5	15	
12	Fixed Assets - Machine		240	
13	Supplies payables	850 – 650		200
14	Supplies expense		500	
15	Security deposits		20	
16	Electricity bill payable			45
17	Petty cash expenses		250	
18	Prepaid salaries		150	
19	Revenue receivables		700	
20	Unearned maintenance revenue			1,250
21	Depreciation expense	60 + 12	72	
22	Allowance for depreciation	(1,200 + 240) x 20% / 12 x 3		72
23	Prepaid office rent	900 x 6/9	600	
			10,757	10,757

Workings:

Journal entries:

i.	Bank	5,000	
	Capital		5,000
ii.	Vehicle	1,200	
	Bank		1,200
iii.	Office supplies	650	
	Bank		650
iv.	Bank	4,500	
	Maintenance services income		4,500
v.	Petty Cash	300	
	Bank		300
vi.	Utility Bills	250	
	Bank		250
vii.	Wages and Salaries	1,450	
	Bank		1,450

viii.	Drawings	390	
	Bank		390
ix.	Rent expense (900/9 x 3)	300	
	Prepaid rent	600	
	Bank		900
x.	Bank Charges	10	
	Bank		10
xi.	Machine	240	
	Capital		240
xii.	Office Supplies	200	
	Payable (850 – 650)		200
xiii.	Supplies expenses	500	
	Supplies		500
xiv.	Refundable deposit	20	
	Utility Bills		20
xv.	Utility Bills	45	
	Payable		45
xvi.	Petty Expense	250	
	Petty Cash		250
xvii.	Prepaid salary	150	
	Wages		150
xviii.	Bank Charges	5	
	Bank		5
xix.	Receivables against maintenance	700	
	Service Income		700
xx.	Maintenance services income	1,250	
	Unearned income		1,250
xxi.	Depreciation	72	
	Accumulated Depreciation 1,200 x 20% x 3/12 = 60 240 x 20% x 3/12 = 12 72		72

A.12

Trial balance for the month of January 2018

Description		Debit	Credit
		Rupees	
Capital	1,000 + 8,000 + 3,000		9,300
Purchase return /Return outward 900 + 50			950
Discount allowed	150 + 90 – 150	90	
Sales	16,600 + 1,250		17,850
Office rent	200 + 300	500	
Fixed assets	1,500 + 250 + 300 – 50	2,000	
Purchases	18,000 + 650 – 100	18,550	
Sales return /Return inward		60	
Drawings	100 + 180 + 100 +50	430	
Utility bills	120 + 140	260	
Trade debtors (W – 1)	(- 6,250 – 1,800 + 6,100 + 16,600 +150 – 4,500)	10,300	
Trade creditors (W-2)	(- 4,000 + 18,000 – 900 – 4,500)		8,600
Discount received			100
Cash in	1,850 – 1,230	620	
Cash at bank	16,760 – 12,770	3,990	
		36,800	**36,800**

(W – 1) Trade debtors

		Rupees
Quality Traders	6,250-150-6,100+6,100+150	6,250
Himalaya Super Store	2,350-90-300-1,410	550
ABC & Co.	8,000-4,500	3,500
	16,000	**10,300**

(W-2) Trade Creditors

		Rupees
ABC & Co.	4,500-4,500	-
Zee Traders	6,000-900-100-500-3,400	1,100
Unity Enterprises	7,500	7,500
	18,000	**8,600**

Workings:

Journal etries:

i.	Cash	1,000	
	Bank	8,000	
	Capital		9,000
ii.	Cash	50	
	Purchase Return		50
iii.	Bank	6,100	
	Discount Allowed	150	
	Debtor Control a/c		6,250
iv.	Bank	1,250	
	Sales		1,250
v.	Cash	300	
	Bank	1,410	
	Discount Allowed	90	
	Debtor Control a/c		1,800
vi.	Cash	500	
	Bank		500
vii.	Office Rent	500	
	Cash		200
	Bank		300
viii.	Fixed Assets	1,500	
	Bank		1,500
ix.	Purchases	650	
	Bank		650
x.	Debtor Control a/c	6,100	
	Bank (Dishonored Cheque)		6,100
	Creditor Control a/c	4,000	
	Cash		500
	Bank		3,400
	Discount Received		100
xi.	Sales Return	60	
	Bank		60
xii.	Fixed Assets	250	
	Cash		250
xiii.	Drawings	280	
	Cash		100
	Bank		180
xiv.	Utility Bills	260	
	Cash		120
	Bank		140
xv.	Purchases	18,000	
	Creditor Control a/c		18,000
xvi.	Creditor Control a/c	900	
	Purchase Return		900

xvii.	Debtor Control a/c	16,600	
	Sales		16,600
xviii.	Fixed Assets	300	
	Capital		300
xix.	Drawings	100	
	Purchases		100
xx.	Debtor Control a/c	150	
	Discount Allowed (Discount allowed to be reversed because of dishonor cheque)		150
xxi.	Drawings	50	
	Fixed Assets		50
xxii.	Creditor Control a/c	4,500	
	Debtor Control a/c		4,500

A.13 Henry Brothers
Books of prime entry

Purchase day book		
Date	**Supplier**	**Rupees**
4-Jul-18	Alpha Enterprises	250,000
4-Jul-18	Bravo Traders	180,000
		430,000

Purchase return day book		
Date	**Supplier**	**Rupees**
17-Jul-18	Alpha Enterprises	35,000
		35,000

Cash Book/Bank Book ----- Rupees -----

Receipts				Payments				
Date	**Description**	**Cash**	**Bank**	**Date**	**Description**	**Discount Received**	**Cash**	**Bank**
1-Jul-18	Balance b/d	76,000	286,000	6-Jul-18	Office furniture			50,000
8-Jul-18	Sales		300,000	14-Ju-18	Return inwards {(245,000)×0.2}		49,000	
8-Jul-18	Sales (250,000×0.98)	245,000		17-Jul-18	Alpha Enterprises - Account payable {(250,000-35,000)×0.97}	6,450		208,550
16-Jul-18	Disposal/gain on	12,000						
23-Jul-18	Sales	236,500						
30-Jul-18	Cash		200,000	26-Jul-18	Purchases {(300×500×0.95)}			142,500
				28-Jul-18	Loan		115,000	
					Interest account		35,000	
				30-Jul-18	Bank		200,000	
				31-Jul-18	Balance c/d		170,500	384,950
		569,500	**786,000**			**6,450**	**569,500**	**786,000**

General Journal

Date	Description	Debit	Credit
		-------- Rupees --------	
6-Jul-18	Office furniture - cost	40,000	
	Advances		40,000
16 July 18	Accumulated depreciation	75,000	
	Furniture		75,000

A.14

Chaman Stores

Trial balance for the month of January 2019

S. No.	Description		Debit	Credit
			----- Rs. in '000 -----	
1.	Cash		36	
2.	Bank		359	
3.	Capital			500
4.	Sales	267 + 19 +36		322
5.	Bank loan			200
6.	Trade receivables	267 – 30 – 95 - 5	137	
7.	Security deposit		45	
8.	Furniture	40 +35 + 55	130	
9.	Insurance		15	
10.	Trade payables	370 - 144 - 13 - 6		207
11.	Purchases	370+35 +43 -30	418	
12.	Return inward (sale return)	30 + 4	34	
13.	Salaries		76	
14.	Utilities	18-6	12	
15.	Drawings	6 + 30	36	
16.	Rent		22	
17.	Rent payable			22
18.	Other payables (furniture payable)			55
19.	Return outward (purchase return)			13
20.	Discount allowed (to Rafiq Ltd)	130 - 30 - 95	5	
21.	Discount received (from shabbier & sons)	150 - 44 - 100		6
			1,325	**1,325**

Test question

Q.5 Following information pertains to Omega Limited (OL) for the month of July 2019:

(i) Opening balances:

	Rupees
Cash in hand	85,000
Cash at bank - as per cash book	650,000
- as per bank statement	780,000

(ii) Transactions for the month:

Date	Transactions
02-Jul	Goods purchased on credit from Danish Stores for Rs. 475,000 (net of 5% trade discount).
04-Jul	Goods sold on credit to XYZ & Co. for Rs. 500,000 after a trade discount of 10%. In this respect, transportation charges of Rs. 15,000 were paid in cash by OL.
05-Jul	Goods sold on credit to Zaid Brothers for Rs. 640,000 and offered a discount of 5% on payment within 30 days.
07-Jul	Cheques issued to Zee & Co. for Rs. 400,000 in full and final settlement of one of its old invoice of Rs. 425,000 and ABC Stores for Rs. 190,000 (net of 5% payment discount).
09-Jul	Goods sold to Qavi & Sons and received a cheque of Rs. 58,000.
10-Jul	Cash payment of utility bills amounted to Rs. 45,000. This included a bill of Rs. 5,000 belonged to the owner's residence.
12-Jul	Goods returned by Zaid Brothers amounted to Rs. 135,000.
12-Jul	Goods returned to Danish Stores amounted to Rs. 50,000.
13-Jul	Goods purchased on credit for Rs. 700,000 from Chenab Stores subject to 10% discount on payment within 30 days.
15-Jul	A cheque of Rs. 100,000 was encashed for day to day cash requirements.
20-Jul	Fully depreciated laptops costing Rs. 134,000 were scrapped.
21-Jul	New laptops were purchased for Rs. 245,000 from Shifa Electronics and issued a cheque of Rs. 100,000 in part payment.
23-Jul	40% of the goods sold to Qavi & Sons on 9 July were returned and the amount was refunded in cash. These goods were sold at cost plus 25%.
26-Jul	Goods purchased for cash from Ravi Brothers having list price of Rs. 68,000 and availed discount of 5%.
30-Jul	Cheques received from Zamil Store of Rs. 285,000 (net of 5% payment discount) and Zaid Brothers of Rs. 500,000 in settlement of an old invoice of Rs. 550,000.

Required:

Enter the above transactions in the books of prime entry in a proper format. (Narrations are not required) **(15)**

A.5 **Omega Limited**

Books of prime entry

Purchases day book		
Date	**Supplier**	**Rupees**
2-Jul	Danish Stores	475,000
13-Jul	Chenab Stores	700,000
		1,175,000

Sales day book		
Date	**Customer**	**Rupees**
4-Jul	XYZ & Co.	500,000
5-Jul	Zaid Brothers	640,000
		1,140,000

Purchases returns day book		
Date	**Supplier**	**Rupees**
12-Jul	Danish Stores	**50,000**

Sales returns day book		
Date	**Customer**	**Rupees**
12-Jul	Zaid Brothers	**135,000**

General Journal			
Date	**Description**	**Debit**	**Credit**
		------ Rupees ------	
20-Jul	Accumulated depreciation office equipment (laptops) Office equipment (laptops)	134,000	134,000
21-Jul	Office equipment (laptops) Other payables – Shifa Electronics	145,000	145,000

Cash Book									
Receipts					**Payments**				
Date	**Description**	**Discont allowed**	**Cash**	**Bank**	**Date**	**Description**	**Discount Received**	**Cash**	**Bank**
1-Jul	Balance		85,000	650,000	4-Jul	Transportation expense		15,000	
9-Jul	Sales			58,000	7-Jul	Trade payable - Zee & Co.	25,000		400,000
15-Jul	Bank		100,000		7-Jul	Trade payable - ABC Stores (190,000/95x5)	10,000		190,000
30-Jul	Trade rec. - Zamil Store (285,000/95 x 5)	15,000		285,000	10-Jul	Utility bills		40,000	
30-Jul	Trade rec. - Zaid Brothers (550,000-500,000)	50,000		500,000	10-Jul	Drawings		5,000	
					15-Jul	Cash			100,000
					21-Jul	Office equipment (laptops)			100,000
					23-Jul	Sales return (58,000×40%)		23,200	
					26-Jul	Purchases (68,000×95%)		64,600	
					31-Jul	Balance		37,200	703,000
		65,000	**185,000**	**1,493,000**			**35,000**	**185,000**	**1,493,000**

Inventories: [Stock Counts]

Problems of Calculating Stock: (in case of a trading business):

The following equation can be rearranged to calculate the missing figures:

Opening Stock + Purchases – Closing Stock = Cost of Sales

If Closing Stock is to be calculated:

Opening Stock + Purchases – Cost of Sales = Closing Stock

If Opening Stock is to be calculated:

Opening Stock = Cost of sales + Closing Stock – Purchases

Suppose:

(1) Stock as on 15-07-2014 is given and we need to find stock as on 30-06-2014.

It means given stock is sort of closing stock for these 15 days and we need to find out opening stock.

(2) Stock as on 20-06-2013 is given and we need to find stock as on 30-06-2013. In this case a sort of opening stock of these 10 days is given and we need to find out closing stock.

When sale is recorded: sale is recorded when control is transferred from seller to buyer. Control is transferred when risks and rewards are transferred from seller to buyer. Normally risks and rewards are transferred when the goods are despatched / delivered.

The invoice of goods is normally issued by seller at the time of delivery of goods. If however invoice is not issued, sale should still be recorded when the risks and rewards are transferred by seller to buyer.The issuance of invoice is not important for recording of sale.

When purchase is recorded: purchase is recorded by buyer when control is transferred from seller to buyer. Control is transferred when risks and rewards are transferred from seller to buyer. Normally risks and rewards are transferred when the goods are received.

The invoice of goods is normally received by buyer at the time of reciept of goods. If however invoice is not received, purchase should still be recorded by buyer when the risks and rewards are transferred by seller to buyer. The receipt of invoice is not important for recording of purchase.

Q.1 Mr. Tufail runs a retail store and makes up his annual accounts to 30 June each year. This year he was unable to take stock of physical inventory till 11 July, 2006 on which date the value of physical stock was calculated as Rs. 177,300. However, while making the valuation he made an error as a sub-total of Rs. 21,500 on one of the stock sheet was entered to the summary of stock sheets as Rs. 12,500.The following information relating to the period 1 July 2006 to 11 July 2006 is available:

(i) Sales invoices totaling Rs. 90,000 were issued. An invoice of Rs. 8,400 pertained to goods which had not been delivered at the time of stock verification. Another invoice of Rs. 14,100 pertained to goods which had been delivered on29 June 2006.

(ii) Credit advices for sales returns amounting to Rs. 4,200 had been issued. These included advices of Rs. 2,700 relating to goods returned prior to year end.

(iii) Purchase invoices of Rs. 60,100 were received. Of these, invoices totaling Rs. 11,100 were in respect of goods received on 28 June 2006 whereas an invoice of Rs. 13,800 pertained to goods received on 15 July, 2006.

(iv) No invoices had been received for goods costing Rs. 9,400 which had been delivered prior to 30 June 2006.

Required:
Determine value of his physical stock at cost on 30 June 2006 if gross profit is 20% of cost price.
Note: credit note / credit advice is a document (page) which is issued as an evidence of sale return

Exceptions to the situations where goods are despatched but risks and rewards are not transferred.

When sale is recorded: sale is recorded when risks and rewards are transferred from seller to buyer. Normally risks and rewards are transferred when the goods are despatched / delivered. However, there are exceptions to the situation where goods are despatched but risks and rewards are not transferred. For example:

1. **Sale or return basis:**

On 1.1.2015, 1000 units are delivered by a manufacturer to a retailer on sale or return basis (means retailer can return the goods not purchased by customers). Upto 31.12.2015, 20 units are still left with retailer which can be returned.

Conclusion: manufacturer should record the sale of 980 units during the year; while the remaining 20 units should be included in the stock of manufacturer at cost rather than in the stock of retailer (even though these units are physically held by retailer)

2. **Sale on approval basis:**

Q.2 Sun Soya Oil & Company is a wholesaler of cooking oil. Due to an emergency, its annual stock taking was delayed till 3 July 2012, on which date the physical stock was valued at Rs. 24 million.An examination of related records disclosed that the following events took place on**1st** and **2nd** July, 2012:

(i) Sales invoices amounting to Rs. 4 million were issued. These included invoices amounting to:
  (a) Rs. 200,000 in respect of oil which was dispatched on 29 June 2012 but had not been invoiced.
  (b) Rs. 400,000 in respect of oil not dispatched until 5 July 2012 and;
  (c) Rs. 200,000 in respect of oil on sale or return basis.
  (d) The average rate of gross profit is $33\frac{1}{3}$% of cost.

(ii) Returns from customers totaled Rs. 600,000.

(iii) Purchase invoices amounting to Rs. 1.8 million were received. These included invoices worth:
  (a) Rs. 600,000 for oil received in June 2012, and;
  (b) Rs. 300,000 for oil received on 7 July 2012.

(iv) Purchase returns totaled Rs. 400,000.

A review of the records also disclosed the following errors:

(a) Stocks lying in Abbotabad were not included in the physical count. The cost of such stock on 30 June 2011 and 3 July 2012 was Rs. 0.5 million and Rs. 3 million respectively.

(b) An arithmetical error in the stock sheets on 3 July 2012 resulted in an overvaluation of Rs. 450,000.

Required:

Prepare a statement showing the correct amount of the stock as on 30 June 2012.

Whether Receipt Means Sale?

Cash	XX		
Sales		XX	(Yes)
Debtor	XX		
Sales		XX	(No)

Therefore receipt does not always means sale.

Therefore when should sale be recorded? Sale should be recorded by seller when risks and rewards are transferred from seller to buyer. Normally it is when the goods are despatched / delivered by seller to buyer.

Whether Payment Means Purchases?

Purchases	XX		
Cash		XX	(Yes)
Purchases	XX		
Creditors		XX	(No)

Therefore payment does not always means purchase. Purchase should be recorded by buyer when risks and rewards are transferred from seller to buyer.

Q.3 Khan Limited closes its accounts on June 30 each year. The company was unable to take stock of physical inventory until July 14, 2009 on which date the physical inventory was valued at Rs. 185,000. The following details are available in respect of the period July 1 to July 14, 2009:

1) Payments against purchases amounted to Rs. 48,000 and included:
- Rs. 5,000 in respect of goods received on June 28, 2009;
- Rs. 6,000 in respect of goods received on July 18, 2009;
- Rs. 2,000 in respect of goods received and returned to supplier on the same date i.e. July 7, 2009

2) Collection against sales amounted to Rs. 60,000 and included:
- Rs. 1,500 in respect of goods which left the warehouse on June 29, 2009;
- Rs. 2,800 in respect of goods which were not dispatched until July 15, 2009;
- Rs. 760 in respect of goods invoiced and dispatched on July 10, 2009 but returned by the customers on July 12. These were included in the stock taken on July 14, 2009.

3) The rate of gross profit is 25% of selling price

4) Goods costing Rs. 6,000 were purchased on June 28 but remained unpaid till July 24, 2009.

5) An invoice amounting to Rs. 10,000 was raised on July 9, 2009 but remained uncollected till July 14, 2009.

6) An item costing Rs. 9,000 which had been purchased on June 25, 2009 was damaged on July 4, 2009. It can be repaired at a cost of Rs. 1,000 and sold for Rs. 7,000 and has been taken in stock at its net realizable value.

7) Stock count sheets prepared on July 14, 2009 showed the following discrepancies:

- A page total of Rs. 5,000 had been carried to the summary as Rs. 6,000.
- The total of another page had been undercast by Rs. 200.

8) Included in the physical count were goods costing Rs. 2,200 which were held on behalf of a supplier.

Required:

Determine the amount of stock required to be disclosed in the financial statements as at June 30, 2009. **(15)**

Q.4 Afridi does not keep perpetual records of stock. At the end of each quarter, the value of stock is determined through physical inventory. However, the record of inventory taken on 31 March2011 was destroyed in an accident and Afridi has extracted the following information for the purpose of stock valuation:

(i) Invoices entered in the purchase day book, during the quarter, totaled Rs. 138,560 of which Rs. 28,000 related to the goods received on or before 31 December 2010. Invoices entered in April 2011 relating to goods received in March 2011 amount to Rs. 37,000.

(ii) Sales invoiced to customers amounted to Rs. 151,073 of which Rs. 38,240 related to goods dispatched on or before 31 December 2010. Goods dispatched to customers before 31 March 2011 but invoiced in April 2011 amounted to Rs. 25,421.

(iii) Credit notes of Rs. 12,800 had been issued to customers in respect of goods returned during the period.

(iv) Purchases included Rs. 2,200 spent on acquisition of a ceiling fan for the shop.

(v) A sale invoice of Rs. 5,760 had been recorded twice in the sales day book.

(vi) Goods having sale value of Rs. 2,100 were given by way of charity.

(vii) Afridi normally sells goods at a margin of 20% on cost. However, he had allowed a special discount of 10% on goods costing Rs. 6,000 which were sold on 15 February 2011.

(viii) On 31 December 2010, the stock was valued at Rs. 140,525. However, while reviewing these stock sheets on 31 March 2011 the following discrepancies were found:

   a. A page total of Rs. 15,059 had been carried to the summary as Rs. 25,059.
   b. 1,000 items costing Rs. 10 each had been valued at Rs. 0.50 each.

Required:

Calculate the amount of stock in hand as on 31 March 2011.

Q.5 Saqib is the sole proprietor of Saqib & Company. He keeps no running records of his stock but a physical count of stock is made at the end of each quarter. The record of stock taken on 30 June 2013 was accidentally destroyed before the items could be valued and therefore he needs to rely on the following information for valuation of stock:**1)** The cost of the stock on 31 March 2013 based on physical count was Rs. 800,525 but the following discrepancies have been detected in the stock sheets:

- A page total of Rs. 6,059 has been carried to the summary as Rs. 6,509.
- The total of a page has been undercast by Rs. 980.
- 100 units of a stock item which costed Rs. 50 each had been taken at 50 paisa each.

2) Invoices entered in the Purchase Book during the month of April, May and June 2013 totalled Rs. 138,560. Of this total, Rs. 12,300 related to goods received on or prior to 31 March 2013. Invoices amounting to Rs. 23,300 relating to goods received in June 2013 were entered in July 2013.

3) Invoices issued to customers in April, May and June 2013 amounted to Rs. 251,070. Of this total, Rs. 13,825 related to goods despatched on or before 31 March 2013. Goods despatched to customers before 30 June 2013 but invoiced in July 2013 totalled Rs. 25,245.

4) Credit notes issued in respect of goods returned during the quarter amounted to Rs. 11,290.

The gross margin earned by Saqib is 25% of cost.

Required:

Statement showing the computation of cost of stock at 30 June 2013. **(11)**

Answers:

A.1

Cost of stock as on July 11.2006		177,300
Add	Balance Understated	9,000
	Cost of Sales (W-1)	55,000
Less:	Purchases (W-2)	(35,200)
Value of Stock as on June 30,2006		206,100

Working 1 Cost of Sales

Sales as per invoice			90,000
Less:	Goods no delivered		8,400
Less:	Goods delivered not invoiced		14,100
	Sales: adjusted		67,500
Less:	Sales Return	4,200	
	Prior period return	(2,700)	(1,500)
Net Sales			60,000
	Cost of sales (66,000 X 100/120)		55,000

Working 2	Purchases	
	As per invoice	60,100
	Invoice of June 28,2006	(11,100)
	Invoice of June 15,2006	(13,800)
		35,200

A.2

		Rupees In "000"	
value of physical stock as on 3 July 2012			24,000
	Add: cost of sales between 1st and 3rd July		
A)	Sales during 1-2 July 2012	4,000	
	Goods dispatched on 29 June 2012 but not invoiced	(200)	
	goods dispatched after stock taking	(400)	
	goods on sales or return basis	(200)	
		3,200	
B)	Return inward/Sales return	(600)	
		2,600	
	Gross profit margin @ 25% of above	(650)	1,950
	Goods on sales or return basis (200 X 0.75)		150
C)	Purchase invoices received on 1 and 2 July	(1,800)	
	goods received in June 2012	600	
	goods received on 7 July	300	
		(900)	
D)	Purchase return	400	(500)
	Stock at Abbotabad		3,000
	Overvaluation of stock		(450)
Value of stock as on 30 June 2012			**28,150**

A. 3

Khan Limited
Statement of Calculation of Stock
As on 30th June

Stock as on 14th July	185,000
Less: Overcasting error	(1,000)
Add: Under casting error	200
Less: Goods held on behalf of supplier	(2,200)
Adjustment of NRV	3,000
Purchases (W-1)	(35,000)
Cost of sales (W-2)	48,705
Stock as on 30th June, 2013	198,705

W-1 Purchases

Payments	48,000
Received before 1st July	(5,000)
Received after 14th July	(6,000)
Goods returned to supplier	(2,000)
	35,000

W-2 Cost of Sales

Collection against sales	60,000
Adjustments to the above	
Last year sales	(1,500)
Sold and not delivered	(2,800)
Sold and returned	(760)
Sales on account	10,000
	64,940

Margin = 25% of sales

= 75 + 25 = 100

$$\text{Cost of Sales} = \frac{\text{Sales}}{100} \times 75$$

$$= \frac{64{,}940}{100} \times 75$$

= 48,705

or

Creditors

Cash	48,000	b/d (5,000 + 6,000)	11,000
		Purchase	$\boxed{35{,}000}$
c/d	6,000	c/d (6,000 + 2,000)	8,000

Debtors

b/d	1,500	Cash	60,000
Sale	$\boxed{64{,}940}$		
c/d (2,800 + 760)	3,560	c/d	10,000

A.4

Statement showing the amount of physical stock
As on March 31, 2011

		Rupees
Stock as on December 31,2011	(Working -1)	140,025
Add: Purchases for the quarter	(Working - 2)	145,360
		285,385
Less: Adjusted Cost of sales	(Working - 3)	(100,345)
Less: goods given in charity (100/120 of Rs. 2,100)		(1,750)
Physical stock balance as on March 31,2011		183,290

Working 1	Rupees
Stock as on December 31,2010	
Stock as valued previously	140,525
Add: Cost of 1,000 items recorded at Re. 0.50 per item instead of Rs. 10 per item.	9,500
	150,025
Less: error in carry forward of a page total	(10,000)
Actual stock as on December 31,2010	140,025

Working-2	
Purchases for the quarter ended March 31,2011	
Total of Invoices from Jan. 01 to Mar. 31,2011 as per purchased day book	138,560
Add: Goods purchased before march 31,2011 but recorded In April 2011	37,000
Less: Invoices pertaining to Goods received before December 31,2011	(28,000)
Less: Purchase of ceiling fan	(2,200)
	145,360

Working-3	
Cost of sales for the quarter	
Total of sales Invoices raised from January 01 to March 31,2011	151,073
Add: Goods dispatched before March 31,2011 but invoiced in April 2011	25,421
Less: Goods dispatched before December 31,2010 but invoiced during the quarter ended March 31,2011	(38,240)
Less: Sale invoice recorded twice	(5,760)
Net sales	132,494
Sales at lower markup	*(6,480)
	126,014

*6,000/100 x 120 = 7,200
Less: discount (10%) = (720)
$\boxed{6,480}$

Cost of Sales

126,014-12,800	= 113,214 X 100/120	=	94,345
Cost of Sales at lower markup		=	6,000
Total cost of sales		=	$\boxed{100,345}$

A. 5

Statement showing the amount of Physical Stock at Cost as on 31st March, 2013		Rs.
(a)	Stock at cost as on 31 March 2013	800,525
	Add: Cost of undervalued items [Rs, 49.5 (50,00 - 0.5) x 100]	4,950
	Total of a page under cast	980
	Less: Error in carry forward of a page total (Rs, 6,509 - Rs. 6,059)	450
	Adjusted stock as on 31 March 2013	**806,005**
(b)	Purchases from April to June 2013	138,560
	Add: Goods purchased before 30 June 2013 but recorded in July 2013	23,300
	Less: Goods received before 31 March 2013 but recorded in the later months	12,300
	Adjusted cost of purchases for April to June 2013	**149,560**
(c)	Sales from 1 April 2013 to 30 June 2013	251,070
	Add: Goods despatched before 30 June 2013 but invoice raised in July 2013	25,245
	Less: Goods despatched before 31 March 2013 but recorded in the later months	13,825
	Less: Credit notes issued to customers for sales return during April to June 2013	11,290
		251,200
	Less: Gross margin @ 25% on cost (251,200 / 125 x 100)	50,240
	Adjusted cost of sales for April to June 2013	**200,960**
(d)	Stock as on 30 june 2013	
	Adjusted stock as on 31 March 2013	806,005
	Purchases	149,560
	Cost of sales	(200,960)
	physical stock as on 30 June 2013	**754,605**

Disclosures of inventories:

The financial statements shall disclose:

(i) Accounting policies used in measuring inventories including cost formula used.

(ii) Total *carrying amount of inventories and the carrying amount in classification appropriate to entity (if manufacturing business).

(iii) The amount of inventories recognized as an expense (means amount of cost of sales).

(iv) Amount of any write-down of inventories recognized as an expense (means any loss due to lower NRV or because of damage of goods).

(v) The carrying amount of inventories pledged as security for liabilities.

*carrying amount means closing value of inventory that will appear in statement of financial position.

Question 1

A company deals in Solar Panels which are imported from China. The company follows a perpetual inventory system and values its inventory on weighted average basis. Details of sales and purchases during the year ended 30 June 2015 are as follows:

(i) Opening inventory on 1 July 2014 amounted to Rs. 49,000,000 and consisted of 2,450 solar panels.

(ii) Purchases during the year were as follows:

Date	Quantity (Units)	Price (Rs. In '000')
30-Sep-2014	4,200	78,120
31-Mar-2015	4,350	87,000

There are non refundable and refundable taxes of 12% and 17% respectively.

(iii) Sales during the year were as follows:

Date	Quantity (Units)	Price (Rs. In '000')
31-Jul-2014	2,100	52,500
31-Oct-2014	2,050	48,750
28-Feb-2015	2,300	55,200
15-May-2015	2,260	53,110

(v) On 31 May 2015, 50 solar panels were totally damaged and were written off (means record as a loss).

(vi) On 30 June 2015 there was a significant decline in the prices of solar panels as a new type of solar panel was introduced in the market. Selling prices are now Rs. 18,500 per unit. However, the company has decided to make some modification in its product which will enable it to sell it at Rs. 22,000 per unit. Cost of modification will be Rs. 2,500 per unit.

Required:

Prepare disclosure of inventories (also called as note of inventories) in the financial statements for the year ended 30 June 2015 in accordance with the requirements of IAS-2 'Inventories'. **(13)**

Question 2

A company deals in imported equipment. The management follows periodic inventory system to maintain and update its inventory records, and values its stock on weighted average.
The following information pertains to the year ended 31 December 2016.

- Opening inventory amounted to Rs. 12,000,000 and consisted of 600 units.
- Purchases during the year were:

Date	Units	Per Unit
31-Mar-16	300	21,500
16-Jun-16	300	22,000
31-Oct-16	400	23,000

- Sales during the year were as follows:

Date	Units	Rate/Unit
25-Feb-16	420	30,000
15-Jul-16	340	30,000
2-Sep-16	390	30,000

- On 10 April 2016, 50 units from the purchase on 31 March were found to be damaged and returned to the supplier.
- During the year, 80 units were damaged in an accident in the warehouse and were written off.
- 75 units were returned by a customer on 25 September, from the sale made on 2 September 2016:
- During the stock count conducted on 31 December 2016, it was found that 100 units were slightly damaged with an estimated selling price of 50% of the normal selling price. Estimated repair charges are Rs. 5,000 per unit.

Required:

(a) Value of inventory to be disclosed in the financial statements on 31 December 2016. **(07)**

(b) Pass necessary journal entry for the loss of inventory. **(02)**

(c) Show the disclosures for inventory (also called as note of inventory) in financial statements for the year ending 31 December 2016. **(04)**

A.1

Inventory is measured at lower of cost and NRV and cost is measured by using weighted average method.

	2015
1. Closing stock	43,680

2. Closing inventory comprises of items costing Rs. 50,015,000 valued at net realizable value of Rs. 43,680,000.
3. The inventory expenses (cost of sales) for the year is Rs. 189,138,000 (W-4)
4. Damaged inventory of Rs. 1,116,000 has been written off. (50 × 22.328)
5. Loss due to lower NRV [50,015 – 43,680] 6,335
6. There are no inventories pledged as security.

Workings:

Rs. In '000'

Date	**Purchases / receipts**			**Sales / issuance**			**Stock balance**		
	Qty	**PUC**	**Value**	**Qty**	**PUC**	**Value**	**Qty**	**PUC**	**Value**
1-7-14							2,450	20.000	49,000
31-7-14				2,100	20.000	42,000	350	20.000	7,000
30-9-14	4,200	20.832	87,494				4,550	20.786	94,494
31-10-14				2,050	20.768	42,574	2,500	20.786	51,920
28-2-15				2,300	20.768	47,766	200	20.786	4,154
31-3-15	4,350	22.400	97,440				4,550	22.328	101,594
15-5-15				2,260	22.328	50,462	2,290	22.328	51,132
31-5-15	(50)	22.328	(1,116)				2,240	22.328	50,015
Total	**8,500**		**183,818**	**8,710**		**182,802**			

(W-1) Cost of Purchases

		Sep-14	**Mar-15**
Purchase price	(A)	78,120	87,000
Non-refundable taxes	(A × 12%)	9,374	10,440
Total cost		87,494	97,440

(W-2) Net Realizable Value

		Rs. '000'
Estimated selling price	(22 × 2,240)	49,280
Less: Estimated cost of completion/repair	(2.5 × 2,240)	(5,600)
		43,680

(W-3) Loss due to lower NRV is (50,015 – 43,680)	6,335

(W-4) cost of sales:

	Rs. '000'
Opening stock	49,000
Purchases (87,494 + 97,440 -1,116)	183,818
Closing stock	(43,680)
	189,138

Or *[42,000 + 42,574 + 47,766 + 50,462 + 6,335 (loss of NRV)] = 189,138*

Note: cost of sales are increased by 6,337 which is that loss due to lower NRV. This loss is to be recorded immediately.

***If* Periodic Inventory System: [Solar Panels] (Weighted Average Method)**

Disclosures:

Inventory is measured at lower of cost and NRV and cost is measured by using weighted average method.

Value of closing stock (W 1) 43,680

Loss due to lower NRV [47,645 – 43,680] = 3,965

Cost of damaged goods = 50 × 21.27 (W.1) = 1,064.5

Cost of Sales:

Opening Stock	49,000
Add Purchases [87,494 + 97,440 – 1,064.5]	183,869
Less Closing Stock	(43,680)
	189,189

There are no inventories pledged as security.

W 1

$$= \left[\frac{49{,}000 + 87{,}494 + 97{,}440}{2{,}450 + 4{,}200 + 4{,}350}\right]$$

$$= \frac{233{,}934}{11{,}000} = 21.27/\text{unit}$$

Closing Stock = 2,240 × 21.27 = 47,645

NRV = 2,240 × [22 – 2.5] = 43,680

A.2

(a) Cost of Closing Stock

Weighted average cost per unit – Opening stock (Rs.) + Purchases (Rs.) – Purchase returns (Rs.)/ Opening Units + Units Purchased – Units Returned

		Rs.	Units
Opening stock		12,000,000	600
Purchases	31-Mar-16	6,450,000	300
	16-Jun-16	6,600,000	300
	31-Oct-16	9,200,000	400
Purchase returns	(50*21,500)	(1,075,000)	(50)
Total		33,175,000	1,550

Per unit = 33,175,000/1,550

21,403

value of closing stock

= 600 + 300 + 300 + 400 – 420 – 340 – 390 – 50 – 80 + 75 = 395

Damaged units = 100

Good units = 395 – 100 = $\boxed{295}$

		Rs.
Value of good units = 295 × 21,403 =		6,313,885
Value of damaged goods:		
Cost (100 x 21,403)		2,140,300
NRV per Unit:		
Estimated selling price (50% x 30,000)	15,000	
Less: Cost of repairs	5,000	
NRV	10,000	
Total NRV of damaged goods = 100 x 10,000 =		1,000,000
Total Value of closing inventory on 31 Dec. (6,313,885 + 1,000,000)		7,313,885

(b)

Cost of inventory lost in an accident = 80 x 21,403 =		1,712,240
Journal Entry:		
Loss of stock	1,712,240	
Purchases		1,712,240

(c) **Disclosures:**

Stocks are valued at the lower of cost and Net Realisable Value. Cost is calculated using weighted average.

	31-Dec-16
1. Closing stock	7,313,952

2. Value of stock as on 31 December 2016 includes items costing Rs. 2,140,300 (W-1), which are valued at 1,000,000 (its NRV).
3. Goods damaged during the year costing 1,712,240.
4. Loss due to lower NRV is 1,140,300 [2,140,300 – 1,000,000]
5. Inventory expenses (cost of sales) for the year amounted to Rs. 24,148,525 (W-2)

(W-1)	100 x 21,403 =	2,140,300
(W-2)	Opening Stock =	12,000,000
	Purchases [(6,450 + 6,600 + 9,200 – 1,075) – 1,772.24]	19,462,760
	Closing Stock	(7,313,885)
	Cost of Sales	24,148,875

6.There are no inventories pledged as security.

Manufacturing Business:

In such a business a factory in addition to head office (in which there are admin and selling departments) is needed to manufacture the goods. In such type of business an extra statement called as **cost of goods manufactured statement** is also prepared in addition to an Income Statement.

Before the format of cost of goods manufactured; we have to understand the followings:

There are three types of stocks in a manufacturing business:

Raw Material also called as direct material (which is an integral part of finished goods)

Finished goods (the products which are manufactured for being sold)

Work-in-process (semi-finished goods).

Direct labor

Salary of those employees directly involved in converting the raw material into finished goods

Factory Overheads:

All expenses within factory except direct material and direct labor.

Indirect Material:

Any material other than raw material e.g cleaning material or oil and lubricants of machinery.

Indirect Labour:

Salary of employees within factory but outside the production department e.g security guards.

Prime cost:

Total of direct material and direct labor cost.

Conversion cost:

Total of direct labor and factory overheads is called as conversion cost.

Extra practice questions of Inventories:

Q.1 Raja makes up his annual accounts to 31st December each year. He was unable to take stock of physical inventory till 9th January 2010 on which date the physical stock at cost was valued at Rs 75,200. You are required to ascertain the value of physical stock at cost on 31s December, 2009 from the following information regarding the period from 1st January, 2010 to 9th January, 2010.

(a) Purchase of goods amounted to Rs 25, 600 of which goods worth Rs 4,700 had been received on 28.12.2009 and goods worth Rs 5,900 has been received on 12.01.2010.

(b) Sales of goods amounted to Rs 38,400 of which goods of value of a sale Rs 3,600 had not been delivered at the time of stock verification and goods of a sale value of Rs 6,000 had been delivered on 29.12.2009.

(c) Sales return amounted to Rs 1,080.

(d) A sub-total of Rs 12,000 on one of the stock sheet had been carried to the summary of stock sheets as Rs 21,000.

(e) In respect of goods costing Rs 4,000 received prior to 31st December 2009 invoice had not been received up to the date of verification of stock.

(f) The rate of gross profit was 20% on the cost price.

Q.2 Basher sells three types of products, which are used in electronic industry. He maintains periodic inventory system and uses monthly weighted average as cost basis. His accounting year ends on 30th June every year.

On 30th June, 2010, he could not carry out physical stock take due to some unavoidable reasons. However he managed to count stock on 3rd July, 2010 which was as follows:

Items	Units
Aa	2,700
Bb	4,800
Cc	1,400

Following transactions took place during first three days of July 2010:

Purchase Data:

	Rate/Unit	Total Cost (Rs.)
Aa	Rs. 15	15,000
Cc	Rs. 23	52,900

Sales data:

Aa This product has good market and is sold at a price of Rs. 28 per unit. Total invoices for the period were of Rs. 30,800.

Bb Due to technology change in last month, demand for this product has gone down. With lesser demand, this product could only be sold for Rs. 22 per unit. However it is expected that price will not fall further. During the period, total sales made were Rs. 5,500.

Cc This is the most profitable product and is sold at a price of Rs. 65 per unit. Sales for the period were Rs. 178,750.

Delivery cost for all type of products is Rs. 2 per unit.

In order to calculate weighted average cost per unit for the month of June 2010, following data is also available:

	Stock as on 1st June 2010			Purchases during June 2010		
Items	**Units**	**Rate (Rs.)**	**Total (Rs.)**	**Units**	**Rate (Rs.)**	**Total (Rs.)**
Aa	3,000	12	36,000	9.000	14	126,000
Bb	4,200	22	92,400	8,400	25	210,000
Cc	2,500	18	45,000	17,500	22	385,000

Required:

Calculate value of inventory as at 30th June 2010. **(13)**

Q.3 **Digital World (DW)** closes its accounts on 30 June each year. This year physical stock taking was delayed and carried out on 10 July 2018. The cost of physical stock on that date was determined at Rs. 1,126,000. Following further information is available:

(i) Purchase invoices received from suppliers during 1 July to 10 July 2018 amounted to Rs. 366,000. These include invoices amounting to:

- Rs. 28,000 for goods dispatched by a supplier but not received by DW till 10 July 2018.
- Rs. 20,000 for goods received on 28 June 2018.

(ii) Goods costing Rs. 44,000 were received on 8 July 2018 but the corresponding invoice was not received till 10 July 2018.

(iii) Details of credit notes from suppliers are as follows:

Credit notes date	Goods returned date	Rupees
4 July 2018	27 June 2018	23,000
9 July 2018	7 July 2018	9,000
13 July 2018	9 July 2018	14,000

(iv) Selling price of goods dispatched to customers from 1 July 2018 to 10 July 2018 amounted to Rs. 375,000. This included:

- Rs. 62,500 relating to goods invoiced but not received by customers till 10 July 2018.
- Rs. 34,000 relating to goods not invoiced till 10 July 2018.

(v) DW's stocks-in-transit from suppliers as on 30 June 2018 were amounted to Rs. 36,000. Of these, goods costing Rs. 13,100 were received on 9 July 2018 and remaining goods have not yet been received.

(vi) Goods costing Rs. 150,000 were found to be damaged and are expected to realize Rs. 110,000 after repairing at a cost of Rs. 26,000. It was ascertained that 40% of the goods were damaged in July 2018.

(vii) It was discovered that goods included in the stock valuation at Rs. 16,600 were mistakenly valued at their selling price.

(viii) DW sells goods at a mark-up of 25% on cost.

Required:
Compute the value of stock as at 30 June 2018. **(10)**

Answers:

A.1

Statement showing the value of physical stock on 31st December, 2009.

	Rs.	Rs.
Stock as on 9th January, 2010		75,200
Add: Cost of goods sold and dispatched during 1st and 9th January, 2010 (Note 1)		23,100
Less: Goods actually received during 1st and 9th January, 2010 (Note 2)		15,000
Less: Wrong carry forward (Rs. 21,000 – 12,000)		9,000
Value of stock on 31st December, 2009		**74,300**

Working Notes:

(1) Cost of Goods Sold

	Rs.
Sales	38,400
Less: Goods not dispatched	3,600
Less: Goods dispatched on 29.12.2009	6,000
	28,800
Less sale return	(1,080)
Net sales	27,720
Cost of sales (27,720 / 120 x 100)	23,100

(2) Goods Actually Received During 1st and 9th January, 2010

	Rs.
Purchases	25,600
Less: Goods received on 28.12.2009	4,700
Less: Goods received on 12.1.2009	5,900
	15,000

A.2 Value of Inventory as on June 30, 2010.

Items	Units (W-1)	Cost/Unit (W-2)	NRV/Unit (W-3)	Lower	Value
Aa	2,800	13.50	26.00	13.5	37,800
Bb	5,050	24.00	20.00	20	101,000
Cc	1,850	21.5	63.00	21.5	39,775
					178,575

(W-1) closing stock units as on 30.06.2010

	Aa	Bb	Cc
Stock on 3rd July	2,700	4,800	1,400
Less Purchases	1,000	--	2,300
	(15,000 ÷ 15)		(52,900 ÷ 23)
Add Sold	1,100	250	2,750
	(30,800 ÷ 28)	(5,500 ÷ 22)	(178,750 ÷ 65)
Stock on 30th June	2,800	5,050	1,850

(W-2) Average Cost/Unit = $\frac{\text{Opening Stock + Purchases (Amount)}}{\text{Opening Stock + Purchases (Unit)}}$

Aa = 13.50

Bb = 24.00

Cc = 21.50

(W-3) NRV / unit:

	Selling Price	Delivery Cost	NRV
Aa	28	2	26
Bb	22	2	20
Cc	65	2	63

Ans. 3

Value of stock as on 10-7-2018		1,126,000
Purchases	**(W-1)**	(352,100)
Cost of sales	**(W-2)**	300,000
Goods mistakenly included at selling price (16,600/125 x 25)		(3,320)
Stock as on 30-6-2018		1,070,580
Adjustment of NRV	**(W-3)**	(39,600)
Physical stock as on 30-6-2018 (At lower of cost and NRV)		1,030,980
Add: Stock in transit as on 30-6-2018		36,000
Total value of stock		1,066,980

W-1) Purchases:

Given (according to invoices)	366,000
(i) Goods invoiced but not received	(28,000)
(i) Goods received prior to year end	(20,000)
(ii) Goods received on 8-7-2018 but invoice not received	44,000
(v) Goods received on 9-7-2018 from in-transit(include in purchases as given figure is according to invoices)	13,100
	375,100

Less: Purchase Return:

7- July – 2018	9,000
9- July – 2018	14,000
	23,000
Net Purchase (375,100 – 23,000)	**352,100**

W-2) <u>Cost of Sales:</u>

Given Sales dispatched	375,000
As both goods in point (iv) are dispatched therefore these goods are sold and as such no need of any adjustment.	

$\frac{375,000}{125} \times 100 = 300,000$

W-3) <u>Adjustment of NRV of stock:</u>

Cost (150,000 x 60%)	90,000
NRV (84,000* x 60%)	50,400
*(110,000 – 26,000 = 84,000)	
	39,600

Test question:

Q. Salman limited (SL) closes its books on 30th June each year. Due to an administrative problems ,SL carried out the stock taking on 10th July 2016. The cost of stock as verified on 10 July 2016 was Rs. 812,500.

Details of transactions from 1 July to 10 July are given below:

I. Total sales amounted to Rs.326, 000. The goods were sold in the normal course of business at cost plus 25% except the following:
   - A sale of Rs.25.000 was made at 40% of normal selling price.
   - A sale of Rs.60,000 was made at normal selling price but the goods were slightly damaged and expenditure of Rs.15,000 was incurred on these goods to bring them saleable condition.

II. Purchases amounted to Rs 246,000. All such purchases were included in stock as on 10 july 2016.

III. Sale returns and purchase returns amounted to Rs. 11,000 and Rs.6,000 respectively.

IV. Goods with customers on sale or return basis were Rs.50,000 (at invoice value). The goods had been sent to customers on 15 june 2016. The customers have the right to return the goods within four weeks. One of the customers informed SL on 29 june 2016 that goods worth Rs.20,000 had been sold to his customer.

Required: Calculate the value of stock at lower of cost and net realizable value.

A. **The value of stock as at 30 june 2016 shall be calculated as follows:**

	Rupees	
Cost of stock on 10 July 2016		812,500
Less: Purchases from 1st July 2016 to 10th July 2016 (246,000-6,000)		(240,000)
Add: Cost of stock for [(326,000-25,000-11,000)/125x100]	232,000	
Cost of goods sold at 40% invoice price [(25,000 /0.4) x100/125]	50,000	
Goods on sale or return basis [(50,000-20,000)x100/125	24,0000	306,000
Cost of stock on 30June 2016		**878,500**
Less: NRV adjustment		
NRV (60,000 - 15,000)	45,000	
Cost (60,000 / 125 x 100)	48,000	(3,000)
Stock sold at 40% of selling price:		
Cost of the goods[(25,000 /0.4) x100/125]	50,000	
Selling price	25,000	(25,000)
Value of stock as on 30 June 2016 [lower of cost and NRV]		**850,500**

Partnership:

It is an agreement in which two or more person agree to share the profits of the business in their profit / loss sharing ratio.

Owners of partnership business are called as partners.

If sole proprietor; then any profit in his income statement is transferred to his capital e.g.

Income Statement

Net Profit		500,000

Statement of financial position

Opening Capital	800,000	
Net profit	500,000	
Drawings	(200,000)	
	1,100,000	

The above figures can be presented in the form of a ledger:

Capital Account

Drawings	200,000	b/d	800,000
		Profit	500,000
c/d	1,100,000		

In partnership, the income statement is prepared in the similar way as in sole proprietorship, however a statement after the calculation of net profit is also prepared called as "Profit Distribution Statement" or Profit Appropriation Statement e.g.

Net Profit		500,000

Profit Distribution Statement

A 3/5	300,000
B 2/5	200,000
	500,000

Partner's Capital Account

	A	B		A	B
Drawings	100,000	150,000	b/d	500,000	700,000
			Profit	300,000	200,000
c/d	700,000	750,000			

In statement of financial position of Partnership

Non current assets		--
Current assets		--
		--
Capital:		
A	700,000	
B	750,000	1,450,000
Non current liabilities		--
Current liabilities		--
		--

Sometimes instead of a single capital account for each partner, capital of each partner is accumulated in two separate ledgers for more detailed information, which are as follows:

1. Partner's Capital Account
2. Partner's Current Account

For example; lets assume first year of business if a combined capital account is prepared then:

Capital Account

	A	B		A	B
Drawings	30	20	b/d	--	--
			Cash	100	200
c/d	120	250	Profit	50	70

If prepared separately then:

Capital Account

A Column form Capital Account is prepared to record investment of partner in partnership business.

Partner's Capital Account

	A	B		A	B
			b/d	--	--
			Cash	100	200
c/d	100	200			

A Column form Current Account is prepared to record profit / loss share and drawings

Partner's Current Account

	A	B		A	B
Drawing	30	20	b/d	--	--
			Profit	50	70
c/d	20	50			

Presentation In Statement of financial position

Non current assets		--
Current assets		--
		--
Capital Account:		
A	100	
B	200	300
Current Account:		
A	20	
B	50	70
Non current liabilities		--
Current liabilities		--
		--

SHARING THE PROFITS BETWEEN THE PARTNERS

The partners are free to decide on how the profit (or loss) of the partnership is shared between the partners. The profit sharing arrangements are set out in the partnership agreement.

Example:

The WXY Partnership has three partners, W, X and Y, who share profits and losses in an agreed ratio of 3:5:8. (Profit is divided into 16 parts {3 + 5 +8} and W, X and Y receives 3 parts, 5 parts and 8 parts respectively). Profits for the year were Rs. 1,920,000.

The total profits are divided between the partners as follows:

Partner		Rs.
W	Rs. 1,920,000 x $3/_{16}$	360,000
X	Rs. 1,920,000 x $^{5}/i6$	600,000
Y	Rs. 1,920,000 x $^{8}/16$	960,000
		1,920,000

Any salary, commission, bonus or interest on capital payable to the partners of the business are not considered as expense of the business, instead these are considered as distributions from the profits. These distributions are called as notional distributions to partners.

Notional salaries for partners

A partnership agreement might recognise the different amount of work done by partners by awarding one or more of the partners with a notional salary.

A notional salary is an agreed amount awarded to the individual partner from the partnership profits.

Note that a notional salary is not a business expense in the same way that salary to employees is. It is a share of the partnership profits.

Also note that notional salary may not be paid to a partner in the same way that salary is paid to employees. A partner takes cash out of the business through drawings.

The salary is awarded to each partner from the profits, and the residual profit after deduction of notional salaries is then divided between the partners in the agreed profit-sharing ratio.

Example:

The PQR Partnership has three partners, P, Q and R.

The partnership agreement provides for the residual profit (or loss) to be shared between them in the ratio 4:3:2, after allowing a notional salary of Rs. 30,000 to R.

The profit for the year is Rs. 345,000.

Residual profits = Rs. 345,000 - Rs. 30,000 = Rs. 315,000.

Solution:

Profits are shared as follows:

			Profit share	
	Total	**P**	**Q**	**R**
	Rs.	**Rs.**	**Rs.**	**Rs.**
Notional salary	30,000			30,000
Residual profit:				
P share (Rs. 315,000 x $4/_{9}$)	140,000	140,000		
Q share (Rs. 315,000 x $^{3}/9$)	105,000		105,000	
R share (Rs. 315,000 x 2/9)	70,000			70,000
	315,000			
Profit share	345,000	140,000	105,000	100,000

The profit share of each partner is added to the balance on their individual current accounts.

Notional interest on capital

The partnership agreement might provide for the partners to obtain notional interest on the capital they have invested in the business. This is interest on the balance in their capital account.

Notional interest on long-term capital is not interest expense, because the capital in the partners' capital account is equity, not a liability of the business.

The notional interest is a share of the partnership profits. Like notional salaries, the notional interest is awarded to each partner in accordance with the partnership agreement.

The residual profit shared between the partners in the profit-sharing ratio is the profit after notional salaries and notional interest on capital are deducted.

Example:

Partnership DEF has three partners, D, E and F.

Partner D has contributed Rs. 100,000 of fixed capital, Partner E Rs. 120,000 and Partner F Rs. 60,000.

They have agreed to share profits in the following way.

- Partner D to receive a salary of Rs. 4,000 and Partner F a salary of Rs. 7,000.
- All three partners receive interest at 5% on the fixed capital contributed.
- Residual profit or loss to be shared between D, E and F in the ratio 3:5:2.

The profit of the partnership for the year is Rs. 95,000.

Solution:

The partnership profits would be shared between the partners as follows:

			Profit share		
		Total	**D**	**E**	**F**
		Rs.	**Rs.**	**Rs.**	**Rs.**
Notional salary		11,000	4,000		7,000
Notional interest at 5%		14,000	5,000	6,000	3,000
Residual profit (balance):					
D share Rs. 70,000 x	$^3/_{10}$	21,000	21,000		
E share Rs. 70,000 x	$^5/_{10}$	35,000		35,000	
F share Rs. 70,000 x	$^2/_{10}$	14,000			14,000
		70,000			
Profit share		95,000	30,000	41,000	24,000

Guaranteed minimum profit share

A partnership agreement might guarantee a minimum profit share for one (or more) of the partners.

In these cases following procedure is to be adopted:

1. The partnership profits are shared according to the partnership agreement, ignoring the minimum profit agreement.
2. If the normal sharing mechanism does not result in a partner receiving the minimum guaranteed profit the other partners must make up the shortfall out of their profit share, in their profit-sharing ratio.

Example:

The XYZ Partnership has three partners, X, Y and Z.

The partnership agreement provides for Partner X to receive a notional salary of Rs. 20,000 and residual profits or losses are shared between X, Y and Z in the ratio 2:4:6.

In addition, the agreement guarantees a minimum profit share of Rs. 32,000 to Partner Y.

The partnership profit for the current year is Rs. 80,000.

Solution:

The partnership profits would be shared between the partners as follows:

			Profit share		
		Total	**X**	**Y**	**Z**
		Rs.	**Rs.**	**Rs.**	**Rs.**
	Notional salary	20,000	20,000		
	Residual profit (balance)				
X share	Rs. 60,000 x 2/12	10,000	10,000		
Y share	Rs. 60,000 x $^4/_{12}$	20,000		20,000	
Z share	Rs. 60,000 x $^6/_{12}$	30,000			30,000
		60,000			
		80,000	30,000	20,000	30,000
Transfer to meet shortfall:					
X share	Rs. 12,000 x $^2/_8$		(3,000)	3,000	
Z share	Rs. 12,000 x $^6/_8$			9,000	(9,000)
				12,000	
Profit share		80,000	27,000	32,000	21,000

Changes in the partnership agreement on profit-sharing during the financial year

The agreement on how the partners should share the profits of the business may be changed during a financial year. When this happens, the total profits for the year should be apportioned, on a time basis, between:

- profits of the business during the time of the 'old' profit-sharing arrangements, and
- profits of the business during the time of the 'new' profit-sharing arrangements.

The profits for each time period are then shared between the partners in accordance with the agreement for that period.

Note: if nothing is mentioned then assume profits are earned evenly over the period.

Example:

The DEF Partnership has three partners, D, E and F.

In the first half of year 1, to 30 June Year 1, Partner D and Partner F each received an annual salary of Rs. 30,000. Residual profits or losses are shared between D, E and F in the ratio 3:5:2. (There is no interest on capital.)

In the second half of the year, from 1 July to 31 December, Partner D's annual salary was increased to Rs. 40,000, and the partners altered the profit-sharing ratio to 1:3:1 for D:E:F). The salary of Partner F was unchanged at Rs. 30,000 per year.

The profit for the year was Rs. 220,000 (arising evenly throughout the period)

Solution:

The annual profit would be shared as follows:

		Total	D	E	F
First six months		Rs.	Rs.	Rs.	Rs.
Notional salary (6 months)		30,000	15,000		15,000
Residual profit (balance)					
D share Rs. 80,000 x 3/10	24,000		24,000		
E share Rs. 80,000 x 5/10	40,000			40,000	
F share Rs. 80,000 x 2/10	16,000				16,000
		80,000			
		110,000	39,000	40,000	31,000
Second six months					
Notional salary (6 months)		35,000	20,000		15,000
Residual profit (balance)					
D share Rs. 75,000 x 1/5	15,000		15,000		
E share Rs. 75,000 x 3/5	45,000			45,000	
F share Rs. 75,000 x 1/5	15,000				15,000
		75,000			
		110,000	35,000	45,000	30,000
Total for the year		220,000	74,000	85,000	61,000

Profits, drawings and the partners' current accounts

For each partner, the share of the annual profit is added to the partner's current account. Any drawings during the year are deducted.

Example:

There are three partners in the ABC Partnership, A, B and C. The capital and current accounts of the partners at the beginning of the year were as follows:

Partner	Capital account (Rs.)	Current account (Rs.)
A	100,000	6,000
B	200,000	3,000
C	160,000	8,000

The profit for the year was Rs. 103,000.

Profit sharing agreement:

Partner A is given a salary of Rs. 17,000 and Partner C has a salary of Rs. 15,000

The partners pay themselves interest on capital at 5% per year (if no indication then assume of capital account only).

The residual profit or loss is shared between A, B and C in the ratio 1:3:2.

During the year, drawings by each partner were:

A	Rs. 20,000
B	Rs. 25,000
C	Rs. 40,000

Solution:

The profit share is as follows:

	Total	A	B	C
	Rs.	Rs.	Rs.	Rs.
Notional salary	32,000	17,000		15,000
Notional interest at 5%	23,000	5,000	10,000	8,000
Residual profit (balance)				
A share Rs. 48,000 x 1/6	8,000	8,000		
B share Rs. 48,000 x 3/6	24,000		24,000	
C share Rs. 48,000 x 2/6	16,000			16,000
	48,000			
Profit share	103,000	30,000	34,000	39,000

The partners' capital accounts are the same at the end of the year as at the beginning of the year. The current accounts are as follows (all amounts in Rs. 000):

Current accounts

	A	B	C		A	B	C
				Balance b/d	6	3	8
Drawings	20	25	40	Profit share	30	34	39
Balance c/d	16	12	7				
	36	37	47		36	37	47

The current accounts can also be set out in columnar form as follows:

Current accounts	Partner A	Partner B	Partner C
	Rs.	Rs.	Rs.
Beginning of the year	6,000	3,000	8,000
Add share of profit	30,000	34,000	39,000
	36,000	37,000	47,000
Deduct drawings	(20,000)	(25,000)	(40,000)
End of the year	16,000	12,000	7,000

Practice question

X, Y and Z are in partnership.

	Partner Capital account at the start of the year	Current account at the start of the year	Drawings during the year
	Rs.	Rs.	Rs.
X	1,000,000	20,000	780,000
Y	800,000	50,000	580,000
Z	600,000	10,000	350,000

The profit for the year was Rs. 1,944,000.

Profits are shared as follows:

- The partners pay themselves interest on capital at 6% per year.
- The residual profit or loss is shared between X, Y and Z in the ratio 4: 3: 2.

Required:

Show how the profits should be shared between the partners, and show their capital and current accounts as at the end of the year.

Solution:

The profit share is as follows:

	Total	X	Y	Z
	Rs. (000)	Rs.	Rs.	Rs.
Notional interest				
Fixed capital		1,000,000	800,000	600,000
Interest @ (6%)	144,000	60,000	48,000	36,000
Residual profit (balance)				
X share Rs. 1.8m x 4/9	800,000	800,000		
Y share Rs. 1.8m x 3/9	600,000		600,000	
Z share Rs. 1.8m x 2/9	400,000			400,000
	1,800,000			
Profit share	1,944,000	860,000	648,000	436,000

Current accounts (Rs. 000)

	X	Y	Z		X	Y	Z
				Balance b/d	20	50	10
Drawings	780	580	350	Profit share	860	648	436
Balance c/d	100	118	96				
	880	698	446		880	698	446

The current accounts can also be set out in coumnar form as follows:

Current accounts	Partner X Rs.	Partner Y Rs.	Partner Z Rs.
Beginning of the year	20,000	50,000	10,000
Add share of profit	860,000	648,000	436,000
	880,000	698,000	446,000
Deduct drawings	(780,000)	(580,000)	(350,000)
End of the year	100,000	118,000	96,000

Adjustment of Goodwill

Goodwill
It is the good reputation of the business. It is an intangible asset.

Example:
Lets assume on 1st July, 1985 A & B started a partnership. Suppose on 1st January, 2015 they decided to admit C as a new partner. In this case, goodwill that is created by A & B should only benefit A & B before admission of C. If C is to get benefit of this goodwill then C has to pay amount of his share of goodwill to A & B. Therefore C will contribute cash for his capital as well as for his share of goodwill.

C contributed 1,500,000 which includes his share of goodwill
Goodwill of the business is 600,000

Profit Sharing Ratio

	Old	New
A	2/4	3/9
B	2/4	3/9
C		3/9

Share of C in goodwill of business is = $600{,}000 \times \frac{3}{9} = 200{,}000$

Entry should be:

C's Capital Account	200,000	
A's Capital Account		100,000
B's Capital Account		100,000

However in exam situation **ACCOUNTING ENTRIES OF GOODWILL are as follows:**

(i) **Raise the goodwill (in old profit sharing ratio)**

Goodwill	600,000	
A's Capital Account		300,000
B's Capital Account		300,000

(ii) **Eliminate the goodwill (in new profit sharing ratio)**

A's Capital Account	200,000	
B's Capital Account	200,000	
C's Capital Account	200,000	
Goodwill		600,000

Capital Account

	A	B	C		A	B	C
Goodwill	200,000	200,000	200,000	b/d (assumed)	700,000	800,000	
				Cash			1,500,000
				Goodwill	300,000	300,000	
c/d	800,000	900,000	1,300,000				

CONCLUSION
The net effect of these entries is that 200,000 is deducted (debited) from C's Capital Account and added (credited) to A & B's capital Accounts.

How to Calculate Goodwill of Partnership:

Goodwill
The value of a business is usually more than the net assets of the business because it reflects the trading potential that the business, i.e. its ability to generate profits in the future. All successful businesses have goodwill, which means that buyers will be prepared to pay more to acquire the business than the value of its net assets.

Illustration: Goodwill	
Value of the firm (what another party would pay for it)	X
Assets less liabilities of the firm (net assets)	(X)
Goodwill	X

The assets and liabilities of the firm should be restated to their fair value in order to measure goodwill. Fair value means the market value of an asset, i.e. how much it is worth.

Example:
A firm has net assets of Rs. 1,000,000
One of the assets held by the firm had a fair value of Rs.200, 000 in excess of its carrying amount.
The firm is valued at Rs. 1,800,000.

Goodwill calculation:	**With revaluation of the asset**
Value of the firm	1,800,000
Assets less liabilities as per the accounts	
Assets less liabilities (at fair value) (1,000,000 + 200,000)	(1,200,000)
Goodwill	600,000
Amount shared by the partners:	
Goodwill	600,000
Revaluation gain	200,000
Amount shared by the partners in the profit sharing ratio:	800,000

In the above example the figure of Rs. 600,000 for goodwill is the value that most closely fits the guidance given in IFRS (accounting standards).

Question bank

Q.1 DEE AND EEE

Dee and Eee are in partnership. The profit sharing ratio between the partners is 3:2. Partners are allowed Interest on capital at the rate of 5% per annum. Eee is entitled to a salary of Rs.6000 per annum. The following balances were extracted from the books on 31st July 2015:

	Rs.
Buildings (cost)	75,000
Vans (cost)	40,000
Equipment (cost)	25,000
Provisions for depreciation	
Buildings	18,000
Vans	10,000
Equipment	15,000
Trade payables	55,900
Trade receivables	39,500
Bank	31,400
Purchases	148,300
Provision for doubtful debts	1900
8% Bank loan (repayable 31 March 2016)	40,000
Capital accounts:	
Dee	40,000
Eee	40,000
	Rs.
Current accounts at 1 August 2014:	
Dee	500 Cr
Eee	900 Cr
Drawings:	
Dee	12,000
Eee	12,000
Revenue	256,000
Returns inwards	5,200
Inventory at 1 August 2014	25,800
Van expenses	11,000
Salaries	28,950
Bank interest paid	1,600
Rent income	3,500
Rent expense	12,000
Heat and light	7,600
Other operating expenses	6,350

Additional information

The following information was available at 31 July 2015:

(1) Inventory was valued at Rs.34,100.

(2) Rent receivable of Rs.1500 was outstanding.

(3) Depreciation is to be charged on all non-current assets owned at the end of the year as follows:
- (i) Straight line method to be used for buildings which are held on a 25 year lease.
- (ii) Vans at the rate of 30 % per annum using the diminishing (reducing) balance method
- (iii) Equipment at the rate of 10% per annum using the straight line method.

(4) On 31st January 2015 the partners had agreed to allow Eee to increase his capital by Rs.20,000. Eee paid a cheque into the partnership bank account on that date.

(5) Trade receivables of Rs.4,500 are irrecoverable. The provision for doubtful debts is to be maintained at 4 %

(6) Other operating expenses prepaid Rs.1,800.

Required:

(a) Prepare the Statement of comprehensive income of Dee and Eee for the year ended 31st July 2015

(b) Prepare the appropriation account of Dee and Eee for the year ended 31st July 2015.

(c) Prepare the current accounts of Dee and Eee.

(d) Prepare the Statement of financial position of Dee and Eee at 31st July 2015.

Q.2 HAMZA AND DANIYAL

Hamza and Daniyal are in partnership. As per the partnership deed they share profits and losses equally. Partners are allowed Interest on capital at the rate of 3% per annum. Interest on drawings is charged at the rate of 4% per annum. The following balances were extracted from the books on 30th April 2015:

	Rs.
Premises (cost)	120,000
Delivery vehicles (cost)	60,000
Office fixtures (cost)	30,000
Provisions for depreciation	
Premises	7,200
Delivery vehicles	20,000
Office Fixtures	22,000
Trade payables	7,900
Bank Overdraft	92,600
Purchases	81,250
Trade Receivables	18,750
Provision for doubtful debts	500
Capital accounts:	
Hamza	50,000
Daniyal	30,000
Current accounts at 1 May 2014:	
Hamza	3,250
Daniyal	1,850
Drawings:	
Hamza	6,000
Daniyal	6,000
Revenue	190,000
Returns inwards	8,600
Inventory at 1 May 2014	15,600
Advertising expenses	11,000
Wages and Salaries	31,450
Delivery vehicle expenses	14,900
Heat and light	9,750
Other operating expenses	12,000

Additional information

The following information was available at 30 April 2015:

(1) Inventory was valued at Rs.13,650.

(2) Heat and light Rs.150 was accrued.

(3) Depreciation is to be charged on all non-current assets owned at the end of the year as follows:
  (i) Premises at the rate of 2% on cost per annum
  (ii) Delivery vehicles at the rate of 20 % per annum using the diminishing (reducing) balance method
  (iii) Office Fixtures at the rate of 10% per annum using the straight line method.

(4) Advertising expenses prepaid were Rs.800

(5) The provision for doubtful debts is to be maintained at 4 %

(6) A cheque payment of Rs.550 made to a credit supplier on 15 April, had not been recorded in the books.

Required:

(a) Prepare the Statement of comprehensive income of Hamza and Daniyal for the year ended 30th April 2015

(b) Prepare the appropriation account of Hamza and Daniyal for the year ended 30th April 2015.

(c) Prepare the current accounts of Hamza and Daniyal.

(d) Prepare the Statement of financial position of the Partnership at 30th April 2015.

Q.3 FAIZ, JALIB AND IQBAL

Faiz, Jalib and Iqbal are partners sharing profits and losses in the ratio 2:2:1 in a retail business. Interest on capital is allowed at the rate of 4% per annum whereas interest on drawings is charged at the rate of 5% per annum on the balances at 30 April 2015.

The following balances were extracted from the books on 30 April 2015:

	Rs.
Building	44,750
Motor vehicles (cost)	16,000
Fixtures and fittings (cost)	30,000
Provisions for depreciation	
Motor vehicles	3,200
Fixtures and fittings	17,500
Trade payables	54,700
Trade receivables	45,000
Provision for doubtful debts	1,500
Bank	7,560 Dr
Purchases	111,200
Revenue	209,500
Returns outwards	4,750
Inventory at 1 May 2014	30,650
Salaries expense	42,100
Heat and light	3,890
General expenses	16,750
Discount received	5,300
Marketing and communication expenses	12,050
Rent	7,500
Capital accounts	
Faiz	40,000
Jalib	35,000
Iqbal	25,000
Current accounts	
Faiz	2,500 Cr
Jalib	1,500 Cr
Iqbal	1,000 Dr
Drawings	
Faiz	10,000
Jalib	10,000
Iqbal	12,000

Additional information

The following information was available at 30 April 2015:

(1) Inventory was valued at Rs.28,100.

(2) The provision for doubtful debts is to be maintained at 5% of trade receivables

(3) Depreciation is to be charged as follows:
  - (i) Motor vehicles at the rate of 20% per annum using the diminishing (reducing) balance method.
  - (ii) Fixtures and fittings at the rate of 10% per annum on cost, using the straight line method

(4) General expenses, Rs.4,200, were prepaid.

(5) Rent Rs.2,500 was accrued.

(6) On 30 April 2015 the partners agreed to allow Iqbal to reduce his capital balance by Rs.10,000. The sum was transferred to his current account on that date. The transfer took place after calculating the interest on capital for the year.

Required:

(a) Prepare the Statement of comprehensive income of Faiz, Jalib and Iqbal for the year ended 30 April 2015

(b) Prepare the appropriation account of Faiz, Jalib and Iqbal for the year ended 30 April 2015.

(c) Prepare the current accounts of Faiz, Jalib and Iqbal.

(d) Prepare the Statement of financial position of Faiz, Jalib and Iqbal at 30 April 2015.

Answers:

A.1 DEE AND EEE

(a) Statement of comprehensive income for the year ended 31 July 2015

	Notes	'000'
Sales (256,000 – 5,200)		250,800
Cost of Sales:	N-1	(140,000)
Gross Profit		110,800
Other Income (Rent income 3,500+1,500)		5,000
Admin and selling Expenses:	N-2	(82,600)
Finance cost (loan interest) W-1		(3,200)
Net Profit		**30,000**

(b) Dee and Eee
Appropriation Account for the year ended 31 July 2015

	Total	Dee	Eee
Interest on capital	4,500	2,000 (40,000 x 5%)	2,500 [(40,000 x 5% x 6/12)+(60,000 x 5% x 6/12)
Salary	6,000		6,000
Profit share	19,500	11,700 (3/5)	7,800 (2/5)
(30,000-4,500-6,000)			
	30,000	**13,700**	**16,300**

(c)

Current accounts

	Dee	Eee		Dee	Eee
	Rs.	Rs.		Rs.	Rs.
			Balance b/d	500	900
Drawings	12,000	12,000			
Balance c/d	2,200	5,200	Share of profit	13,700	16,300

(d) Dee and Eee
Statement of financial position at 31 July 2015

	Rs.	Rs.	Rs.
Non-current assets	Cost	Accumulated Depreciation	NBV
Buildings	75,,000	21,000	54,000
Van	40,000	19,000	21,000
Equipment	25,000	17,500	7,500
	140,000	57,500	82,500
Current assets			
Inventory		34,100	
Trade receivables (39,500 - 4,500)	35,000		
Less: Provision for doubtful debts	(1,400)		
		33,600	
Rent receivable		1,500	
Prepaid operating expenses		1,800	

Bank (31,400 + 20,000)	51,400	
		122,400
Total Assets		204,900
Equity and liabilities		
Capital accounts:		
Dee	40,000	
Eee (40,000+20,000)	60,000	
		100,000
Current accounts:		
Dee	2,200	
Eee	5,200	
		7,400
		107,400
Current liabilities		
Trade payables	55,900	
8% Bank loan	40,000	
Interest payable	1,600	
		97,500
		204,900

Notes:

N-1: Cost of sales

Opening Stock	25,800
Add Purchases (33,436 – 120 - 180)	148,300
Less Closing Stock	(34,100)
Total	**140,000**

N-2: Admin and selling expenses

Rent	12,000
Salaries	28,950
Heat and light	7,600
Other operating expenses (6,350 – 1,800)	4,550
Van expenses	11,000
Depreciation (W-2)	14,500
Bad debts (4,500 - 500)	4000
Total	**(82,600)**

W-1 Loan Interest

*40,000 x 8% = 3,200

1,600 paid

1,600 payable

W-2 **Depreciation**

Buildings (75,000/25)	3,000
Van (40,000 -10,000) x 30%	9,000
Equipment (25,000 x 10%)	2,500
Total	**14,500**

A.2 HAMZA AND DANIYAL

(a) Statement of comprehensive income for the year ended 30 April 2015

	Notes	'000'
Sales (190,000 – 8,600)		181,400
Cost of Sales:	N-1	(83,200)
Gross Profit		98,200
Admin and selling Expenses	N-2	(92,100)
Net Profit		**6,100**

(b) Hamza and Daniyal
Appropriation Account for the year ended 30 April 2015

	Total	H	D
Interest on drawings	(480)	(240)	(240)
Interest on capital	2,400	1,500	900
Profit share	4,180	2,090	2,090
(6,100 – 2,400 +480)			
	6,100	**3,350**	**2,750**

(c) Current accounts

	Hamza	Daniyal		Hamza	Daniyal
	Rs.	Rs.		Rs.	Rs.
			Balance b/d	3,250	1,850
Drawings	6,000	6,000			
			Share of profit	3,350	2,750
Balance c/d	600		Balance c/d		1,400

(d) Hamza and Daniyal
Statement of financial position at 30 April 2015

	Rs.	Rs.	Rs.
Non-current assets		**Accumulated**	
	Cost	**Depreciation**	**NBV**
Premises	120,,000	9,600	110,400
Delivery vehicles	60,000	28,000	32,000
Office fixtures	30,000	25,000	5,000
	210,000	62,600	147,400
Current assets			
Inventory		13,650	
Trade receivables	18,750		
Less: Provision for doubtful debts	(750)	18,000	
Prepaid advertisement		800	
			32,450
Total Assets			179,850
Equity and liabilities			
Capital accounts:			
Hamza		50,000	
Daniya		30,000	
			80,000
Current accounts:			
Hamza		600	
Daniyal		(1,400)	
			(800)
			79,200
Current liabilities			
Trade payables (7,900 – 550)		7,350	
Heating and light payable		150	
Bank Overdraft (92,600 + 550)		93,150	
			100,065
			179,850

Notes:

N-1: Cost of sales

Opening Stock	15,600
Add Purchases (33,436 – 120 - 180)	81,250
Less Closing Stock	(13,650)
Total	**83,200**

N-2: Admin and selling expenses

Other operating expenses	12,000
Advertising (11,000 – 800)	10,200
Wages and salaries	31,450
Delivery vehicle expenses	14,900
Heat and light (9,750 + 150)	9,900
Bad debts	250
Depreciation (W-1)	13,400
Total	**(92,100)**

W-1 Provisions for depreciation-

Premises (120,000 x 2%)	2,400
Delivery vehicles (60,000–20,000)x 20%	8,000
Office fixtures (30,000 x 10%)	3,000
Total	**13,400**

A.3 FAIZ, JALIB AND IQBAL

(a) Statement of comprehensive income for the year ended 30 April 2015

	Notes	'000'
Sales		209,500
Cost of Sales:	N-1	(109,000)
Gross Profit		100,500
Other Income (discount received)		5,300
Admin and selling Expenses:	N-2	(86,900)
Net Profit		**18,900**

(b) Faiz, Jalib and Iqbal
Appropriation Account for the year ended 30 April 2015

	Total	Faiz	Jalib	Iqbal
Interest on capital	4,000	1,600	1,400	1,000
Interest on drawings	(1,600)	(500)	(500)	(600)
Profit share	16,500	6,600	6,600	3,300
(18,900+1600-4,000)				
	18,900	**7,700**	**7,500**	**3,700**

c) Current accounts

	Faiz	Jalib	Iqbal		Faiz	Jalib	Iqbal
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
Balance b/d			1,000	Balance b/d	2,500	1,500	
				Capital transfer			10,000
Drawings	10,000	10,000	12,000				
Balance c/d	200		700	Share of profit	7,700	7,500	3,700
				Balance c/d		1,000	

(d) Faiz, Jalib and Iqbal
Statement of financial position at 30 April 2015

	Rs.	Rs.	Rs.
Non-current assets	Cost	Accumulated Depreciation	NBV
Buildings			44,750
Motor vehicles	16,000	5,760	10,240
Fixtures	30,000	20,500	9,500
	46,000	26,260	64,490
Current assets			
Inventory		28,100	
Trade receivables	45,000		
Less: Provision for doubtful debts	(2,250)		
		42,750	
Prepaid general expenses		4,200	
Bank		7,560	
			82,610
Total Assets			147,100
Equity and liabilities			
Capital accounts:			
Faiz		40,000	
Jalib		35,000	
Iqbal (25,000 – 10,000)		15,000	
			90,000
Current accounts:			
Faiz		200	
Jalib		(1,000)	
Iqbal		700	
			(100)
			89,900
Current liabilities			
Trade payables		54,700	
Rent payable		2,500	
			57,200
			147,100

Notes:

N-1: Cost of sales

Opening Stock	30,650
Add Purchases (111,200-4,750)	106,450
Less Closing Stock	(28,100)
Total	**109,000**

N-2: Admin and selling expenses

Rent (7,500 + 2,500)	10,000
Salaries expense	42,100
Heat and light	3,890
General expenses (16,750 – 4,200)	12,550
Marketing and communication expense	12,050
Depreciation (W-1)	5,560
Bad debts	750
Total	**(86,900)**

W-1 Depreciation

Motor vehicles (16,000 -3,200) x 20%		2,560
Fixtures (30,000 x 10%)		3,000
	Total	**5,560**

Practice question

Q. A and U

A and U are in partnership sharing profits and losses in the ratio 2:3. Partners are allowed Interest on capital at the rate of 7% per annum. A is entitled to a salary of Rs. 20,000 per annum. The following balances were extracted from the books on 30th April 2013:

	Rs.
Capital accounts	
A	120,000
U	100,000
Current accounts	
A	500 Cr
U	2,700 Dr
Drawings	
A	20,000
U	14,000
6% Loan repayable 31 December 2021	80,000
Trade receivables	58,000
Provision for doubtful debts	2,500
Inventory at 1 May 2012	53,750
Trade payables	20,340
Bank deposit	5,000
Bank	9,150 Cr
Land and Buildings (cost)	200,000
Equipment (cost)	48,000
Fixtures and Fittings (cost)	35,000
Provisions for Depreciation:	
Land and Buildings	14,000
Equipment	12,000
Fixtures and fittings	26,000
Revenue	380,000
Purchases	170,000
Returns from customers	11,100
Returns to suppliers	8,900
Carriage outwards	6,290
Wages and salaries	69,530
Loan interest paid	3,600
Postage expenses	8,900
Marketing expenses	17,800
Administration expenses	25,720
Building works	24,000

Additional information

1. Inventory was valued at 30th April, 2013, Rs.48,500.
2. At 30th April, 2013, Postage expenses, Rs.890, were prepaid and marketing expenses, Rs.4,000 were accrued.
3. Depreciation is to be charged on all non-current assets owned at the end of the year as follows:
   (i) Buildings at the rate of 2% per annum on cost. No depreciation is charged on land. On 1st of April 2012 the land was valued at Rs.75,000

(ii) Equipment at the rate of 20% per annum using the diminishing (reducing) balance method.

(iii) Fixtures and fittings at the rate of 10% using the straight line method.

4. The salary paid to A had been posted to the wages and salaries account.
5. Trade receivables contain a debt of Rs.3000 which is considered irrecoverable.
6. Building works consisted of an extension to the building, Rs.20,000 and repairs to the existing air conditioning, Rs.4,000.
7. The provision for doubtful debts is to be maintained at 6% of remaining trade receivables.

Required:

a Prepare the Statement of comprehensive income of A and U for the year ended 30th April 2013

b Prepare the appropriation account of A and U for the year ended 30th April 2013.

c Prepare the current accounts of A and U.

d Prepare a statement of financial position of A and U as on 30.04.2013

Solution

(a) Income statement for the year ended 30 April 2013

Revenue		380,000
Less Returns		(11,100)
		368,900
Inventory at 1 May 2012	53,750	
Purchases	170,000	
Less Returns	(8,900)	
Less Inventory at 30 April 2013	(48,500)	
		(166,350)
Gross profit		202,550
Less Expenses		
Carriage outwards	6,290	
Administration expenses	25,720	
Marketing (17,800+4,000)	21,800	
Wages and salaries (69,530 – 20,000)	49,530	
Postage expenses (8,900 – 890)	8,010	
Loan interest (3,600+1,200*)	4,800	
Building works/Repairs to air cond	4,000	
Bad debt	3,000	
Increase in provision for doubtful debts	800	
Provisions for depreciation-		
Buildings (125,000 + 20,000)x 2%	2,900	
Equipment (48,000 – 12,000) x 20%	7,200	
Fixtures and fittings (35,000 x 10%)	3,500	
		(137,550)
Profit for the year		65,000

*80,000 x 6% = 4,800
Less: paid = 3,600
Payable = 1,200

(b) A and U

Appropriation Account for the year ended 30 April 2013

	Total	A	U
Interest on capital	15,400	8,400	7,000
Salary	20,000	20,000	
Profit share	29,600	11,840	17,760
(65,000 – 15,400 -20,000)			
	65,000	**40,240**	**24,760**

(c) Current accounts

	A Rs.	U Rs.		A Rs.	U Rs.
Balance b/d		2,700	Balance b/d	500	
Drawings	20,000	14,000			
Drawings-Salary	20,000				
Balance c/d	740	8,060	Share of profit	40,240	24,760
	40,740	24,760		40,740	24,760

(d) A and U - Statement of financial position at 30 April 2013

	Rs. Cost	Rs. Accumulated Depreciation	Rs. NBV
Non-current assets			
Land and Buildings	220,,000	16,900	203,100
Equipment	48,000	19,200	28,800
Fixtures and fittings	35,000	29,500	5,500
	303,000	65,600	237,400
Current assets			
Inventory		48,500	
Trade receivables (58,000 – 3,000)	55,000		
Less: Provision for doubtful debts	(3,300)		
		51,700	
Prepaid postage expenses		890	
Bank deposit		5,000	
			106,090
Total Assets			343,490

Equity and liabilities		
Capital accounts:		
A	120,000	
U	100,000	
	220,000	
Current accounts:		
A	740	
U	8,060	
		8,800
		228,800
Non-current liabilities		
6% Loan		80,000
Current liabilities		
Trade payables	20,340	
Marketing expenses payable	4,000	
Interest payable	1,200	
Bank Overdraft	9,150	
		34,690
		343,490

Discussion of markup and margin commission on profit after commission and before commission.

Question 4

Galaxy Traders is a partnership with three partners, Z, A and B. The following information is available in respect of the year ended 31 December 2016:

(i) Partners' balances:

	Z	A	B
	---------- Rs. In '000 ----------		
Opening balance: Capital accounts	12,000	8,000	10,000
Current accounts	500	700	600
Drawing by the partners during the year	4,500	5,000	4,000

(ii) Profit sharing arrangement:

- Z, who is working as managing partner, is entitled to receive commission at 5% on profit after commission.
- A and B are entitled to a monthly salary of Rs. 50,000 each.
- All partners are entitled to receive interest at 8% on their opening capital balances.
- The remaining profit is shared by the partners in the ratio of their opening capital account balances. However, the agreement guarantees a minimum annual profit share of Rs. 5 million to A and Rs. 3 million to B. Further, 20% of the profit allocated to each partner is to be retained for business expansion and transferred to the partners' capital accounts.

(iii) The net profit for the year ended 31 December 2016 was Rs. 34 million. However, the partners have noted that no provision for doubtful debts is being maintained. In this respect, ageing analysis of the closing account receivable balances was carried out and it has been agreed that prior to appropriation of profit, provision for doubtful debts is to be accounted for as under:

		Period outstanding			Total
		Less than 3 months	3 to 12 months	More than 1 year	
Customers' balances under dispute	(Rs. In '000)	-	10,000	6,000	16,000
Agreed prevision % on disputed balances		-	50%	100%	
Other outstanding balances	(Rs. In '000)	50,000	35,000	15,000	100,000
Agreed general provision %		2%	8%	10%	
	(Rs. In '000)				116,000

Required:

Compute the partners' current and capital account balances as on 31 December 2016. **(15)**

Question:5

Alpha, Beta & Gamma are three partners in a partnership firm. The following information is available in respect of the year ended 31 December 2016:

The net profit for the year ended 31 Dec. 2016 was Rs. 44 million. However depreciation and interest for the year is yet to be charged.

(a) Partners' balances:

	Alpha	Beta	Gamma
	---------- Rs. in '000' ----------		
Opening balance: Capital accounts	25,000	10,000	15,000
Current accounts	1,000	1,500	900
Drawings by the partners during the year	5,000	5,500	4,500

(b)

	Rs. '000'	
Fixed Assets	**Cost**	**Accumulated Depreciation**
Building	3,200	608
Plant & Machinery	2,500	384
Furniture	1,500	280

Depreciation rates for the building and furniture is 10% and for plant and machinery is 8%. Method of depreciation is diminishing balance method.

Bank loan of 2,000,000 was taken on 1-9-2016 @ 12% per annum.

(c) **Profit sharing arrangement:**

Alpha, who is working as managing partner, is entitled to receive commission at 7% on profit after commission. Beta and Gamma are entitled to a monthly salary of Rs. 50,000 each. All partners are entitled to receive interest at 10% on their opening capital balances. The remaining profit is shared by the partners in the ratio of their opening capital account balances. However, the agreement guarantees a minimum annual profit share of Rs. 7 million to Alpha and Rs. 5 million to Beta. Further, 25% of the profit allocated to each partner is to be retained for business expansion and transferred to the partners' capital accounts.

Required:

Compute the partner's current and capital account balances as on 31 December, 2016

Discussion of Goodwill

Valuing goodwill

The method of arriving at total value of the firm might be based on a formula set out in the partnership agreement.

Example:

The XYZ Partnership has an agreed method to value the goodwill of the firm for purposes of change in partnership as 10x the average annual profit for the last three years for which financial statements are available. Profit for the last three years has been as follows:

Year 3	Rs. 100,000
Year 2	Rs. 90,000
Year 1	Rs. 80,000

The average annual profit is: 100,000 + 90,000 + 80,000 /3 = Rs. 90,000

The goodwill be: 10 x Rs. 90,000 = Rs. 900,000

Alternatively, a partnership agreement might specify a method for valuing goodwill directly. One such method is measuring goodwill as a multiple of average annual profits or a multiple of its average annual 'excess' profits.

Example:

The XYZ Partnership values its goodwill as two times the average of the annual profits in excess of Rs. 60,000 each year for the last three years.

Profit for the last three years has been as follows:

Year 3	Rs. 100,000
Year 2	Rs. 90,000
Year 1	Rs. 80,000

The profits in excess of Rs. 60,000 have been:

Rs. 40,000 + Rs. 30,000 + Rs. 20,000 = Rs. 90,000

The average annual excess profit is: Rs.90,000 / 3 = Rs. 30,000

The valuation of goodwill is: 2 x Rs. 30,000 = Rs. 60,000

Q.6 Chagi Prides has three partners B, P and S. Following information pertains to the year ended 31 December 2016:

	B	P	S
	------- Rs. in '000 -------		
Opening balances: Capital accounts	21,000	13,500	9,000
Current accounts	2,000	(2,000)	2,300
Drawings for the year (other than salary)	5,500	3,800	3,500

As per the partnership agreement applicable up to 31 May 2016:

(i) B, P and S share profit in the ratio of 3:2:1 respectively.
(ii) Interest on partners' capital is allowed at 8% per annum.

The partnership agreement was revised with effect from 1 June 2016 as follows:

- There will be no change in B's share of profit whereas P and S will have equal share.
- Interest on partners' capital will be increased to 12% per annum.
- S will be entitled to a monthly salary of Rs. 135,000.
- Goodwill will be recognized at two years purchase of average net profit of the last three completed years.

Profits for the relevant years are as under:

2013	2014	2015	Jan-May 2016	Jun-Dec 2016
------------------------------		Rs. in '000	------------------------------	
11,000	9,300	13,000	6,100	8,000

S has not withdrawn salaries for the months of November and December 2016 due to weak liquidity position of the firm.

Required:
For the year ended 31 December 2016:
(a) show how the partnership profits should be shared among the partners. **(11)**
(b) prepare partners' current accounts. **(04)**

Q.7 Famous Garments (FG) has three partners M, A and J sharing profits and losses in the ratio of 2:3:1. Following information pertains to the year ended 31 December 2017:

		M	A	J
		--------	Rs. in '000	--------
Opening balances:	Capital account	3,000	5,000	4,000
	Current account	800	(200)	600
Drawings for the year (other than salaries)		4,500	6,250	5,000

As per the partnership agreement:
M and J are entitled for a monthly salary of Rs. 45,000 each;
Interest on the partners' opening capital balances is allowed at 10% per annum; and
J is entitled to a minimum profit share of Rs. 3,500,000 per annum. Any shortfall is to be shared by M and A in their profit sharing ratio

FG's draft statement of profit or loss for the year ended 31 December 2017 shows net profit of Rs. 15,000,000 after incorporating bonus to fashion designers (5% of the profit after the bonus). On review of the financial statements, the partners have identified the following errors:

(i) M and J withdrew cash against their salaries for nine and ten months respectively. Salaries withdrawn by M and J were charged to salary expense.

(ii) On 1 January 2017, partners had agreed to sell a vehicle to M at book value. The disposal has not been recorded in the books.

The vehicle was purchased on 1 October 2015 at a cost of Rs. 1,200,000 and its book value as at 31 December 2017 is Rs. 660,000. FG uses straight line method to depreciate its vehicles.

(iii) A sales invoice for Rs. 400,000 was wrongly raised against goods costing Rs. 300,000 withdrawn by A and the amount is included in trade receivables.

Required:
For the year ended 31 December 2017:
(i) Compute corrected profit and the share of each partner in the profit. **(10)**
(ii) Prepare partners' current accounts. **(05)**

Q.8 Toby Apparels has three partners A, B and K. The net profit for year ended 30 June 2018 was Rs. 12.5 million which arose evenly throughout the year. Following further information pertains to the year ended 30 June 2018:

	A	B	K
	------- Rs. in '000 -------		
Opening balances: Capital accounts	5,000	13,000	7,000
Current accounts	(500)	100	2,800
Drawings for the year	3,100	4,300	3,400

As per the partnership agreement valid up to 30 September 2017:

(i) A, B and K shared profit in the ratio of 3:7:5 respectively.

(ii) All partners were entitled to receive interest on capital at 12% per annum.

(iii) A was entitled to monthly salary of Rs. 50,000.

(iv) B was entitled to commission of 4% of net profit.

On 1 October 2017, all partners agreed to revise the partnership agreement. Before revision, they agreed to make the following changes in the capital accounts:

- Goodwill was recognized at 2 times the average annual profit for the last 3 completed years in excess of Rs. 6 million. The profits for the firm were as follows:

30 June 2017	30 June 2016	30 June 2015
---------------- Rs. in '000 ----------------		
10,500	9,500	9,250

- Partner A made additional investment of Rs. 3.5 million while B withdrew Rs. 4.5 million of his capital. Partner K transferred Rs. 2.5 million from his current account to capital account.

As per the revised partnership agreement effective from 1 October 2017:

1. All partners will be entitled to interest on capital at 9% per annum.
2. A will be entitled to monthly salary of Rs. 60,000 while B and K will be entitled to monthly salary of Rs. 75,000 each.
3. A, B and K will share profit in the ratio of 2:4:3 respectively.

Required:

For the year ended 30 June 2018:

(a) show how the partnership profits would be shared among the partners. (09)

(b) prepare partners' current and capital accounts. (06)

Q.9 Bannu Traders has three partners A, B and C. The net profit for the year ended 31 December 2018 was Rs. 5.8 million. Following further information pertains to the year ended 31 December 2018:

	A	B	C
	------- Rs. in '000 -------		
Opening balances: Capital accounts	9,000	6,000	3,000
Current accounts	800	1,700	(600)
Drawings during the year	2,500	750	1,000

As per the partnership agreement:

(i) interest on the partners' opening capital is allowed at 10% per annum if the partner has positive opening current account balance.

(ii) A and C are entitled to monthly salaries of Rs. 100,000 and Rs. 120,000 respectively for the months in which they attend the partnership office. C did not attend the office for 3 months during 2018.

(iii) interest is charged at 8% per annum on drawing balances as at 31 December in excess of salary entitlement.

(iv) B is entitled to a bonus of 10% of profit after partners' salaries.

(v) residual profit is to be shared as follows:

Up to Rs. 1.2 million equally; and
Balance would be shared by A, B and C in the ratio of 3:3:2 respectively.

However, B is entitled to a minimum annual profit share of 30% of his capital balance. Any shortfall is to be contributed by A and C in the ratio of their capital balances.

Required:

For the year ended 31 December 2018:

(a) show how the partnership profits would be shared among the partners. (09)

(b) prepare partners' current accounts. (03)

Answer 4

Current Account **Rs. In '000**

	Z	A	B		Z	A	B
Drawing	4,500	5,000	4,000	b/d	500	700	600
				Profit (W-1)	5,586	4,000	4,574
c/d	1,586		1,174	c/d		300	

Capital Account

	Z	A	B		Z	A	B
				b/d	12,000	8,000	10,000
				Profit (W-1)	1,397	1,000	1,143
c/d	13,397	9,000	11,143				

Workings:

(W 1) Profit Distribution Statement **Rs. In '000**

	Total	Z	A	B
Commission [17,700 (working) × 5/105]	843	843		
Salaries	1,200		600	600
Interest on Capital	2,400	960	640	800
		(12,000×8%)	(8,000×8%)	(10,000×8%)
Residual Profit [17,700 – 843 – 1,200 – 2,400]				
13,257				
Z [13,257 × 12/30]	5,303	5,303		
A [13,257 × 8/30]	3,535		3,535	
B [13,257 × 10/30]	4,419			4,419
	13,257			
Total share before minimum share adjustment		**7,106**	**4,775**	**5,819***
Shortfall of A:				
[5,000 – 4,775] = 225 x 12/22 & 10/22	--	(123)	225	(102)
Final share		**6,983**	**5,000**	**5,717**
20% Profit share that is allocated to be transferred to capital account		(1,397)	(1,000)	(1,143)
	17,700	5,586	4,000	4,574

*B's share is already more than 3 million.

(W-2) Calculation of Adjusted Profit for the year:

Profit before adjustment =	34,000
* Bad debts (working)	(16,300)
Adjusted profit	17,700

*** Provision**

		b/d	--
		Bad debt (bal)	16,300
c/d	16,300		

Specific Allowance:

10,000 × 50% =	5,000
6,000 × 100% =	6,000
	11,000

General Allowance:

50,000 × 2% =	1,000
35,000 × 8% =	2,800
15,000 × 10% =	1,500
	5,300
Total Allowance =	16,300

Solution:5

Capital A/c **000**

	Alpha	Beta	Gamma		Alpha	Beta	Gamma
				b/d	25,000	10,000	15,000
				Profit (W 1)	5,626	2,117	3,100
c/d	30,625	12,117	18,100				

Current A/c **000**

	Alpha	Beta	Gamma		Alpha	Beta	Gamma
Drawing	5,000	5,500	4,500	b/d	1,000	1,500	900
c/d	12,879	2,350	5,700	Profit (w-1)	16,879	6,350	9,300

Workings:

(W-1) Profit Distribution Statement:

	Total	Alpha	Beta	Gamma
Commission [43,370×7/107]	2,837	2,837		
Salaries	1,200		600	600
Interest on Capital	5,000	2,500 [25,000×10%]	1,000	1,500

Residual Profit [43,370-2,837-1,200-5,000] 34,333				
A[34,333×25,000/50,000]	17,167	17,167		
B[34,333×10,000/50,000]	6,867		6,867	
C[34,333×15,000/50,000]	10,300			10,300
	34,333			
		22,504	8,467	12,400
No. problem of minimum share				
25% to be transferred to Capital A/c		(5,626)	(2,117)	(3,100)
	43,370	16,879	6,350	9,300

(W-2) Calculation of adjusted Profit:

Profit before adjustment =	44,000
Depreciation	(550)
Interest	(80)
	43,370

(W-2.1) Depreciation:

Building	[3,200-608] = 2,592 × 10%	=	259
Plant and Machinery	[2,500-384] = 2,116 × 8%	=	169
Furniture	[1,500-280] = 1,220 × 10%	=	122
			550
(W-2.2) Interest on Loan:	2,000,000 × 12% × 4/12	=	80

A. 6 Chagi Prides

Appropriation Account for the year ended 31-12-2016

	Total	B	P	S
First 5 months Interest for 5 months	1,450	(21,000x8%x5/12) 700	(13,500x8%x5/12) 450	(9,000x8%x5/12) 300
Residual profit (6,100 – 1,450)	4,650	2,325 3/6	1,550 2/6	775 1/6
Total	**6,100**	**3,025**	**2,000**	**1,075**
Next 7 months Interest on Capital	4,599	2,247 (32,100x12%x7/12)	1,463	889
Salary	945	-	-	945 (135x7)
Residual Profit (8,000–4,599-945)	2,456	1,228 2/4	614 1/4	614 ¼
Total	**8,000**	**3,475**	**2,077**	**2,448**
Grand total	**14,100**	**6,500**	**4,077**	**3,523**

Current accounts

	B	P	S		B	P	S
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
Balance b/d		2,000		Balance b/d	2,000		2,300
				Profit	6,500	4,077	3,523
Drawings	5,500	3,800	3,500				
Balance c/d	3,000		1,648				
				Balance c/d		1,723	

Workings

W.1 Calculation of goodwill:

[(11,000+9,300+13,000)/3x2 = 22,200]

Capital Account

	B	P	S		B	P	S
				b/d	21,000	13,500	9,000
				Goodwill [3:2:1]	11,100	7,400	3,700
c/d	32,100	20,900	12,700				

W.2 New Ratio

	Old Ratio	New	Adjusted	Or
B	3/6	3/6	6/12	2/4
P	2/6	1.5/6	3/12	¼
S	1/6	1.5/6	3/12	¼

A.7 Rs. '000'

(a) Computation of corrected profit

Given profit after bonus	15,000
Salary	855
Depreciation	240
Sales	(400)
Purchases	300
Adjusted profit after bonus	15,995
Bonus (15,000/100 x 5)	750
Adjusted profit before bonus	16,745
Bonus (16,475/105 x 5%)	(797)
Adjusted profit after bonus	15,948

Profit before bonus	16,745	(105)
Bonus (16,745/105 x 5%)	(749)	(5)
Adjusted Profit after bonus	15,948	100

Profit appropriation statement

Description	Total	M	A	J
Salary (45x12)	1,080	540	-	540
Interest on capital 10%	1,200	300	500	400
Residual profits (15,948-1,080-1,200)	13,668	4,556 (2/6)	6,834 (3/6)	2,278 (1/6)
Total share before minimum share adjustment	15,948	5,396	7,334	3,218
Adjustment of minimum profit*		(113)	(169)	282
Final share	15,948	5,283	7,165	3,500

*3,500-3,218=282
M 2/5 113
A 3/5 169
J 282

(b) Partner's Current accounts

Partner's current account

Description	M	A	J	Description	M	A	J
Opening balance		200		Opening balance	800	-	600
Drawings	4,500	6,250	5,000	Profit	5,283	7,165	3,500
Drawings	405		450				
Purchases		300					
Closing balance	1,178	415		Closing balance			1,350

Workings:

		Dr	Cr
i)	Drawings – **M**	405	
	Drawings – **J**	450	
	Salaries		855
ii)	Acc. Depreciation	240	
	Depreciation		240
	(1,200 x X x 2.25 = 540)		
	(X = 20%)		
	For one year = 1,200 x 20% = 240		

Disposal:

		Dr	Cr
	Cash	900	
	Acc. Depreciation	300	
	(1,200 – 660 - 240)		
	Vehicle		1,200
iii)	Sales	400	
	Debtor		400
	Drawings – **A**	300	
	Purchases		300

A.8 Toby Apparels

Appropriation of profit for the year ended 30 June 2018

	Profit for the period	Appropriation of profit A	B	K
	-------------- Rs. in '000			--------------
Profit for 3 months ended 30 Sep 2017:(12,500,000/12×3)	**3,125**			
– 3 months' interest at 12% p.a. on capital balances	(750)	150	390	210
– Salary to A (50 x 3)	(150)	150		
– Commission to B at 4% of net profit (3,125×4%)	(125)		125	
– Remaining profit in the ratio of 3:7:5 (3,125 – 750 -150 - 125)	(2,100)	420	980	700
Profit for 9 months ended 30 Jun 2018: (12,500,000/12×9)	**9,375**			
– 9 months' interest at 9% p.a. on updated capital	(2,295)	675	810	810
– Salary to B and K @ Rs.75,000 p.m and to A @ Rs.60,000 p.m.	(1,890)	540	675	675
– Remaining profit in the ratio of 2:4:3 (9,375 -2,295 -1,890)	(5,190)	1,153	2,307	1,730
Total share	-	**3,088**	**5,287**	**4,125**

Partner's Current Account

Description	A	B	K	Description	A	B	K
	------- Rs. in '000		--------		-------- Rs. in '000		--------
Opening balance	500			Opening balance		100	2,800
Transferred to capital			2,500	Profit	3,088	5,287	4,125
Drawings	3,100	4,300	3,400				
Closing balance		1,087	1,025	Closing balance	512		
	3,600	**5,387**	**6,925**		**3,600**	**5,387**	**6,925**

Partners' capital accounts

Description	A	B	K	Description	A	B	K
	-------- Rs. in '000		--------		-------- Rs. in '000		--------
Cash Capital withdrawn		4,500		Opening balance	5,000	13,000	7,000
				Goodwill (W-1)	1,500	3,500	2,500
				Cash Further Investment	3,500		
Closing balance	10,000	12,000	12,000	Transfer from current account			2,500
	10,000	**16,500**	**12,000**		**10,000**	**16,500**	**12,000**

W-1 Calculation of Goodwill:

10,500 - 6,000	4,500
9,500 - 6,000	3,500
9,250 - 6,000	3,250
	11,250
11,250 / 3 x 2	7,500

7,500

3 / 15	7 / 15	5 / 15
=1,500	=3,500	=2,500

Goodwill	7,500	
A		1,500
B		3,500
K		2,500

A.9 **Bannu Traders**

(i) Profit sharing for the year ended 31 December 2018

	A	**B**	**C**	**Total**
	---- Rs. in '000 ----			
Interest on partner's capital	900	600	-	1,500
Salary to partners A: (100×12) and C: (120×9)	1,200	-	1,080	2,280
Interest on drawings **A:**(2,500 - 1,200)×8%, **B:** (750×8%)	(104)	(60)	-	(164)
Bonus to B (5,800 - 2,280) ×10%	-	352	-	352
Distribution of Rs. 1.2 million	400	400	400	1,200
Distribution of remaining in 3:3:2 (5,800 – 1.500 – 2,280 + 164 – 352 – 1,200 = 632)	237	237	158	632
Total share	**2,633**	**1,529**	**1,638**	
*Guaranteed profit to **B:** (6,000×30% - 1,529)	(203)	271	(68)	
	2,430	**1,800**	**1,570**	

A 3/4 203
C 1/4 68
B 271

Ratio of capital for guaranteed profit share:

A	9,000	**9**	**3**
C	3,000	**3**	**1**
Total	**12,000**	**12**	**4**

(b)

Partner's Current Account

Description	**A**	**B**	**C**	**Description**	**A**	**B**	**C**
	---- Rs. in '000 ----				---- Rs. in '000 ----		
Opening balance			600	Opening balance	800	1,700	
Drawings	2,500	750	1,000	Profit	2,430	1,800	1,570
Closing balance	730	2,750		Closing balance			30
	3,230	**3,500**	**1,600**		**3,230**	**3,500**	**1,600**

Test question

Q.3 Sigma Brothers (SB) has three partners A, B and C sharing profits and losses in the ratio of 3:2:5 respectively. SB's draft statement of profit or loss for the year ended 30 June 2019 shows net profit of Rs. 4,100,000. On review of the financial statements, the partners have identified the following matters:

- Annual bonus to SB's employees at 10% of the net profit after bonus has not been accrued.
- Salaries withdrawn by the partners were charged to profit or loss. Salary for June 2019 was not withdrawn by C.
- On 1 May 2019, SB opened a new outlet in a rented building. Annual rent effective from 1 April 2019 amounting to Rs. 1,200,000 was paid in advance by C from his personal bank account. The rent paid has not been accounted for in the books of SB.

As per the partnership agreement:

(i) A and C are entitled to a monthly salary of Rs. 50,000 each.

(ii) A is entitled to a minimum profit share of Rs. 1,800,000 per annum. Shortfall in profit, if any, would be shared by B and C in their profit sharing ratio.

Required:

Show how SB's profit for the year ended 30 June 2019 would be shared among the partners

Answer:

Given profit	4,100
Salary expense	1,150
Rent expense	(300)
Profit before bonus to employees	4,950
Bonus (4,950/110x10)	(450)
Profit after bonus	4,500

(W 1) **Profit Distribution Statement**

	Total	A	B	C
Salaries	1,200	600	-	600
Residual Profit [4,500 – 1,200]	3,300	990	660	2,100
		(3/10)	(2/10)	(5/10)
	4,500			
Total share before minimum share adjustment		**1,590**	**660**	**2,100**
Shortfall of A:				
[1,800 - 1,590] = 210 x 2/7 & 5/7	--	210	(60)	(150)
	4,500	1,800	600	2,100

Workings:

i.	Drawings A (50 x12)	600	
	Drawings C (50 x 11)	550	
	Salary expense		115
ii.	Prepaid rent	1,200	
	Capital –C		1,200
iii.	Rent expense	300	
	Prepaid rent		300 (1,200 /12 x3)
iv.	Bonus expense	450	
	Payable		450 (4,950/110x100)

RECTIFICATION OF ERRORS

Types of errors:

1) Those errors that do not cause a difference In trail balance agreement.
2) Those errors that do cause a difference in trail balance.

Main Heads

- Assets
- Liabilities
- Income
- Expenses
- Capital

1 Errors that do not cause any difference in trail balance include:

Sr #	Reasons of errors	Rectifying entry
1	***Error of omission:*** When financial information completely omitted for recording in the books of original entry e.g. Sale invoice of Rs. 1000 issued before closing date but not recorded In the books of original entry (Sales Journal)	Debtors Account 1,000 Sales Account 1,000
2	***Errors of Commission:*** When correct accounting effect (Dr/Cr) is given in the wrong accounting head but the main head remains correct E.g. Purchase of computer Rs. 5,000 for office was wrongly debited to the furniture account (Both accounts relate to the assets main head)	Computer a/c 5,000 Furniture a/c 5,000
3	***Error of Principle:*** When correct accounting effect (Dr/Cr) is given in the wrong accounting head as well as the wrong main head. E.g. Purchase of computer Rs. 5,000 for office was wrongly debited to the salary account, (both accounts belong to the different main head like computer Is Asset and salary is Expense). This error will also cause a different in financial performance and financial position (Asset = Owner's equity + Liability).	Computer a/c 5,000 Salary a/c 5,000
4	***Error of Original entry (transposition error):*** When the correct accounting entry is recorded in the books of accounts but the amount in both accounting effects is wrong although the amount is same: E.g. Debtors to be written off for Rs. 250 as bad debts were recorded in the correct accounts but the amount was posted in both accounts was Rs. 520 causing a different of Rs. 270 on both sides. It Is also known as transposition error	Debtors a/c 270 Bad debt a/c 270

5	*Compensating Error:* When sum of more than One errors contra the accounting effect with each other. E.g. Sales were less credited with Rs.260 and at the same time opening balance of capital account was brought forward with an amount that is Rs. 200 more than the correct amount and Rent Expense owing of Rs.60 was although credited to rent payable account but was not debited to the rent expense a/c.	Capital A/c 200 Rent Expenses 60 Sales 260

Possible reasons for Difference in Trial Balance

When sum of debit column of trial balance exceeds sum of credit column the difference named as suspense account will appear in credit column of trial balance and vice versa (unless errors are corrected).

Sr#	Reasons of errors	Rectifying entry
1	Under/over casting of a ledger a/c maintained in main ledger e.g. • Sales income account was over casted by Rs. 200 • Sales Income Account Was under Casted by Rs. 500	Sales A/c 200 Suspense a/c 200 Suspense a/c 500 Sales a/c 500
2	Omission of a balance from trail balance e.g. balance of a bad debts account Rs. 700 is not appearing in the trail balance.	Bad debt a/c 700 Suspense a/c 700
3	Balance representing an account appearing in trail balance with less or excess amount e.g. Building a/c balance c/f Rs. 700,000 wrongly appearing in the Trail balance with Rs. 70,000.	Building a/c 630,000 Suspense a/c 630,000
4	An account was given debit effect instead of credit effect (causing difference with double amounts) e.g Sales of Rs. 800 on credit was correctly debited in debtors a/c but was also debited in sale a/c mistakenly	Suspense a/c 1600 Sales a/c 1600
5	An account was given credit effect instead of debit effect (causing difference with double amounts) e.g Sales of Rs. 800 on credit was correctly credited in sales a/c but was also credited in debtors a/c mistakenly	Debtor a/c 1,600 Suspense a/c 1,600
6	Single accounting effect either Dr or Cr was recorded /posted in the books of account e.g. sales of Rs.800 on credit was posted in sales a/c only.	Debtor a/c 800 Suspense a/c 800
7	One of the accounting effects was given with wrong amount e.g. sales of Rs. 800 on credit was correctly credited in sales a/c but was wrongly debited to debtors a/c with Rs.80 only.	Debtor a/c 720 Suspense a/c 720

CORRECTION OF ERRORS

1. GRANT

The accountant of Grant Company has prepared a trial balance, but has found that the total of debit balances is Rs.864,600 and the total of credit balances is Rs.862,150.
On investigation, he discovers the following errors in the book-keeping:

(1) Total purchases in the period were recorded at Rs.100 below their correct value, although the total value of trade payables was correctly recorded.
(2) Total telephone expenses were recorded at Rs.1,000 above their correct amount, although the total value of the amounts payable was correctly recorded.
(3) Purchase returns of Rs.550 were recorded as a debit entry in the sales returns account, but the correct entry had been made in the trade payables control account.
(4) Equipment costing Rs.2,000 had been recorded as a debit entry in the repairs and maintenance account.
(5) Rental expenses of Rs.5,490 were entered incorrectly as Rs.5,940 in the expense account but were entered correctly in bank account in the ledger.
(6) Bank charges of Rs.200 have been omitted entirely from the ledger.

Required:
Prepare journal entries for the correction of the errors.

Open a suspense account. Record the appropriate corrections in the suspense account, so that the balance on this account is eliminated.

2. EASTERN PRODUCTS

The following errors and adjustments were discovered:

(i) An invoice of Rs. 3,700 was debited to purchases but the goods were received after year-end and were not included in the closing inventory.
(ii) Store equipment costing Rs. 8,100 and having a book value of Rs. 3,600 was sold for Rs. 2,500. Cash was debited and store equipment was credited by Rs. 2,500. No other entries were made.
(iii) A cheque of Rs. 1,850 received from a customer was dishonoured on June 25, 2013 but no entry was made in the books. Cash there against was received after year-end.
(iv) Purchase of office equipment costing Rs. 15,200 was entered in the purchases account. Depreciation on office equipment is provided at the rate of 10%.
(v) A purchase invoice of Rs. 197 was debited to the supplier account as Rs. 917.
(vi) Purchase returns book was under-casted by Rs. 650.
(vii) The opening balance of furniture account was brought forward as Rs. 18,300 instead of Rs.13,800. Depreciation on furniture is provided at the rate of 10%.
(viii) A balance of Rs.730 in the debtor ledger is to be offset against a balance of Rs. 880 in the creditor ledger.

The profit for the year was calculated at Rs. 956,180 before the correction of above errors..

Required:
(a) Prepare journal entries to adjust the above items.
(b) Recalculate the net profit for the year.

3. CND

The bookkeeper has prepared a preliminary trial balance of CND for the year ended 31 December as follows.

	Rs.	Rs.
Capital account		110,000
Accumulated profit at 1 January		50,000
Bank loan		30,458
Trade receivables and payables	77,240	60,260
Cash in hand and bank overdraft	1,000	5,036
Inventories at 1 January	108,000	
Non-current assets at cost and accumulated depreciation at 31 December	161,879	60,943
Depreciation for the year	15,000	
Purchases and revenues	300,297	402,000
Returns	4,370	4,630
Discounts allowed and received	9,760	6,740
Wages and salaries	22,000	
Rent, rates and insurance	18,036	
Postage, telephone and stationery	3,009	
Repairs and maintenance	2,124	
Advertising	4,876	
Packing materials	924	
Motor expenses	2,000	
Sundry expenses	1,000	
Loan interest	4,000	
Accrued expenses		6,478
Suspense account	1,030	
	736,545	**736,545**

When the bookkeeper discovered that the preliminary trial balance did not balance he made it do so by opening a suspense account and entering the required amount on the appropriate side. A subsequent investigation shows the following mistakes have been made.

(1) A loan to the business of Rs.10,000 from the owner's brother, X, has been added to capital.

(2) Accrued interest on the bank loan of Rs.458 has been credited to the bank loan account instead of being treated as a current liability.

(3) Bank charges of Rs.1,000 have been completely omitted from the books.

(4) In addition to allowing discount of Rs.240 and receiving discount of Rs.260, various customers' and suppliers' accounts amounting to Rs.10,000 were set off by contra. No entries whatever have been made in respect of these items.

(5) Trade receivables amounting to Rs.2,000 are bad and need to be written off.

(6) A debt of Rs.1,000 written off as bad in a previous year has been recovered in full. The amount has been credited to the trade receivables ledger control account.

(7) Goods returned from a customer of Rs.630 have been correctly entered into the receivable ledger control account, but by mistake were entered in the returns outwards journal.

(8) A payment for stationery of Rs.234 was correctly entered in the cash book but debited in the ledger as Rs.243.

(9) A payment of Rs.76 for packing materials has been correctly entered in the cash book, but no other entry has been made.

(10) A payment of Rs.124 for advertising has been debited to repairs and maintenance.

(11) A cheque payment of Rs.26 for insurance has been recorded in all accounts as Rs.62.

(12) A page in the purchase account correctly totalled Rs.125,124 was carried forward to the top of the next page as Rs.125,421.

All entries other than those given above are to be assumed to have been made correctly.

Required:

(a) Show the correcting entries in journal form (i.e. showing accounts and amounts debited and credited but no supporting narrative is required) in respect of each of the mistakes mentioned above.

(b) Show the trial balance of the company at 31 December after these corrections have been made. A working showing how the suspense account is cleared should be included.

4. MR. FAWWAD

Mr. Fawwad owns a factory and closes his books on June 30. The trial balance prepared by him, contained a difference which he kept in a suspense account. On scrutinising the records, the following errors were detected:

- **a.** A cheque of Rs. 10,800 was paid to a creditor who allowed 10% cash discount. The payment was correctly entered in the bank book but was posted to purchase account as Rs. 1,080 only. No other entry was made.
- **b.** Sundry receivables include an amount of Rs. 15,000 which had proved irrecoverable but was not written off. According to a consistent policy, a reserve for bad debt was created @ 5% on closing receivables;
- **c.** Commission of Rs. 3,500 was paid but was debited twice, once in the party's account and again in the commission account;
- **d.** Purchases of Rs. 4,500 were entered as sales in the Sales Day Book.
- **e.** Rs. 600 collected from a party in respect of dues which had been written off as bad two years ago, was credited to the receivables control account.
- **f.** ~~Goods invoiced at Rs. 4,600 were returned by a debtor. These were entered in the~~ purchase book and posted from there to debtor's account as Rs. 6,400.
- **g.** The discount allowed column in the cash book was short casted by Rs. 1,500.
- **h.** A cash sale of Rs. 7,300 to Mr. Anwar was correctly entered in the cash book but was posted to the credit of Mr. Anwar's account
- **i.** An amount of Rs. 17,400 was received in full and final settlement from a customer after he was allowed a discount of Rs. 2,600. However, while writing the books, the amount received was entered in the discount allowed column of the bank book and the discount allowed was entered in the bank column.

Required:

Pass rectification entries (without narration) to correct the above errors.

5. MR REHAN

While closing his books on 30 June 2013, Mr. Rehan identified a difference in the trial balance which he kept in a suspense account. He prepared his P & L account on the basis of this trial balance and arrived at a profit of Rs. 679,000. While trying to reconcile the trial balance he detected the following errors:

- **a.** A cheque of Rs. 25,000 received from the insurance company in respect of loss of inventory has been paid into the proprietor's personal bank account and has not been recorded in the books. No entry has been passed in respect of the loss.
- **b.** Bill received from ABC Furnishings on 1 July 2012 for repairs to furniture Rs. 3,000 and for new furniture supplied Rs. 10,000 was entered in the purchase day book as Rs. 11,000. Depreciation on furniture is provided @ 10 % per annum.
- **c.** Goods worth Rs. 10,200 purchased from a creditor on 28 June 2013 had been entered in the Purchase Day Book and credited to him but were not delivered till 5 July 2013. However, the title of the goods had passed on 28 June 2013.
- **d.** A computer bought originally for Rs. 70,000 four years ago and depreciated to Rs. 12,000 had been sold for Rs. 15,000 on the first day of the year. The amount deposited was entered in the bank book but no other entry was passed.
- **e.** Goods valuing Rs. 13,000 were returned by Zahid. These were entered in the Purchase Day Book and posted to a supplier's account as Rs. 31,000.
- **f.** Discount of Rs. 3,700 was allowed but posted to the credit of discount received a/c as Rs. 7,300.

g. A cheque of Rs. 10,800 was paid to a creditor who allowed 10% cash discount, but the payment was wrongly posted to purchase account as Rs. 1,080 only without any other entry.

Required:

(a) Pass rectification entries (without narration) to correct the above errors.

(b) Recalculate the profits after taking into account the above corrections.

6. **AYUB BROTHERS**

The trial balance of Ayub Brothers did not agree as at 31 December 2013 and the difference was carried to a suspense account. On scrutinising the books of account, the following types of errors were detected:

a. Receivables include Rs. 15,000 which are irrecoverable and need to be written off.

b. Goods invoiced at Rs. 4,600 were returned by a customer. It was entered in the purchase book and posted from there to a creditor's account as Rs. 6,400.

c. A cheque of Rs. 8,000 received from a customer was not posted to his ledger account. Moreover, the corresponding sales invoice for Rs. 12,000 was incorrectly passed through the sales day book as Rs. 2,000.

d. An amount of Rs. 3,800 owed by Zahid & Company for goods supplied was to be adjusted against an amount of Rs. 8,500 owed to Zahid & Company. No entry has been made in this regard.

e. A purchase of Rs. 15,100 was entered in the purchase day book as Rs. 1,500 and posted to the supplier's account as Rs. 5,100.

f. Goods invoiced at Rs. 23,000 and returned by Hamid Khan, a debtor, were entered in the purchase day book and posted therefrom to Hammad Khan, a creditor, as Rs. 32,000.

g. A supplier's invoice for Rs. 12,300 had been entered in the purchase day book on 28 December 2013. However, the goods were received on 2 January 2014.

h. Ayub Brothers maintains a allowance of 5% of the gross amount of receivables.

Required:

Prepare journal entries to rectify the errors identified above.

(Narrations are not required.)

Answers:

1. GRANT

Transaction		Debit	Credit
		Rs.	Rs.
1	Purchases	100	
	Suspense account		100
	Correction of error: purchases under-stated by Rs.100.		
2	Suspense account	1,000	
	Telephone expenses		1,000
	Correction of error: telephone expenses over-stated by Rs.1,000.		
3	Suspense account	1,100	
	Purchase returns		550
	Sales returns		550
Correction of error. Purchase returns of Rs.550 incorrectly recorded as a debit entry in sales returns.			
4	Equipment	2,000	
	Repairs and maintenance		2,000
Correction of error. Equipment purchase costs incorrectly recorded as repairs and maintenance expenses			
5	Suspense account	450	
	Rent expenses		450
	Correction of error: rent expenses over-stated by Rs.450.		
6	Bank Charges	200	
	Bank account		200

Transaction omitted from the ledger.

Suspense account

	Rs.		Rs.
Telephone expenses	1,000	Opening balance	2,450
Purchase returns	550	(864,600 – 862,150)	
Sales returns	550	Purchases	100
Rent expenses	450		
	2,550		2,550

2. EASTERN PRODUCTS

(a)

		Debit	Credit
1	Creditor account	3,700	
	Purchases		3,700
2	Accumulated Depreciation	4,500	
	Loss on sale of store equipment	1,100	
	Store equipment a/c		5,600
3	Debtors a/c	1,850	
	Bank		1,850
4	Office Equipment	15,200	
	Purchases		15,200
	Depreciation expense	1,520	
	Accumulated depreciation – office equipment		1,520
5	Suspense a/c	1,114	
	Creditor a/c (197 + 917)		1,114
6	Creditors	650	
	Purchase Returns		650
7	Suspense a/c	4,500	
	Furniture a/c		4,500
	Accumulated Depreciation	450	
	Depreciation expenses		450
8	Creditor a/c	730	
	Debtors a/c		730

(b) **Recalculation of net profit for the year**

Net profit as per question	956,180
Add: Reversal of purchases	3,700
Equipment wrongly debited to purchases	15,200
Purchase returns	650
Reversal of depreciation on furniture	450
	976,180
Less: loss on sale of store equipment	(1,100)
Depreciation on office equipment	(1,520)
Adjusted net-profit	973,560

3. CND

(a) **Correcting entries**

		Dr Rs.	*Cr* Rs.
(1)	Capital a/c	10,000	
	Loan a/c X		10,000
(2)	Bank loan a/c	458	
	Accrued expenses a/c		458
(3)	Bank charges a/c	1,000	
	Bank overdraft a/c		1,000
(4)	Trade payables a/c	10,260	
	Discounts allowed a/c	240	
	Trade receivables a/c		10,240
	Discount received a/c		260
(5)	Bad debts a/c	2,000	
	Trade receivables a/c		2,000
(6)	Trade receivables a/c	1,000	
	Bad debts a/c		1,000

(7)	Sales returns a/c	630	
	Purchases returns a/c	630	
	Suspense a/c		1,260
(8)	Suspense a/c	9	
	Postage, telephone and stationery a/c		9
(9)	Packing materials a/c	76	
	Suspense a/c		76
(10)	Advertising a/c	124	
	Repairs and maintenance a/c		124
(11)	Bank overdraft a/c (62-26)	36	
	Insurance a/c		36
(12)	Suspense a/c (125,421 – 125,124)	297	
	Purchases a/c		297

(b) **Trial balance at 31 December**

	Dr Rs.	*Cr* Rs.
Capital account Rs.(110 – 10)		100,000
Accumulated profits at 1 January		50,000
Bank loan Rs.(30,458 – 458)		30,000
Loan account – X		10,000
Trade receivablesRs. (77,240 – 10,240 – 2,000 + 1,000) 66,000		
Trade payables Rs.(60,260 – 10,260)		50,000
Cash in hand	1,000	
Bank overdraft Rs.(5,036 + 1,000 – 36)		6,000
Inventories at 1 January	108,000	
Non-current assets at cost	161,879	
Accumulated depreciation at 31 December		60,943
Depreciation for the year	15,000	
Purchases Rs.(300,297 – 297)	300,000	
Revenues		402,000
Sales Returns (4,370 +630)	5,000	
Purchase Returns(4,630 -630)		4,000
Discounts allowed Rs.(9,760 + 240)	10,000	
Discounts received Rs.(6,740 + 260)		7,000
Wages and salaries	22,000	
Rent, rates and insurance Rs.(18,036 – 36)	18,000	
Postage, telephone and stationery Rs.(3,009 – 9)	3,000	
Repairs and maintenance Rs.(2,124 – 124)	2,000	
Advertising Rs.(4,876 + 124)	5,000	
Packing materials Rs.(924 + 76)	1,000	
Motor expenses	2,000	
Sundry expenses	1,000	
Loan interest	4,000	
Bank charges	1,000	
Bad debts (2,000 – 1,000)	1,000	
Accrued expenses		6,478
Interest payable		458
	726,879	726,879

Working

Suspense a/c

	Rs.		Rs.
Original balance	1,030	(7) Goods returned mis posting	1,260
(8) Stationery transposition Error	9	(10) Materials payment omitted	76
(12) Purchases transposition Error	297		
	1,336		1,336

4. MR. FAWWAD
Journal Entries

	Debit Rs.	Credit Rs.
1. Creditor A/c (10,800+1,200)	12,000	
Purchases A/c		1,080
Suspense A/c		9,720
Discount received		1,200
2. Bad Debts expenses	15,000	
Debtors A/c		15,000
Allowance for doubtful debts A/c	750	
Bad debt expense account		750
3. Suspense A/c	3,500	
Parties A/c		3,500
4. Sales A/c	4,500	
Debtors A/c		4,500
Purchase A/c	4,500	
Payables A/c		4,500
5. Debtors (receivables control account)	600	
Other income or bad debt expense A/c		600
6. Sales return A/c	4,600	
Purchase A/c		4,600
Debtors A/c	1,800	
Suspense A/c		1,800
7. Discount allowed	1,500	
Debtors account		1,500
8. Mr. Anwar	7,300	
Cash sales		7,300
9. Bank (17,400 – 2,600)	14,800	
Discount allowed		14,800

5. MR REHAN

(a)

S. No.	Particulars	Debit (Rs.)	Credit (Rs.)
(i)	Drawings A/c	25,000	
	Purchases		25,000
(ii)	Repairs	3,000	
	Furniture and Fittings	10,000	
	Purchases		11,000
	ABC Furnishings		2,000
	Depreciation	1,000	
	Acc. dep. on furniture		1,000
(iv)	Goods-in-transit	10,200	
	Purchases		10,200
(v)	Suspense Account	15,000	
	Accumulated depreciation - computers	58,000	
	Non-current assets		70,000
	Gain on disposal of computers		3,000
(vi)	Returns Inward	13,000	
	Payables	31,000	
	Purchases		13,000
	Debtors		13,000
	Suspense Account		18,000
	(On the assumption that purchase isrecorded as Rs. 13,000 and creditor as Rs.31,000)		
(vii)	Discount Allowed	3,700	
	Discount Received	7,300	
	Suspense Account		11,000
(viii)	Creditor A/c	12,000	
	Suspense A/c	1,080	
	Purchases		1,080
	Discount received		1,200
	Bank		10,800

(b)

Recalculation of Profit and Loss — **Amount in Rupees**

(ii)	Repair exp	3,000		Unadjusted Profit	679,000
(ii)	Dep. on furniture 10% of 10,000	1,000	(i)	Drawings a/c (receipt from ins co.)	25,000
			(ii)	Purchases	11,000
			(v)	Goods-in-Transit	10,200
			(vi)	Gain on sale of asset	3,000
(vii)	Return inwards	13,000			
(viii)	Discount allowed/received (3,700+7,300)	11,000	(vii)	Purchases	13,000
	Adjusted profit for the Year	722,855	(ix)	Purchases	1,080

	(ix)	Discount Received	1,200
715,480			715,480

6. **AYUB BROTHERS**

		Dr.	Cr.
1.	Bad debts accounts	15,000	
	Debtors A/c		15,000
2.	Sales return A/c	4,600	
	Payables	6,400	
	Purchase A/c		4,600
	Suspense A/c		1,800
	Debtors A/c		4,600
3.	Suspense A/c	8,000	
	Debtor A/c		8,000
	Debtor A/c	10,000	
	Sales		10,000
4.	Payables A/c – Zahid & Co.	3,800	
	Debtors A/c – Zahid & Co.		3,800
5.	Purchases A/c (15,100-1,500)	13,600	
	Payables A/c (15,100-5,100)		10,000
	Suspense A/c		3,600
6.	Returns Inwards/Sales returns	23,000	
	Payables A/c	32,000	
	Purchase A/c		23,000
	Debtors A/c		23,000
	Suspense A/c		9,000
7.	Creditors /Goods in transit	12,300	
	Purchases		12,300
8.	Allowance for doubtful debts - B/S	2,220	
	Bad Debt Expenses		2,220
	(-15,000-4,600-8,000+10,000-3,800-23,000)= - 44,400 × 5%		

Extra practice questions

Q1. Draft income statement of Timothy Enterprises (TE) for the year ended 31 December 2017 shows gross profit of Rs. 850,000 and net profit of Rs. 460,000.

During the review of the financial statements, following errors were noticed:

(i) An invoice of Rs. 3,700 was debited to purchases but the goods were received after year-end and were not included in the closing inventory.

(ii) Transportation inward amounting to Rs. 2,000 was included in transportation outward.

(iii) The sub-total of a closing stock sheet had been carried forward as Rs. 21,830 instead of Rs. 21,380.

(iv) A receipt of Rs. 21,850 was credited to sales. The amount was received from a debtor as full and final settlement of an outstanding balance of Rs. 23,000.

(v) Goods having sales value of Rs. 4,500 were used for office repairs. No entry has been made in the books.

(vi) Purchase of office computer on 1 April 2017 amounting to Rs. 42,000 was entered in the purchase account.

(vii) An item of furniture was sold on credit for Rs. 3,000 and entered in the sales day book. The book value of this item was Rs. 5,000.

(viii) Purchase return amounting to Rs. 6,700 has been recorded as sales return.

(ix) The owner had withdrawn goods costing Rs. 4,680 for personal use. No entry has been made in the books.

TE uses periodic inventory method. Goods are sold at cost plus mark up of 25%.
Depreciation on office computer is provided at the rate of 25%.

Required:
Compute the corrected gross profit and net profit for the year. **(14)**

Ans.

Effect on Gross Profit

Given Profit	850,000 Cr
Purchases	3,700 Cr
Carriage Inwards	2,000 Dr
Cost of sales	450 Dr
Sales	21,850 Dr
Purchases	3,600 Cr
Purchases	42,000 Cr
Sales	3,000 Dr
Purchase return	6,700 Cr
Sale return	6,700 Cr
Purchases	4,680 Cr
Adjusted Gross Profit	890,080 Cr

Effect on Net Profit	
Given Profit	460,000 Cr
Purchases	3,700 Cr
Carriage Inwards	2,000 Dr
Carriage Outward	2,000 Cr
Cost of sales	450 Dr
Sales	21,850 Dr
Discount Allowed	1,150 Dr
Office Repairs	3,600 Dr

Purchases	3600 Cr
Purchases	42,000 Cr
Depreciation	7,875 Dr
Sales	3,000 Dr
Loss	2,000 Dr
Purchases return	6,700 Cr
Sale return	6,700 Cr
Purchases	4,680 Cr
Adjusted Net Profit	487,455 Cr

Note:

Increase in closing stock increases the Gross Profit because of decrease in cost of sale while decrease in closing stock decrease the gross profit because of increase in cost of sale.

Workings:

1	Creditor	3,700	
	Purchases		3,700
2	Carriage Inwards	2,000	
	Carriage Inwards		2,000
3	Cost of sales	450	
	Stock		450
4	Sales	21,850	
	Discount Allowed	1,150	
	Debtor		23,000
5	Office Repairs	3,600	
	Purchases		3,600
6	Office Computer	42,000	
	Purchases		42,000
	Depreciation	7,875	
	Acc. Depreciation		7,875
7	**Posted:**		
	Debtor	3,000	
	Sale		3,000
	Required:		
	Receivable	3,000	
	Loss	2,000	
	Furniture		5,000(WDV)
	Rectifying:		
	Sale	3,000	
	Debtor		3,000
	Receivable	3,000	
	Loss	2,000	
	Furniture		5,000(WDV)
	When the error is made in Day Book then we will rectify the double entry. But if the error is made in ledgers, then we assume other Dr /Cr effect is correct		
8	Suspense	13,400	
	Purchase return		6,700
	Sale Return		6,700
9	Drawings	4,680	
	Purchases		4,680

Q.2 Financial statements of **Zeta Traders (ZT)** for the year ended 30 June 2019 is under preparation. Following information has been gathered in this respect:

(i) Trade receivables as at 30 June 2019:

	Rupees
Trade receivables	2,500,000
Provision for doubtful debts	(400,000)
Net trade receivables	2,100,000

It was noted that:

- an old outstanding balance of Rs. 250,000 which was written off previously was settled during the year at 20% discount. The amount received was credited to trade receivables.
- purchase return amounting to Rs. 500,000 was mistakenly debited to trade receivables.
- Rana and Sons having a balance of Rs. 80,000 due for more than one year was declared bankrupt and its balance needs to be written off.

ZT maintains provision for doubtful debts:

- at 25% for balances outstanding for more than six months. As at 30 June 2019, such balances are aggregated to Rs. 600,000 (excluding balance of Rana and Sons); and
- at 5% for the remaining balances

(ii) A cheque dated 25 June 2019 for Rs. 150,000 was received from an insurance company and deposited by the owner in his personal bank account. The cheque was received in settlement of an inventory loss claim. Actual inventory loss was determined at Rs. 180,000. No entries have been made for loss of inventory and insurance claim.

(iii) The opening balance of accumulated depreciation was brought forward as Rs. 280,000 instead of Rs. 820,000. The error was tried to be corrected with the difference by crediting accumulated depreciation and debiting depreciation expense.

(iv) Goods amounting to Rs. 350,000 received from a supplier on 30 June 2019 were included in the year-end physical inventory count but recorded in purchases day book on 1 July 2019.

(v) Third party stock of Rs. 500,000 lying on ZT premises has been included in ZT's year-end inventory.

(vi) ZT uses periodic inventory method.

Required:

a) Prepare adjusting / correcting entries for the year ended 30 June 2019. (Narrations are not required)

b) Compute the net effect of the above on ZT's profit for the year ended 30 June 2019

A.2 (a) Zeta Traders

Adjusting/correcting entries

General journal

	Description	Debit	Credit
		------ Rupees ------	
(i)	Trade receivable (250,000 x 80%)	200,000	
	Bad debt		200,000
	OR		
	Trade receivable (250,000 x 80%)	200,000	
	Discount allowed	50,000	
	Bad debts		250,000
	Trade payable	500,000	
	Trade receivable		500,000
	Bad debts	80,000	
	Trade receivable		80,000
	Allowance for doubtful debts (W-1)	174,000	
	Bad debts		174,000
(ii)	Abnormal loss	180,000	
	Purchases		180,000
	Drawings	150,000	
	Abnormal loss		150,000
(iii)	Suspense (820,000–280,000)	540,000	
	Depreciation expense		540,000
(iv)	Purchases	350,000	
	Trade payables		350,000
(v)	Cost of sales	500,000	
	Closing inventory		500,000

Debtors

Unadjusted b/d	250,000	Creditors	500,000
Bad debts	200,000	Bad debts	80,000
		c/d	2,120,000

Allowance

Allowance	174,000	Unadjusted b/d	400,000
c/d (W.1)	226,000		

W-1

1.Specific allowance	
600,000 x 25%	150,000
2.Closing debtors	2,120,000
Less balance on which specific allowance is created	(600,000)
Remaining Debtors	1,520,000
3. General allowance @5%	76,000
4.Total allowance (150,000 + 76,000)	**226,000**

(b)

Increase / decrease in net profit

Recovery of old outstanding balance previously written off	200,000 Cr.
Bad debts	80,000 Dr
Bad debts	174,000 Cr
Loss of goods (180,000-150,000)	30,000 Dr
Purchases	180,000 Cr
Depreciation expense	540,000 Cr
Purchases	350,000 Dr
Cost of sales	500,000 Dr
Net effect on profit	**134,000 Cr**

Theory with Questions

Introduction to business and accounting

Definitions: Business

Business is an economic system where goods and services are exchanged for one another or for money.

Definitions: A business entity

A business entity is a commercial organization that aims to make a profit from its operations.

Characteristics of business

All businesses share certain characteristics.

- Businesses exist to make profits.
- Businesses make profit by supplying goods or services to others (customers).
- Businesses that supply goods might make those goods or buy them from other parties (for example, food retailers buy food off food producers and sell it to their customers).
- Profit is the reward for accepting risk. For example, a food retailer might buy 100 kgs of bananas but might not be able to sell them all. In other words, he runs the risk of paying for bananas that he will have to throw away. He is willing to run the risk because if he does not buy bananas he has no chance of selling them for a profit.
- The profit of a business belongs to its owners. A share of the profits might be paid to the owners periodically.

There are three main types of business entity:

- sole proprietorship;
- a business partnership;
- a company (a limited liability company).

Characteristics of different types of business entity

The advantages and disadvantages of operating as each type of business entity may be summarised briefly as follows:

Business structure	Sole trader	Partnership	Company
Owned by...	One person	Several individuals working together	Shareholders
Liability for the unpaid debts and other obligations of the business	Personal liability of owner	Personal liability of partners	Limited
Management	Business managed by its owner	Business managed by its owners	Larger companies are managed by professional managers
Raising capital	Capital for the business is provided by its sole owner. Likely to be limited in amount.	Capital for the business is provided by its owners. Often limited in amount	Capital for the business is provided by its shareholders. Public companies can raise new capital from investors in the stock market. Most very large businesses are companies.

Financial accounting and auditing	Some financial accounts needed for tax purposes.	Financial accounts needed for the benefit of the partners and for tax purposes.	Fairly strict regulation of financial reporting by companies. Also legal requirements for audit.

The purpose of financial accounting

Financial accounting is a term that describes:

- maintaining a system of accounting records for business transactions and other items of a financial nature; and
- reporting the financial position and the financial performance of an entity in a set of financial statements.

The term ***entity*** is used to describe any type of organization. Business entities include companies, business partnerships and the businesses of 'sole traders'

Accounting systems

Business entities operate a system to record business transactions in accounting records. This system is called a ***book-keeping system***. All large businesses (and many small ones) have a book-keeping system for recording the financial details of their business transactions on a regular basis. The bookkeeping records of a business are often referred to as ***the accounts*** of the business.

At this stage of study, financial statements include;

- A statement of financial position; and
- A statement of comprehensive income.

The business entity concept

Financial reports are constructed as if the business entity is separate from its owners. In other words, the business entity and its owners are different. This is known as the ***business entity concept***.

In other words, personal incomes and expenses of owner are not considered while calculating profit of business. This concept has legal 'reality' in the case of companies. A company by law is a legal person, separate from its owners (the shareholders). However, the concept is also applied to sole traders and partnerships.

Illustration:

Ilyas Khan sets up a sole trader business as a builder, and he calls the business 'IK Builders'.

Legally, IK Builders does not have a separate legal personality. The debts of IK Builders are debts of Ilyas Khan. However, for the purpose of financial reporting, the business is accounted for as an entity separate from Ilyas Khan.

Responsibility for preparing financial statements

Type of entity	Responsibility
Sole trader	There may be no obligation to prepare financial statements (other than for tax purposes) but if so the owner of the business is responsible. The owner might employ a person or persons to maintain the accounting records and prepare financial statements.
Partnership	There may be no obligation to prepare financial statements (other than for tax purposes) but if so the partners are responsible. They might employ a person or persons to maintain the accounting records and prepare financial statements.
Company	Companies must prepare financial statements for shareholders and for filing with relevant regulatory bodies. It is the responsibility of the directors to ensure that this is done. Usually the work is delegated to employees (accountants).

Components of financial statements
A full set of financial statements would include the following
- a statement of financial position;
- a statement of comprehensive income;
- a statement of changes in equity (not in this syllabus);
- a statement of cash flows (not in this syllabus) and
- notes to the financial statements (not in this syllabus).

The objective of financial reporting
The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity.

Users of financial statements:

Investors
Investors in a business entity are the providers of capital. They need information that will help them to make investment decisions.
In the case of shareholders in a company, these decisions will often involve whether to buy, hold or sell shares in the company. Financial statements also give some indication of the ability of a company to pay dividends to its shareholders out of profits.
Lenders
Lenders, such as banks, are interested in financial information about businesses that borrow from them. Financial statements can help lenders to assess the continuing ability of the borrower to pay interest, and its ability to repay the loan principal at maturity.
Suppliers
Financial information about an entity is also useful for suppliers who provide goods on credit to a business entity, They can use the financial statements to assess the ability of the company to make payment to them.
Government
The government and government agencies are interested in the financial statements of business entities. They might use this information for the purpose of business regulation or deciding taxation policies.
The public
In some cases, members of the general public might have an interest in the financial statements of a company. 'For example, entities may make a substantial contribution to the local economy in many ways including the number of people they employ and donation they make to a charitable institution etc.
Employees
Employees need information about the financial stability and profitability of their employer. An assessment of profitability can help employees to reach a view on the ability of the employer to pay higher wages, or provide more job opportunities in the future.
Customers
Customers might be interested in the financial strength of an entity, especially if they rely on that entity for the long-term supply of key goods or services.
Managers
They are interested in current performance of the business to improve future performance.

Capital and revenue expenditure
Capital expenditure is expenditure made to acquire or improve long term assets that are used by the business:
Examples include:
- purchase of property, plant and equipment, office equipment; and motor vehicles;
- installation costs associated with new equipment;
- Improvements and additions to existing non-current assets (for example, building extensions, installation of air-conditioning etc.)
- These expenditures are recognized as an asset and then depreciated over their useful life

Revenue expenditure is expenditure on day-to-day operating expenses.
Examples include:
- Purchase of goods meant for resale in the normal course of business;
- Expenditures made to meet the day to day running costs of a business (for example, rent, energy, wages etc.)
- Expenditures made to repair non-current assets.
- Expenditures made to distribute goods to customers.
- Costs of administering a business (for example, accounting services, license fees etc.)

Revenue income and capital receipts

Revenue income is income arising from the normal operations of a business from its investments.

Examples include:

- Revenue from the sale of goods.
- Commission income against provisions.
- Interest income
- Rent income

Revenue is reported in the statement of comprehensive income

Capital receipts are receipts of 'long term' such as money from a bank loan, or new money invested by the business owners (which is called 'capital').

Capital receipts affect the financial position of an entity, but not its financial performance. Capital receipts are therefore excluded from the statement of comprehensive income.

These are statements of financial position items.

ACCOUNTING CONCEPTS

Accrual basis (matching concept)

Income and expenses of a period should be recognized in income statement of the same period

Example 1: Accruals basis

A company prepares its financial statements to the 30 June each year.

It sells goods for Rs. 50,000 to a customer on 6 June 2017, but does not receive a cash payment from the customer until 15 August 2017.

Accruals basis:

The sale is recognized as income in the year to 30 June 2017, even though the cash is not received until after the end of this financial year.

Example 2: Accruals basis

A company starts its business on 1 September 2016. It acquires an office for which it pays one year's rent in advance, to 31 August 2017.

The cost of the annual rental is Rs. 120,000. The company prepares its financial statements for a financial period ending on 31 December each year.

Accruals basis:

The office rental cost in the period to 31 December 2016 is the cost of just four months' rent.

The expense is therefore Rs. 40,000 (Rs. 120,000 x 4/12) in 2016, and there has been a prepayment for Rs. 80,000 that relates to the next financial period, the year to 31 December 2017.

Prepayment.

A prepayment is an amount of money paid in advance for benefits that will be received in the next accounting period.

A prepayment in Year 1 of some expenses relating to Year 2 should not be charged as an expense in Year 1, but should be treated as an expense in Year 2.

Accrued expense or accrual.

An accrual or accrued expense is an amount that is payable in respect of a benefit that has been received in period but for which payment has not been made

Income receivable: (accrued income)

Means an amount for which goods or services have been provided but cash is not yet received. (In other words, income has been earned but amount is yet to be received)

Unearned income: (Advance income)

Means amount has been received but for which goods or services are to be delivered. (In other words, amount has been received but income is not yet earned)

Consistency

The content of the financial statements must be presented consistently from one period to the next.

Example: Consistency

A manager of a business has been promised a bonus if he can improve gross profit to more than 10% above what it was last year.

In the event the results of the business have been exactly the same but the manager has prepared the financial statements on a slightly different basis.

	2012	2013
	Rs.000	Rs.000
Sales	25,000	25,000
Cost of sales:		
Production costs	10,000	10,000
Warehousing costs	10,000	
	(20,000)	(10,000)
Gross profit	5,000	15,000
Less: Other expenses	(4,000)	(14,000)
Net profit	1,000	1,000

The manager has presented the information in a different way. This year's presentation is inconsistent with last year's.

This might mislead the user of the financial statements (in this case the person who will decide if the manager will receive a bonus)
It might be that the manager's presentation is correct but in this case the previous year's results should be represented onto a consistent basis in order to prevent a misleading impression.

Completeness
The objective of financial reporting is to provide useful information. Information is only useful if a person can rely on it. A person can only rely on information if it is complete.
Completeness refers to whether all transactions that occurred during the period have been recorded

Example: Completeness

The accruals example can be used to illustrate this.

A company rents office space at a cost of Rs. 6,000,000 per year paid 12 months in arrears (this means that the company pay the rent at the end of the year).

The first payment is due on 30 June Year 2.

The company prepares its financial statements to 31 December each year.

The company will not have received an invoice for the rent when it is preparing its financial statements for 31 December Year 1

If the company does not accrue for the expense that relates to the 6 months to 31 December year 1 the information would be incomplete.

True and fair view (faithful representation)
Financial statements should give a ***true and fair view*** of the financial position, financial performance and changes in financial position of an entity. Another way of saying this is that financial statements should provide a ***faithful representation*** of these.
A perfectly faithful representation would have three characteristics. It would be:

- **Complete** – means financial statements should include all information
- **Neutral** – means financial statements should be prepared without any bias; and
- **Free from error** – there should be no errors or omission in financial statements.

Materiality
The relevance of information is affected by its materiality.
Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity.
An error which is too trivial to affect a user's understanding of financial statement is referred to as immaterial.

Prudence
Prudence involves allowing for some caution in preparing financial statements, by making reasonable and sensible allowances in order to avoid overstating assets or income and to avoid understating expenses or liabilities.

Financial statements must sometimes recognize the uncertainty in business transactions. For example, if a business is owed Rs. 1,000,000 by a number of its customers, there will be some uncertainty as to whether all the money will actually be collected.
Prudence concept is used in the measurement of inventories and trade receivable.

Example: Prudence
A company has receivables of Rs. 10,000,000.
The company knows from experience that about 2% of its receivables will not be collected because of customers being in financial difficulty.
It is prudent to make an allowance for doubtful debts to 2% of receivables (but it would be inappropriate to make an excessive allowance, say 10% of receivables).
The company would recognize an allowance of Rs. 200,000 to set against the receivable in the statement of financial position showing a net amount of Rs. 9,800,000 (10,000,000 less 200,000).

Going concern basis
This means that financial statements are prepared on the assumption that the entity will continue to operate for the foreseeable future, and does not intend to go into nor will be forced into liquidation.
If the going concern assumption is valid; then prepare the financial statements on the basis of accounting standards.
If however going concern assumption is not valid, then assets are measured at market values and liabilities are measured at settlement values.

Substance over form
Financial information must account for transactions in a way that reflects their substance and economic reality rather than their legal form. If there is a difference between economic substance and legal form, the financial information should represent the economic substance.
Example of situation where concept of substance over form is applied:
- Lease agreements.
- Sales and repurchase agreements.

Example: Substance over form (leases)

Alpha rents (leases) an asset from Beta.

The asset is expected to be useful for 10 years after which it will be scrapped.

Alpha has a contract to use the asset for 10 years.

Analysis:

The substance of the transaction is that Alpha has bought the asset from Beta.

Beta would only agree to let Alpha use the asset for all of its useful life if the rentals received from Alpha covered Beta's costs of buying the asset and gave Beta a financial return. This is the same as Alpha borrowing money and buying the asset.

Alpha must recognize the leased asset as if it owns it and also must recognize a liability to pay for the asset.

Elements of financial statements:

Assets

An asset is defined as:

- a resource controlled by the entity;
- as a result of past events; and
- From which future economic benefits are expected to flow to the entity.

Liabilities

A liability is defined as:

- a present obligation of an entity
- arising from past events
- The settlement of which is expected to result in an outflow of resources that embody economic benefits.

Equity [Total Assets – Total liabilities]

Equity is the residual interest in business entity after the value of all its liabilities has been deducted from the value of all its assets. Equity comprises of amount invested by owners into business plus undrawn profits.

Incomes

Financial performance is measured by profit or loss. Profit is measured as income less expenses. Income includes both revenue and gains.

- **Revenue** is income arising in the course of the ordinary activities of the entity. It includes sales revenue, fee, rental income and income from interest.
- **Gains** include gains on the disposal of non-current assets.

Expenses

Expenses include both routine business expenses and losses.

- **Expenses** arising in the normal course of activities, such as the cost of sales and other operating costs, including depreciation of non-current assets.
- **Losses** include for example, the loss on disposal of a non-current asset, and losses arising from damage due to fire or flooding

Measurement of assets and other elements

Assets, liabilities, income and expenses can be measured in the following ways according to circumstances:

- **Historical cost.** This is the actual amount of cash paid or received. For example, the historical cost of an item of equipment is the amount that it cost to buy (at some time in the past).
- **Current cost.** Assets might be valued at the amount that would have to be paid to obtain an equivalent current asset 'now'. For example, if a company owns shares in another company, these assets might be valued at their current market value. Similarly, a company that owns a building might choose to value the building at its current cost, not the amount that it originally cost.
- **Realizable value or settlement value.** Assets might be valued at the amount that would be obtained if they were disposed of now (in an orderly disposal).
- **Present value.** This is a current value equivalent of an amount that will be receivable or payable at a future time.

The most common method of measurement is historical cost, but the other methods of measurement are also used in certain cases. These cases are not in your syllabus.

Questions

Question 1:

In respect of each of the following, give example of a transaction which would result in:

(i) Decrease in a liability and increase in another liability.

(ii) Increase in an asset and decrease in another asset.

(iii) Decrease in an asset and decrease in liability.

(iv) Decrease in capital and decrease in asset. **(04)**

Question 2:

Consider the following situations:

(i) Due to heavy losses during the current year, Quality traders (QT) decided to discontinue its operations with effect from 1 August 2016. However, QT's financial statements for the year ended 30 June 2016 were prepared using the same basis as last year.

(ii) Results of Shan enterprises (SE) fluctuate widely from year to year. Therefore, SE's management has decided to create certain provision in the periods of higher profits and adjust those provisions in the period of lesser profits to maintain profits at a consistent level from year to year.

Required:

(a) Identify and explain the accounting concept/principle relevant to each of the above situations. **(04)**

(b) Suggest adjustments, if any, to correct the financial statements for the year ended 30 June, 2016. **(02)**

Question 3:

While preparing the financial statements, you are faced with the following situation:

(i) The future existence of the company is uncertain.

(ii) The credit cards bills of the proprietor were paid and charged to the business.

(iii) Property, plant and equipment now costs more than the price at which it was purchased at the inception of business. However, the current prices are not reflected in the financial statements.

(iv) During the year, the company purchased stationery worth Rs. 30,000. The amount has been charged to office supplies consumed, however major portion of the stationery was consumed after year-end.

(v) The company had a poor trading year and the owners have decided to adopt weighted average valuation method instead of FIFO.

(vi) Leased equipment have been recorded as assets although these are not owned by the organization.

Required:

State the accounting concept that has been applied or needs to be considered in each of the above situations. **(06)**

Question 4:

(a) Briefly describe the concept of 'Substance over form'. Give two examples. **(04)**

(b) Big Traders, who is a multi-million rupees trading house, purchased a calculator for Rs. 1,500. The calculator is to be used for 3 years. Keeping in view the relevant accounting concepts, describe the accounting treatment of the above transaction. **(03)**

Question 5:

Name the accounting concepts/principles on which the following rules are based.

(i) Nothing material is left out that would be vital to investors or other users in assessing the underlying events and conditions of the business.

(ii) Whether the item in question affects decision of the users of the financial statements.

(iii) A company is separate and distinct from its owners.

(iv) Financial information must not only represent relevant phenomena but it must also be complete, neutral and free from error.

(v) Expenses incurred in a particular time period should be compared with the revenue earned during the same time period.

(vi) Caution should be exercised while preparing financial statements in order to avoid overstatement of net assets and net income.

(vii) The assumption that a business entity will continue in existence for the foreseeable future.

(viii) Same accounting policy shall be applied to accounting events from period to period. **(08)**

Question 6:

What do you understand by accrual basis of accounting? Identify the main advantage of following the accrual basis of accounting?

Question 7:

On reviewing the draft financial statements of Sky-link traders (ST) for the year ended 31 December 2015, following matters have been identified:

(i) Trade Receivables

ST does not provide any allowance for doubtful debts. Past experience shows that each year about 4% of the receivables are not collected and charged to cost.

(ii) Stock-in-trade

These are valued at lower of cost or net realisable, value. This year, cost has been determined by using first in first out formula instead of weighted average which was in use for last many years. There is no reason for change in the cost formula. However, due to the change, profit for the year has increased by Rs. 8 million.

(iii) Fixed Assets

Fixed assets worth less than Rs. 5,000 are not capitalized and charged to cost.

(iv) Other income

In December 2015, Rs. 7 million were received and credited to income for which services are to be rendered in 2016.

Required:

(a) Suggest adjustments, if any, which may be required to ensure that the financial statements present a true and fair view. **(04)**

(b) Identify and briefly describe the accounting concept/principle relevant to each adjustment suggested by you. **(06)**

Q 8. Identify accounting concepts/principles on which the following statements are based and give one example of each: **(05)**

- (i) Expenses are recognized on the basis of a direct association between the costs incurred and the earning of specific items of income.
- (ii) Accounting policies in use are applied from one period to the next.
- (iii) Overstating assets/income and understating liabilities/expenses are avoided.
- (iv) Revenue and other income are recognized when these are earned, irrespective of the date of receipt.
- (v) Any information, omitting or misstating of which could influence a decision of a user of the financial statements, is disclosed.

Q 9. On reviewing the draft financial statements of Aladdin Traders (AT) for the year ended 30 June 2018, following matters have been identified:

- I. Freight-in incurred on merchandise was classified into administration expenses. Last year such cost was charged to cost of sales.
- II. Depreciation on land and building has not been charged due to rising market values.
- III. Cost of improvements and repairing equipment was capitalized to the cost of the equipment.
- IV. A part of the business premises is used by owner for residential purposes. However, total rent and utilities of the premises are charged to expenses.
- V. A leased vehicle has been recorded in the books as non-current asset although the vehicle is registered in the bank's name.
- VI. Sales has been recorded for goods not yet dispatched.

Required:

Identify and briefly describe the accounting concept(s) that has been applied or needs to be considered in each of the above situations. (08)

Answers:

Answer 1:

(i) Payment of creditors by bank overdraft.
(ii) Purchase of machine against cash.
(iii) Creditors paid through bank.
(iv) Cash withdrawal by the proprietor.

Answer 2:

(i) (a) Accounting concept that effects preparation of QT's financial statements for the year ended 30 June 2016 is **'going concern'**.
This means that financial statements are prepared on the assumption that the entity will continue to operate for the foreseeable future and does not intend to go into nor will be forced into liquidation.
(b) After QT's decision to discontinue its operations, QT is no more a going concern. Therefore, as at 30 June 2016, its assets and liabilities should be valued at their estimated disposal value.

(ii) (a) Accounting concept pertaining to this situation is **'true and fair view' (faithful representation)**.
According to this concept, financial statements should give true and fair view / faithful representation of the financial position, financial performance, and changes in financial position of an entity.
(b) Making provisions just to even out the profits is against the true and fair view/faithful representation and should be avoided. Therefore, any provisions made on this basis should be reversed immediately.

Answer 3:

Accounting Concepts:

(i) Going concern
(ii) Business entity
(iii) Historical cost
(iv) Matching/Accrual
(v) Consistency
(vi) Substance over form

Answer 4:

(a) Substance over form:
It is an accounting principle that transactions and other events must be accounted for and presented according to their substance and financial / economic reality instead of according to their legal form.

Example 1: Leased Assets:
In a lease, the lessee obtains title to the assets only at the end of the lease. However, the substance of the transaction is that the lessee obtains use of the asset from the outset of the lease. Thus, we treat the asset as if it was purchased outright at the start.

Example 2: Sale and lease-back agreements:

(b) The matching concept directs the Big Traders to expense the cost of the calculator over the period of three years i.e. Rs. 500 per year.
However, in view of the materiality concept, Big Traders may expense the entire cost of Rs. 1,500 in the year of purchase as it is an insignificant amount for businesses and therefore this treatment would not render the financial statements misleading.

Answer 5:

(i) Completeness
(ii) Materiality
(iii) Business entity concept
(iv) Faithful representation / True and fair view
(v) Matching principle / Accrual concept
(vi) Prudence
(vii) Going concern concept
(viii) Consistency principle

Answer 6:

Accrual basis of accounting:

Under accrual basis of accounting:

- Revenue is recognised when it is earned, irrespective of the date of receipt.
- Expense is recognised in the period in which it is incurred irrespective of the date of payment.

Main advantage of accrual basis of accounting:

The accrual basis of accounting gives a better measurement of profitability than does the cash basis. Because accrual basis matches revenues with expenses that an entity incurred to earned it.

Answer 7:

Sky-link Traders

(a) **Suggested adjustments to ensure that financial statements present a true and fair view:**

(i) Trade receivables:
ST should recognise an allowance for doubtful debts at 4% on year end balance of trade account receivables.

(ii) Stock-in-trade:
As there is no reason for change of the cost formula, ST should determine cost of closing stock-in-trade under weighted average cost formula as it is being followed for last many years.

(iii) Fixed Assets:
According to the matching concept, depreciation is to be charged on a fixed asset over its useful life. However, in view of materiality concept, ST may charge off assets costing less than Rs. 5,000 in the year of purchase as this would not render the financial statements misleading. Therefore, no adjustment is required.

(iv) Other income:
As services are to be performed in 2016 therefore, under the matching concept expenses have not yet been incurred, other income should be reversed and a liability should be recognised in respect of the amount received in advance.

(b) **Concept/principle relevant to each suggested adjustment:**

(i) Prudence/Matching:
Prudence involves allowing for some caution in preparing financial statements, by making reasonable and sensible allowance in order to avoid overstating assets or income and to avoid understating liabilities and expenses.

(ii) Consistency:
The content of the financial statements must be presented consistently from one period to another.

(iii) Materiality:
Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial statements about a specific reporting entity.

(iv) Accrual/matching:
Other income should be recognised in the period when it arises which might not be the same as the period when the cash is received. Income and expenses incurred to earn that income must be reported in the same financial period.

Ans 8.

Accounting concept/principle with examples

S.No.	Accounting Concept/principle	Example(s) [Only one example is required for each concept)
(i)	Matching	• Cost of sales is recorded in the period in which Sales is recorded. • Costs are charged in the period in which benefits are received.
(ii)	Consistency	Use of same cost formula for stock valuation which was used in the previous period.
(iii)	Prudence	Provision for doubtful debts Inventory valuation at lower of cost and net realizable value.
(iv)	Accruals	Purchases are recorded although suppliers are yet to be paid. Sales are recorded although cash their against is yet to be received from the customers.
(v)	Materiality	Fixed assets below a certain limit, are charged to profit and loss account

A 9. 1. **Consistency:**

The contents of financial statements must be presented consistently from one period to another. Therefore, cost of freight-in should be consistently charged to cost of sales rather than operating expenses.

2. **Matching:**

Depreciation is the systematic allocation of the cost of property, plant and equipment over its estimated useful life. Building needs to be depreciated over useful life irrespective of its market value. However, land should not be depreciated because of indefinite useful life.

3. **Capital or Revenue Expenditure (Matching)**

Expenditure made to improve equipment are capitalized while costs of repairs are expensed out.

4. **Business entity/separate entry:**

This concept implies that affairs of a business are to be treated as being quite separate from the non-business activities of its owner(s). Therefore, rent related to residential premises should be treated as drawings instead of business expenses.

5. **Substance over form:**

It is an accounting principle that transactions and other events must be accounted for and presented according to their substance and financial / economic reality instead of according to their legal form. In a lease, the lessee obtains title to the assets only at the end of the lease, if it is written in the agreement. However, the substance of the transaction is that the lessee obtains substantial rights on the asset from the inception of the lease. Thus, we treat the asset as if it was purchased at the start of the lease (means just like a credit purchase).

6. **Accrual concept / Revenue recognition:**

Revenue from sales and other income should be reported in the period in which the income is earned i.e., when the goods are dispatched.

Test Question

Q 10. Following principles are used by ABC Enterprises for preparation of its financial statements:

I. Fixed assets are stated at cost less accumulated depreciation.
II. Items of capital nature, costing less than Rs. 1,000 are charged to cost.
III. Stock-in-trade is valued on the same basis as is being followed for last many years.
IV. Appropriate provision is made for bad and doubtful debts.
V. Sales revenue is recorded on dispatch of goods to customers irrespective of the date of receipt of payment.
VI. Cost of sales is recorded in the same period in which the revenue earned from the sale is recorded.

Required:

Identify and explain the above accounting concepts/principles being followed by ABC Enterprises for preparation of its financial statements.

Ans 10.

i. Historical cost

This is the actual amount of cash paid or received. For example, the historical cost of an item of fixed assets is the amount that was paid to buy it in the past.

ii. Materiality

Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial statements of an entity.

iii. Consistency

The financial statements must be presented consistently from one period to another. The presentation may be changed only if necessary to improve the quality of information presented in terms of its usefulness to the users or if a new rule requires a change.

iv. Prudence

Prudence involves allowing for some caution in preparing financial statements, by making reasonable and sensible allowance in order to avoid overstating assets or income and to avoid understating liabilities and expenses.

v. Accrual basis accounting

Revenue from sales and other income should be reported in the period when income arises (which might not be the same as the period when the cash is received)

vi. Matching concept

The cost of sales in the statement of comprehensive income must be matched with the sales.

Depreciation with Exchange of Assets

Q.1 The following information is available in respect of Fixed assets of MJ Enterprises (MJE):

1) The opening balances of cost and accumulated depreciation of fixed assets as on January 1, 2009 were Rs. 100,000 and Rs. 33,000 respectively.
2) Assets costing Rs. 20,000 were acquired on July 1, 2008. The remaining fixed assets were acquired when MJE commenced business on January 1, 2005. There were no disposals of fixed assets up to January 1, 2009.
3) MJE provides for depreciation on the cost of assets at the rate of 10% per annum using the straight line basis. Depreciation is calculated on a monthly basis.
4) Assets acquired on January 1, 2005 whose net book value on June 30, 2009 was Rs. 2,750 were sold for Rs. 1,500.
5) On July 1, 2009, an asset which was acquired at a cost of Rs. 2,000 when MJE commenced business, was exchanged for a new asset. The balance of the purchase price was settled with a cheque for Rs. 800. The list price of the new asset was Rs. 1,200 (list price means purchase price).
6) On October 1, 2009 MJE transferred to its factory an asset which had been included in its trading stock and which bore a price label of Rs. 15,400 in the showroom. MJE makes a gross profit of 40% of cost, on sale of such assets.

Required:
Prepare the following ledger accounts for the year ended December 31, 2009:
a) Fixed assets
b) Accumulated depreciation
c) Profit/loss on sale of fixed assets (means disposal account)

Q.2 Draft Financial Statements of Asian Talent & Co as on 30 June 2009 reveals followings balances of Plant & Machinery:

Cost	Rs.4, 500,000
Provision for Depreciation	Rs.1, 800,000

The above balances are after the adjustment of following during the year

1) Three Machines were bought on 1st October 2008 each costing Rs.500, 000 for which 60% was paid through cheque and balance is still due. Plant & Machinery account is depreciable @ 10% p.a. on Straight line basis using time proportionate basis.
2) One Machine was sold for Rs.100, 000 at a loss of Rs.250, 000, the Machine was sold .on 1 January 2009 after taking into account Depreciation for the months in use during the reporting period. This Machine was bought on 01-07-2002.

Required:
Prepare plant & Machinery account and provision for Depreciation account for the year ending on 30-06-09.

Q.3 Following information has been extracted from the financial statements of Full Speed Enterprises (FSE) for the year ended 30 June 2013:

	Rupees
Machine -cost	62,501,721
Less: Accumulated Depreciation	(12,576,132)
WDV of Machine	49,925,589

FSE provides depreciation on machines @ 10% per annum on written down values.
Depreciation on addition/deletion is provided in proportion to the period of use.

Other related information is as follows:
(i) On 1 November 2013, a machine which was acquired at a cost of Rs. 850,000 on 1 February 2010 was exchanged for a new machine. The balance was settled with a cheque for Rs. 350,000. The list price of the new machine was Rs. 950,000.
(ii) Two new machines were purchased and installed on 1 February 2014 for Rs. 1,150,000 each.
(iii) On 1 May 2014, another machine was purchased for Rs. 250,000. However, it took one month in its installation therefore it became available for use on 1 June 2014. Cost of installation was Rs. 20,000.
(iv) On 30 November 2013, a machine purchased on 1 February 2011 at a cost of Rs. 1,200,000 was sold for Rs. 700,000.

Required:

Prepare the following ledger accounts for the year ended 30 June 2014:

- Plant and machinery account
- Accumulated depreciation
- Disposal account

Q.4 The following information is available in respect of machines of akaml brothers ;

I. The balance of cost and accumulated depreciation of machine as on 1 January 2017 were Rs. 800,000 and Rs. 333,000 respectively

II. A machine acquired on 1 January 2014 having net book value of Rs. 31,935 on 1 January 2017 was sold for Rs. 34,000 on 30 April 2017. Cost of disposal incurred was Rs. 5,000.

III. On 1 July 2017, a machine was exchanged for a new machine. The balance of the purchase price was paid through a cheque of Rs. 80,000. The list price of the new machine was Rs. 130,000. The old Machine had been acquired at a cost of Rs. 65,000 on 1 October 2015.

IV. Machine are depreciated at 15% per annum using the reducing balance method.

Required:

Prepare the following ledger accounts pertaining to the Machines for the year ended 31 December 2017 :

a) Cost **(03)**

b) Accumulated depreciation **(05)**

c) Gain/ Loss on disposal **(04)**

Q5. Ziakot steel Works provides depreciation on plant and machinery at 20% per annum on diminishing balance method. On 30.06.2014 the balances in the plant and machinery account and accumulated depreciation accounts were Rs. 1,512,000 and Rs. 700,000 respectively.

It was discovered that:

- Cost of installation of plant amounting to Rs. 50,000 incurred on 01.07.2013 had been erroneously charged as repair expense.
- A machine which was purchased on 1 February 2011 for Rs. 600,000 was traded in (means exchanged) on 30 April 2014 for a new machine. The disposal was not recorded and the new machine was capitalized at Rs.620,000 being the net amount paid to supplier. The trade in allowance was agreed at Rs. 150,000.

Depreciation for the year has been correctly calculated and recorded except for the effect of any errors.

Required:

Prepare the adjusted Plant and machinery account and accumulated depreciation account for the year ended 30.06.2014.

A. 1

MJE enterprises

Fixed asset account			
b/d	100,000	Disposal	5,000
Bank	800	Disposal	2,000
Disposal	400		
	1,200		
Purchases (15,400 / 140 x 100)	11,000	c/d	105,200
	112,200		112,200

Accumulated depreciation account			
		b/d	33,000
Disposal	2,250	Depreciation	9,985
Disposal	900		
c/d	39,835		

Disposal account			
Fixed asset	5,000	Cash	1,500
		Acc depreciation	2,250
Fixed asset	2,000	Fixed asset	400
		Acc depreciation	900
		Loss (I/S)	1,950
	7,000		7,000

Workings:

Disposal

Purchase date	01-01-2005
SLM	10% =10year
Disposal date	30-06-2009
WDV	2,750
Period elapsed	4.5 year means 55%
Therefore WDV	55%
Cost	2,750/55*100 = 5,000
Accumulated depreciation	5,000-2,750 = 2,250

Depreciation

(100,000- 5,000-2,000)*10%	9,300
1,200*10%*6/12	60
11,000*10%*3/12	275
5,000*10%*6/12	250
2000*10%*6/12	100
	9,985

A.2

Plant and machinery account (Cost)

		Rupees			Rupees
1-Jul-08	Opening b/d	4,000,000	1-Jan-09	Disposal account	1,000,000
1-Oct-08	Bank (60%)	900,000			
1-Oct-08	Creditors	600,000	30-Jun-09	Balance c/f	4,500,000
		5,500,000			5,500,000

Provision for depreciation account

		Rupees			**Rupees**
1Jan 09	Disposal A/c	650,000		Opening balance (Balancing Fig,)	1,987,500
			1-Jan-09	Dep. Expense (W)	462,500
	Closing balance	1,800,000			
		2,450,000			2,450,000

Workings

Disposal Account

		Rupees			Rupees
1-Oct-09	Cost	1,000,000	1-Oct-09	Provision for depreciation	650,000
			1-Oct-09	Bank	100,000
				Loss on disposal	250,000
		1,000,000			1,000,000

Date of purchase;	01 July 2002
Date of Disposal;	01 January 2009
Total Period;	6 years & 6 months = 6.5 years
Remaining life;	3 years & 6 Months =3.5 years
Cost;	$350,000 \frac{10}{3.5} = 1,000,000$

Depreciation Charge:

Machine sold	1,000,000 x 10% x 6/12	50,000
Machine in use	(4,000,000 – 1,000,000) x 10%	300,000
On additions	1,500,000 x 10% x 9/12	112,500
		462,500

A. 3

Fixed asset account

b/d	62,501,721	Disposal	850,000
New asset in exchange for old	950,000	Disposal	1,200,000
2 @1,150,000 each	2,300,000		
Cash (250,000+20,000)	270,000	c/d	63,971,721

Accumulated depreciation account			
		b/d	12,576,132
Disposal	275,962	Depreciation	5,060,048
Disposal	307,312		
c/d	17,052,905		

Disposal account			
		plant(trade in allow)	600,000
Plant and mach	850,000	Accumulated depreciation	275,962
Plant and mach	1200,000	Cash	700,000
		Accumulated depreciation	307,312
		Loss (I/S)	166,726

W-1

(62,501,721 – 12,576,132)	49,925,589
Less: WDV of disposal	(593,382)
Less: WDV of disposal	(931,500)
Total	48,400,257
Depreciation @10%	4,840,026
+depreciation on disposal	19,794
+ depreciation on disposal	38,812
$950{,}000 * 10\% \frac{8}{12}$	63,333
$2{,}300{,}000 * 10\% \frac{5}{12}$	95,833
$270{,}000 * 10\% \frac{1}{12}$	2,250
Total	5,060,048

W-2:

Cost	850,000
Depreciation @ 10% x 5/12	(35,417)
30 June 2010	814,583
Depreciation @ 10%	(81,458)
30 June 2011	733,125
Depreciation @ 10%	(73,312)
30 June 2012	659,813
Depreciation @ 10%	(65,981)
30 June 2013	593,832
Depreciation @ 10%	(19,794)
Acc depreciation upto disposal	275,962

W-3

Cost	1,200,000
Depreciation @ 10% x 5/12	(50,000)
30 June 2011	1,150,000
Depreciation @ 10%	(115,000)
30 June 2012	1,035,000
Depreciation @ 10%	(103,500)
30 June 2013	931,500
Depreciation @ 10%	(38,812)
Acc depreciation upto disposal	307,312

Answer 4

Machinery Account

1/1/2017	b/d	800,000	30/4/2017	Disposal	65,000
1/7/2017	Disposal	50,000	1/7/2017	Disposal(Exchange) W-1	52,000
1/7/2017	Bank	80,000	31/12/2017	c/d (bal)	813,000
		930,000			930,000

Accumulated Depreciation

Disposal (w-1)	(20,065+1,597)	21,662	b/d	333,000
Disposal (w-2)		15,809	Depreciation	72,918
c/d (bal.)		368,146		
		405,618		405,618

Disposal Account

Machine	52,000	Accumulated depreciation	333,000
Machine	65,000	Cash (34-5)	29,000
		Accumulated depreciation	15,809
		Machine (New)	50,000
		Loss (bal)	529
	117,000		117,000

Working s (w-1) Cost of

Machine sold:

1-1-2014	Cost	100
	@15%	(15)
31-12-2014		85
	@15%	(12.75
31-12-2015		72.25
	@15%	(10.84)
31-12-2016		61.4125

Cost $= \frac{31,935}{61.4125} x\ 100$ = 52,000

Accumulated depreciation on 31 -12-2016 = 52,000 – 31,935 = 20,065

Depreciation charge during the year = 31,935 x 15% x 4/12 = 1,597

(W-2) Machine Exchange:

Cost (1-10-2015)	65,000
Depreciation @ 15% x 3/12	(2,437)
31-12-2015	62,563
Depreciation @ 15%	(9,384)
31-12-2016	53,179
Depreciation @ 15% x 6/12	(3,988)
1-7-2017	49,191

1-7-2017Accumulated depreciation is (65,000 -49,191) = 15,809

(W-3) Depreciation for the year 2017:

Opening WDV (800,000 – 333,000)	467,000
Less : Opening WDV of disposal	(31,935)
Opening WDV of Disposal	(53,179)
	381,886
X 15%	57,283
+Depreciation of disposal	
31,935 x 15% x 4/12	1,597
53,179 15% x 6/12	3,988
+Depreciation on addition	
130,000 x 15% x 6/12	9750
	72,618

A5.

Plant and machinery

Unadjusted balance	1,512,000	Disposal	600,000
Repair	50,000		
Disposal	150,000		
		c/d	1,112,000
	1,712,000		1,712,000

Accumulated depreciation account

		Unadjusted balance	700,000
Depreciation	11,733	Depreciation	10,000
Disposal	306,667	Depreciation (on TIA)	5,000
c/d	396,600		
	715,000		715,000

W 1 cost of installation:

1 .7. 2013

Plant and machinery	50,000	
Repair expense		50,000
Depreciation 10,000		
Accumulated depreciation	10,000	
(50,000 x 20%)		

W 2 machine exchange:

Disposal	600,000	
Machine		600,000
Accumulated depreciation	11,733	
Depreciation		11,733
Accumulated depreciation (50,000+110,000+88,000+58,667)	306,667	
Disposal		306,667

Cost (1.2.2011)	600,000
Depreciation @ 20% x 5/12	(50,000)
30 June 2011	550,000
Depreciation @ 20%	(110,000)
30 June 2012	440,000
Depreciation @ 20%	(88,000)
30 June 2013	352,000
Depreciation @ 20%	(70,400)
30 June 2013	281,600
(70,400 x 2/12)	11,733
(70,400 x 10/12)	58,667

Trade in allowance = cost – cash paid

150,000 = 770,000 -620,000

	Debit	Credit
New machine	150,000	
Disposal		150,000
Depreciation on 150,000 for two months		
150,000 x 20% x 2/12 = 5,000		
Depreciation	5,000	
Accumulated depreciation		5,000

Initial measurement

Property, plant and equipment are initially measured at cost

The cost of an item of property, plant and machinery consists of:

- its purchase price after any trade discounts and rebates have been deducted plus any import taxes or *non-refundable* sales tax; plus
- the directly attributable costs of 'bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management'.

These directly attributable costs may include:

- employee costs (means salary) arising directly from the installation or construction of the asset
- the cost of site preparation
- initial delivery and handling costs
- installation and assembly costs
- testing costs
- professional fees such as architect and surveyor fee.

When the entity has an obligation to dismantle and remove the asset at the end of its life, its initial cost should also include an estimate of the costs of dismantling and removing the asset and restoring the site where it is located.
The cost of a non-current asset cannot include any administration costs or other general overhead costs.

Example: Cost

A company has purchased a large item of plant.

The following costs were incurred.

List price of the machine	1,000,000
Trade discount given	50,000
Delivery cost	100,000
Installation cost	125,000
Cost of site preparation	200,000
Architect's fees	15,000
Administration expense	150,000

Local government officials have granted the company a license to operate the asset on condition that the company will remove the asset and return the site to its former condition at the end of the asset's life.

The company has to recognise a liability of Rs. 250,000 in respect of the expected dismantling cost.

Answer:

The cost of the asset is as follows:

Purchase price of the machine (1,000,000 – 50,000)	950,000
Delivery cost	100,000
Installation cost	125,000
Cost of site preparation	200,000
Architect's fees	15,000
Decommissioning cost	250,000
	1,640,000

When the land is acquired, certain costs are necessary and should be part of the cost of land. These costs include the cost of the land, title and legal fees, site preparation costs like grading and draining and survey costs etc. All of these costs may be considered necessary to get the land ready for its intended use. Some costs are **land improvements**. This asset category includes the cost of parking lots, sidewalks, landscaping, irrigation systems etc. Care must be taken to distinguish land and land improvement costs. Land is considered to have an indefinite life and is not depreciated. Whereas, land improvements do wear out and must be depreciated.

The costs of day-to-day servicing of an asset (means repair cost) are not included in the carrying amount (means capitalized) of the asset but expensed when incurred.

Examples of costs that are not costs of an item of property, plant and equipment are:

- costs of advertising and promotional activities;
- administration and other general overhead costs.
- Interest paid to finance the purchase of property, plant and equipment is expensed.
- The acquisition of new machinery is accompanied by employee training. The normal rule is that training costs are expensed. The logic is that the training attaches to the employee not the machine.
- costs incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity;
- initial operating losses (means business losses); and
- relocating cost.(means the cost of shifting the asset from one place to another after it starts working)

Exception
If a company main business is selling machines then that machine does not classify as property, plant and equipment. The machine manufactured for sale is classified as inventory. The same goes for real estate companies. Their offices are PP&E but the houses they sell are inventory.

Practice question

Q.1 Following information pertains to plant and machinery of Alpha Enterprises (AE):

(i) As at 1 January 2018, balances of cost and accumulated depreciation amounted to Rs. 12,700,000 and Rs. 6,240,000 respectively.

(ii) On 1 April 2018, an old machine having fair value of Rs. 340,000 was exchanged for a new machine. The balance of the purchase price was paid through a cheque of Rs. 680,000. The list price of the new machine was Rs.1,020,000. The old machine had been acquired for Rs. 870,000 on 1 September 2015.

(iii) On 1 February 2018, a plant having a list price of Rs. 10,000,000 was acquired. A trade discount of 5% was allowed on the list price. The plant was ready for use on 1 August 2018 after incurring the following costs:

	Rs. in '000
Freight charges	660
Consultant fees	540
Installation and testing	600
Administration and other general overheads	160
Staff training	120
Opening ceremony	100
	2,180

(iv) On 31 October 2018, another machine was sold for Rs. 334,000. It was acquired on 1 January 2015 and had a net book value of Rs. 512,000 on 1 January 2018. A cost of Rs. 25,000 was incurred on its disposal.

(v) AE depreciates plant and machinery at 20% per annum using the reducing balance method

Required:

Prepare following ledger accounts pertaining to the plant and machinery for the year ended 31 December 2018:

(a) Cost (06)
(b) Accumulated depreciation (06)
(c) Assets disposal (04)

A.1 Alpha Enterprises

Plant and machinery - Cost					
Date	**Description**	**Rs. in '000**	**Date**	**Description**	**Rs. in '000**
1-Jan-2018	Balance	12,700	1-Apr-2018	Assets disposal	870
1-Apr-2018	Bank	680	31-Oct-2018	Assets disposal **(W-2)**	1,000
	Disposal	340			
		1,020			
1-Aug-2018	Cash **(W-4)**	11,300	31-Dec-2018	Balance	23,150
		25,020			**25,020**

Accumulated depreciation - Plant and machinery					
1-Apr-2018	Assets disposal **(W-1)**	376	1-Jan-2018	Balance	6,240
31-Oct-2018	Assets disposal **(W-2)**	573	31-Dec-2018	Depreciation exp. **(W-3)**	2,292
31-Dec-2018	Balance	7,583			
		8,532			**8,532**

Assets disposal - Plant and machinery					
1-Apr-2018	Old machine	870	1-Apr-2018	Acc. depreciation **(W-1)**	376
31-Oct-2018	Cost	1,000	1-Apr-2018	New machine	340
			31-Oct-2018	Acc. depreciation **(W-2)**	573
			31-Oct-2018	Cash (334-25)	309
			31-Dec-2018	Loss on disposal **(P.L)**	272
		1,870			**1,870**

W-1: Accumulated depreciation – Machine exchange		**Rs. in '000**
Depreciation for 2015	870×0.2×4÷12	58
Depreciation for 2016	(870–58)×0.2	162
Depreciation for 2017	(870–58–162)×0.2	130
Accumulated depreciation upto 31-12-2017 (WDV = 870-350=520)		350
Depreciation for 2018	(870–350)×0.2×3÷12	26
		376

W-2:Accumulated depreciation – Machine sold

1-1-2015	100
x 20%	(20)
31-12-2015	80
x 20%	(16)
31-12-2016	64
x 20%	(12.8)
31-12-2017	51.2
512,000/51.2 x 100 Cost = 1,000,000 Acc.dep on 31-12-2017=1,000,000-512,000=488,000 + 512,000 x 20% x 10/12=85,333 Acc.dep on 10-10-2018=573,333	

W-3 : Depreciation for the year

Opening WDV (12,700 – 6,240)	6,460
Less:Opening WDV of Disposal (512 + 520)	(1,032)
	5,428
x 20%	1086
+depreciation on Disposals (26+85)	111
+depreciation on Additions	
1,020 x 20% x 9/12	153
11,300 x 20% x 5/12	942
Total depreciation	2,292

W-4 : Cost of the plant :

		Rs.in "000"
Purchase price of the plant	10,000 × 0.95	9,500
Other directly related cost	(660 + 540 + 600)	1,800
		11,300

Exchange of non monetary asset:

1. If fair value (i.e its cost) of only new asset received is available or is more reliably measureable then measure the new asset at its fair value.
2. If fair value of new asset received as well as fair value of old asset given up both are reliable measureable or only fair value of old asset given up is reliably measureable, then measure the new asset received at fair value of asset given up plus cash paid minus cash received (if any)

Example 1:

Book value of old machine 8,000 (comprising of cost of 12,000 and accumulated depreciation of 4,000).

Fair value of machine given up = 6,000

List price of new machine = 16,000

Trade in allowance for old machine = 9,000

(it may not be the same as fair value of old machine because supplier may be charging an inflated price for his new machine).

Cash paid (16,000 – 9,000) = 7,000

Required:

Prepare accounting entry to record gain / loss on exchange

Answer:

New machine (6,000 + 7,000)	13,000	
Acc. Depreciation	4,000	
Loss on exchange (P&L)	2,000	
Old machine		12,000
Cash		7,000

3. If fair value of both the asset received or given up are not reliably measureable or are not available then measure the new asset at carrying amount of asset given up plus cash paid minus cash received.

Comprehensive Example:

Following information pertains to three exchange transactions relating to fixed assets:

	--------- Rs. in million ---------		
	1	2	3
Cash received/(paid)	1.1	(2.1)	-
Assets given-up:			
Original cost	10.3	12.4	14.5
Book value	6.4	7.3	3.4
Estimated fair value	8.5	6.6	4.6
Assets received:			
Estimated fair value	7.1	9.0	4.1

Additional information:

i. In case of transaction (i), fair values of both assets are reliably measurable.

ii. In case of transaction (ii), fair value of the asset received is clearly more evident.

iii. In case of transaction (iii), fair value of neither asset is reliably measurable.

Required:
Prepare accounting entries in respect of the above exchange transactions. (06)

Answer

(i)

New asset (8.5-1.1)	7.4		
Cash	1.1		
		Old asset	6.4
		Gain (P.L)	2.1

(ii)

New asset	9.0		
Loss (P.L)	0.4		
		Cash	2.1
		Old asset	7.3

(iii)

New asset (3.4+2)	5.4		
		Cash	3.4
		Old asset	2.0

Q. Following information pertains to Rose Enterprises for the year ended 31 December 2017:

(i) Acquisition of land and constructions of a factory building:

Cost of freehold land purchased with old building structure	25,000
Cost of demolition of the old building structure	1,500
Proceeds from sale of scrap of the old building	250
Fee paid to ABC Architects for site plan and drawings	800
Advance paid to Quality Construction (QC) for construction of the building	6,000
Further payment to QC	35,000

(ii) Acquisition and installation of new plant:

	Rs. In '000'
25% cost of the plant paid in advance	4,000
Transportation and import charges	1,250
Cost of installation	400

(iii) Other information:

- Cost of freehold land includes property tax for 2017-18 and transfer fee of Rs. 120,000 and Rs. 850,000 respectively.
- Factory building was available for use from 1 July 2017. The final invoice of Rs. 19,000,000 is still unpaid.
- Transportation and import charges of the plant include annual fire insurance premium and insurance in-transit of Rs. 350,000 and Rs. 60,000 respectively.
- The plant started operations on 1 August 2017. Remaining amount was paid on 31 August 2017.
- Old plant was sold on 1 September 2017 at its written down value plus 20%. The plant was purchased on 1 April 2015 at a cost of Rs. 8,500,000.
- Building and plant are depreciated at the rate of 5% and 10% respectively on reducing balance method.

Required:

(a) Pass journal entry to record disposal of the old plant. **(03)**

(b) Determine written down value of the fixed assets as at 31 December 2017. **(09)**

A. 2 Rose limited

(a) Journal entry for disposal of old plant:

		Debit	Credit
		-------Rs. In '000'-------	
Bank/cash/receivable	**(8,500 – 1,896) x 1.2**	7,925	
Accumulated depreciation	**(W-1)**	1,896	
Fixed assets (Plant)			8,500
Gain on disposal **(Balancing Figure)**			1,321

(W-1) Accumulated depreciation:

		Rs. In '000'
From 1 April to 31 December 2015	**(8,500 x 0.1 x 9/12)**	638
For the year ended 31 December 2016	**(8,500 – 638) x 0.1**	786
From 1 January to 31 August 2017	**(8,500 – 638 – 786) x 0.1 x 8/12**	472
		1,896

(b) WDV as at 31 December 2017

		Freehold land	Building	Plant
		-----------Rs. In '000'-----------		
Costs				
Purchase price		25,000		
Property tax for the year 2017-18		(120)		
Transfer fee		-		
Demolition of old building		1,500		
Proceeds from sale of building scrap		(250)		
Architect fee paid to ABC consultant			800	
25% Advance paid to QC			6,000	
Further payment			35,000	
Final invoice under process for payment			19,000	
Advance paid for the plant				4,000
Transportation and import charges				1,250
Fire insurance premium				(350)
Insurance in transit				-
Installation charges				400
Remaining cost of plant	(4,000÷0.25-4,000)			12,000
Cost to be capitalized		**26,130**	**60,800**	**17,300**
Depreciation for 2017				
- Land				
- Building	**(60,800 × 0.05 × 6 ÷ 12)**		(1,520)	
- Plant	**(60,800 × 0.05 × 6 ÷ 12)**			(721)
WDV of fixed assets as at 31 December 2017		**26,130**	**59,280**	**16,579**

QUESTIONS

INVENTORY [Extra Practice questions]

1.HM

HM has following products in hand as at 31st December 2001, the relevant information is as follows:

Product	Cost	Estimated Selling Price (ESP)	Estimated Selling cost (ESC)	Estimated Cost to complete sale (ECCS)	Ratio of Credit sales based on past experience	Recovery cost	Bad debt expense
A	100,000	20% Markup	5% of ESP	15% of Cost	60%	1% of cost	5%
B	270,000	15% margin	3% of ESP	7% of Cost	40%	1% of cost	3%
C	830,000	25% Markup	6% of ESP	20% of Cost	20%	1% of cost	2%
D	690,000	30% Markup	8% of ESP	22% of Cost	0%	0%	0%
E	500,000	50% margin	10% of ESP	2% of Cost	100%	2% of cost	10%

Required:
Based on above information, calculate the value of inventories to be shown in financial statements and NRV loss to be booked, if any.
Note: recovery cost and bad debts are not expenses necessary to make sale.

2 MARFANI & CO.

Marfani&Co. has purchased goods costing Rs.100,000 at the start of 2001,however the goods remain unsold for 5 years and the estimated selling prices and cost of realization (means expenses necessary to make sale) were as follows as at each year end:

	Est. selling price	**Est. selling expenses**
01-Jan-01	220,000	20,000
31-Dec-01	135,000	15,000
31-Dec-02	100,000	10,000
31-Dec-03	90,000	15,000
31-Dec-04	110,000	15,000
31-Dec-05	120,000	10,000

Required
As at each year end, calculate the value at which inventory should be reported in the financial statements of Marfani&Co. and NRV loss/reversal of any write down for each accounting year assuming year end is 31st December

3. CHEESECAKE LIMITED

Part (a):

Goods purchased to be resold, cost of Rs.10,000 have been damaged. At the balance sheet date their replacement buying price is Rs.9,000. They can be sold in the normal course of business for Rs.14000, provided Rs.4500 is spent on rectifying the damage.

Required

At what amount should the stock be valued?

Part (b):

Cheesecake Limited produces cheese cakes for the local market. At its financial year ended 30 September 2005, it had raw materials of Rs. 320 000 on hand. Current replacement cost (means purchase cost) is 300,000 (which is NRV for the raw material).It is expected that the cost to convert the raw materials into finished cheese cakes is Rs.80 000.

Required

Calculate the net realisable value of the raw materials and journalise the write-down (means loss), if any, assuming that, once converted into the finished cheese cakes, the total inventory of cheese cakes would have a:

i) sales value of Rs. 480 000, where related selling costs would be Rs. 40 000.
ii) sales value of Rs. 400 000, where related selling costs would be Rs. 40 000.

4. M/S MOLA BAKHSH

Following information relates to M/S Mola Bakhsh

Product A

		Units		Rate/unit
01-Jan-16	Opening stock	40 units	@	400
02-Jan-16	Purchases	100units	@	500
03-Jan-16	sales	50units	@	1000
04-Jan-16	sales	10units	@	1500
05-Jan-16	Purchases	200units	@	300
06-Jan-16	Purchases	300units	@	700
07-Jan-16	sales	200units	@	1200
08-Jan-16	sales return	100 units	@	1200
09-Jan-16	purchases	200units	@	400

10-Jan-16 Purchase return were 100 units of purchases on 9 jan 2016

11-Jan-16 Shortage 10 units

12-Jan-16 Drawings 5 units

At the end of the month the estimated Selling price of the product A was Rs.300 and the cost of realization (means selling expenses) was Rs.150

Required

Calculate the value of closing stock and cost of sales under Perpetual system by using

- **Weighted average**
- **FIFO**

ANSWERS

1 HM

Product	Cost	Net Realizable value Estimated Selling Price (ESP)	Estimated Selling cost (ESC)	Estimated Cost to complete sale (ECCS)	Net Realizable Value	Value to be shown in Financial Statements	NRV Loss
A	100,000	120,000	6,000	15,000	99,000	99,000	1,000
B	270,000	317,647	9,529	18,900	289,218	270,000	-
C	830,000	1,037,500	62,250	166,000	809,250	809,250	20,750
D	690,000	897,000	71,760	151,800	673,440	673,440	16,560
E	500,000	1,000,000	100,000	10,000	890,000	500,000	-
			Total			2,351,690	38,310

2 MARFANI & CO.

	Cost	Net Realizable Value ESP	ECR	NRV	Value to be shown in Financial Statements	NRV (Loss)/Reversal
01-Jan-01	100,000	220,000	20,000	200,000	100,000	-
31-Dec-01	100,000	135,000	15,000	120,000	100,000	-
31-Dec-02	100,000	100,000	10,000	90,000	90,000	(10,000)
31-Dec-03	100,000	90,000	15,000	75,000	75,000	(15,000)
31-Dec-04	100,000	110,000	15,000	95,000	95,000	20,000
31-Dec-05	100,000	120,000	10,000	110,000	100,000	5,000

3.

Part (a):

Cost	10,000
NRV	
Est. Selling price	14,000
Est. Selling expenses	(4,500)
	9,500
Lower	9,500
NRV Loss	500

Part b (i):

	cost	NRV	Value
Raw Material	320,000	300,000	320,000*
*Finished Goods (320000+80000)	400,000	440,000 (480000-40000)	400,000

*it is just a working to find the loss of raw material on the basis of relevant finished goods.

Note: raw material loss is only recorded if the related finished goods are expected to be sold below cost.

	Cost	NRV	Value	NRV Loss
RM	320,000	300,000	300,000	20,000
*Finished Goods (320000+80000)	400,000	360,000	360,000	

*it is just a working to find the loss of raw material on the basis of relevant finished goods.

Entry of loss:
If periodic inventory system then no entry is required.
If perpetual inventory system

Cost of sales	**20,000**	
Inventory-RM		**20,000**

4. M/S MOLA BAKHSH

Product A

Perpetual System (Weighted Average)

Date	Purchases/Inflows			Cost of Sales/Outflows			Stock balance		
	Unit	Rate	Amount	Unit	Rate	Amount	Unit	Rate	Amount
01-Jan-16							40	400	16,000
02-Jan-16	100	500	50,000				140	471	66,000
03-Jan-16				50	471	23,571	90	471	42,429
04-Jan-16				10	471	4,714	80	471	37,714
05-Jan-16	200	300	60,000				280	349	97,714
06-Jan-16	300	700	210,000				580	531	307,714
07-Jan-16				200	531	106,108	380	531	201,606
08-Jan-16				(100)	531	(53,054)	480	531	254,660
09-Jan-16	200	400	80,000				680	492	334,660
10-Jan-16	(100)	400	(40,000)				580	508	294,660
11-Jan-16	(10)	508	(5,080)				570	508	289,580
12-Jan-16	(5)	508	(2,540)				**565**	**508**	**287,040**
			352,380			**81,339**			

Valuation of stock

cost	287,040	
NRV	84,750	(300-150)*565
Value	84,750	
NRV loss	202,290	

Perpetual System (FIFO)

Date	Purchases/Inflows			Cost of Sales/Outflows			Stock balance		
	Unit	Rate	Amount	Unit	Rate	Amount	Unit	Rate	Amount
01-Jan-16							40	400	16,000
02-Jan-16	100	500	50,000				40 100	400 500	16,000 50,000
03-Jan-16				40	400	16,000			
				10	500	5,000	90	500	45,000
04-Jan-16				10	500	5,000	80	500	40,000
05-Jan-16	200	300	60,000				80 200	500 300	40,000 60,000
06-Jan-16	300	700	210,000				80 200 300	500 300 700	40,000 60,000 210,000
07-Jan-16				80	500	40,000			
				120	300	36,000	80 300	300 700	24,000 210,000
08-Jan-16				(80)	500	(40,000)			
				(20)	300	(6,000)	80 100 300	500 300 700	40,000 30,000 210,000
09-Jan-16	200	400	80,000				80 100 300 200	500 300 700 400	40,000 30,000 210,000 80,000
10-Jan-16	(100)	400	(40,000)				80 100 300	500 300 700	40,000 30,000 210,000
							100	400	40,000
11-Jan-16	(10)	500	(5,000)				70 100 300 100	500 300 700 400	35,000 30,000 210,000 40,000
12-Jan-16	(5)	500	(2,500)				65 100 300 100	500 300 700 400	32,500 30,000 210,000 40,000
			352,500			**56,000**	**565**		**312,500**

Valuation of stock

Cost	312,500	
NRV	84,750	(300-150)*565
Value	84,750	
NRV loss	227,750	

ACCRUALS AND PREPAYMENTS

Question-1

Mr. Amjad has hired a property on rent from Mr. Sameer. The details are given below:

	Per month
January 06 – June 06	500
July 06 – December 06	1,000
January 07 – June 07	1,500
July 07 – December 07	2,000
January 2008 onwards	2,000

- Rent for January 2006 – June 2006 was paid on June 30, 2006.
- Rent for July 2006 – September 30, 2006 was paid on September 30, 2006.
- Rent for October 2006 – June 30, 2007 was paid on June 30, 2007.
- Rent for July 2007 – March 31, 2008 was paid on July 1, 2007.
- Year end is December 31.

Required:

a) Calculate rent expense of Mr. Amjad for the year ended December 2006 and 2007?

b) Also calculate rental income of Mr. Sameer for the year ended December 2006 and 2007?

Question-2

From the information given below, you are required;

a) To calculate the charges to the profit and loss account for the year ended 30 June 2004 in respect of rent, rates and insurance;

b) To state the amount of accrual or prepayment for rent, rates and insurance as at 30 June 2004.

The accruals and prepayments as at 30 June 2003 were as follows:

	Rs.
Rent accrued	2,000
Rates prepaid	1,500
Insurance prepaid	1,800

Payments made during the year ended 30 June 2004 were as follows:

2003		Rs.
10 August	Rent, three months to 31, July 2003 (1,000 x 3)	3,000
26 October	Insurance, one year to 31, October 2004 (500 x 12)	6,000
2 November	Rates, six months to 31, March 2004	3,500
12 December	Rent, four months to 30 November 2003 (1000 x 4)	4,000
2004		
17 April	Rent, four months to 31, March 2004	4,000
9 May	Rates, six months to 30 September 2004	3,500

Concept of combined Ledgers:

3. BONES

Bones owns various properties which he rents; some tenants pay in advance, some in arrears. Similarly with his various borrowings the interest is paid in arrears and in advance.

During 2013 rent collected was Rs.229,500 and interest charged to the statement of comprehensive income was Rs.52,500.

Rents receivable and paid in advance together with amounts of interest prepaid and payable at the statement of financial position dates were as follows.

	31 December	
	2012	2013
	Rs.	Rs.
Rents owed by tenants	34,200	40,500
Rents prepaid by tenants	20,700	15,300
Prepaid interest	3,500	5,600
Interest payable	9,800	7,000

Required:

Write up the rent income account and the interest expense account for the year ended 31 December 2013.

4.

Waqas Estates has purchased a number of different properties over the years by obtaining variety of loans from banks. Some of the interest on loans is paid in arrears and some in advance. Further, these properties are rented out to tenants who pay their dues in advance and some in arrears.

The opening and closing balances of rentals and interest are as follows:

	31st July 2004	31st July 2005
Interest payable	120,000	145,000
Interest prepaid	80,000	64,000
Rent due from tenants	150,000	190,000
Rental received in advance	30,000	25,000

During the year to July 31, 2005 the amount of interest charged to profit and loss account was Rs. 560,000 and the cash collected from rentals was Rs. 1,160,000.

You are required to write up the interest expense account and rental income account for the year ended on July 31, 2005.

5.

Mr. Aneel made the following rent payments during 2001.

- Rs. 9,000 on March 31, 2001 for the six months ended 31 March 2001.
- Rs. 10,000 on September 30, 2001 for the six months ended 30 September 2001.
- Rs. 11,200 on October 1, 2001 for the year ended 30 September 2002.

Calculate charge to the income statement for rent for the year ended 31 December 2001? Show Workings.

Answers:

Answer No. 1

(a)

Rent Expense Account 2006

	Rs.		Rs.
30-06-06 Cash (500×6)	3,000		
30-06-06 Cash (1,000×3)	3,000		
30-06-06 Rent Payable (1,000×3)	3,000	c/d (I/S)	9,000
	9,000		**9,000**

Rent Payable

	Rs.		Rs.
		b/d	--
c/d	3,000	Rent Expense	3,000
	3,000		**3,000**

(b)

Rent Expense Account 2007

	Rs.		Rs.
30-06-06 Cash (1,500×6)	9,000		
31-12-06 Prepaid (2,000×6)	12,000	c/d (I/S)	21,000
	21,000		**21,000**

Prepaid Rent

	Rs.		Rs.
1-7-06 Cash (2,000 x 9)	18000	Rent Exp (2,000 x 6)	12,000
		c/d	6,000
	3,000		**3,000**

(c)

Rent Income Account 2006

	Rs.		Rs.
		30-06-06 Cash	3,000
		30-09-06 Cash	3,000
c/d (I/S)	9,000	31-12-06 Receivable	3,000
	9,000		**9,000**

Rent Receivable

	Rs.		Rs.
b/d	--		
Rent Income	3,000	c/d	3,000
	3,000		**3,000**

(d)

Rent Income Account 2007

	Rs.		Rs.
		30-06-06 Cash	9,000
c/d	21,000	31-12-06 Advance	12,000
	9,000		**9,000**

Unearned Rent

	Rs.		Rs.
Rent Income	12,000	01-07-06 Cash	18,000
c/d	6,000		
	18,000		**18,000**

Answer No. 2

(a)

Rent Payable Account 2003

	Rs.		Rs.
10-08-03 Cash	3,000	b/d	2,000
12-12-03 Cash	4,000	Rent expense (1,000×12)	12,000
17-04-04 Cash	4,000		
c/d $\left(\frac{4,000}{4} \times 3\right)$	3,000		
	14,000		**14,000**

Rent Expense Account

	Rs.		Rs.
Rent Payable	12,000		
		c/d (I/S)	12,000
	12,000		**12,000**

Prepaid Rates Account

	Rs.		Rs.
b/d	1,500	Rates Expense	6,750
12-11-03 Cash	3,500		
09-05-04 Cash	3,500	c/d $\left(\frac{3,500}{6} \times 3\right)$	1,750
	8,500		**8,500**

Rates Expense Account

	Rs.		Rs.
Prepaid Rates	6,750		
		c/d (I/S)	6,750
	6,750		**6,750**

Prepaid Insurance Account

	Rs.		Rs.
b/d	1,800	Insurance Expense	5,800
26-10 Cash	6,000		
		c/d $\left(\frac{6,000}{12} \times 4\right)$	2,000
	7,800		**7,800**

Insurance Expense Account

	Rs.		Rs.
Prepaid insurance	5,800		
		c/d (I/S)	5,800
	6,750		**6,750**

(b) The accrual or prepayment for each expense can be summarized as follows:

As at June 30, 2004:

	Rs.
Rent Payable	3,000
Rates Prepaid	1,750
Insurance Prepaid	2,000

3. BONES

A

Rent receivable + Un earned rent

2013		**Rs.**			**Rs.**
1 Jan	Accrued income Reversal	34,200	1 Jan	Deferred income reversal	20,700
	Statement of Comprehensive Income (calculated as a balancing figure)	**241,200**		Cash	229,500
31 Dec	Deferred income	15,300	31 Dec	Accrued income	40,500
		290,700			290,700
1 Jan	Accrued income Reversal	40,500	1 Jan	Deferred income reversal	15,300

B

Interest payable + Prepaid interest

2013		Rs.			Rs.
1 Jan	Prepayment Reversal	3,500	1 Jan	Accrual reversal	9,800
	Bank (calculated as a balancing figure)	**57,400**		Statement of comprehensive income	52,500
31 Dec	Accrual	7,000	31 Dec	Prepayment	5,600
		67,900			67,900
1 Jan	Prepayment Reversal	5,600	1 Jan	Deferred income reversal	7,000

Answer No. 4

(i) **Interest Expense Payable / Interest Expense Prepaid Accounts**

	Rs.		**Rs.**
b/d	80,000	b/d payable	120,000
31-07 Cash	519,000		
		Interest Expense	560,000
c/d	145,000	c/d	64,000
	602,500		**602,500**

(ii) **Rental Income Receivable / Advance Income Accounts**

	Rs.		Rs.
b/d	150,000	b/d	30,000
		Cash	1,160,000
Rent Income	$\boxed{1,205,000}$		
c/d	25,000	c/d	190,000
	1,380,000		**1,380,000**

Answer No. 5

Rent Payable Account

	Rs.		Rs.
31-03-2001 Cash	9,000	b/d $\left(\frac{9,000}{6} \times 3\right)$	4,500
30-09-2001 Cash	10,000	Rent Expense	$\boxed{17,300}$
01-10-2001 Cash	11,200		
		c/d $\left(\frac{11,200}{12} \times 9\right)$	8,400
	30,200		**30,200**

Extra practice questions:

Q. The details of two office buildings acquired on rent by Ninja Enterprises (NE) are as follows:

(i) On 1 April 2016, Building I was acquired on annual rent of Rs. 2,400,000. Effective from 1 October 2017 the rent was increased by 20%. NE pays rent on half yearly basis in advance.

(ii) On 1 September 2016, Building II was acquired on annual rent of Rs. 900,000. Payments were made on quarterly basis in advance. However, the quarterly payment due on 1 December 2017 was made on 15 January 2018.

NE's financial year ends on 31 December each year.

Required:
Prepare rent expense account for the year ended 31 December 2016 and 2017. (05)

Solution:
Ninja Enterprises:

Prepaid rent expense 2016

Date	Description	Rs.in '000'	Date	Description	Rs. In '000'
1-april-16	Cash – B1 (2,400/2)	1,200	31-dec-16	Expense – B1 (1,200+1,200/6 x 3)	1,800
1-sep-16	Cash – B2 (900/4)	225	31-dec-16	Expense – B2 (225+225/3 x 1)	300
1-oct-16	Cash – B1 (2,400/2)	1,200	31-dec-16	Closing prepaid – B1 (1,200/6 x 3)	600
1-dec-16	Cash – B2 (900/4)	225	31-dec-16	Closing prepaid – B2 (225/3 x 2)	150
		2,850			**2,850**

Rent expense account-2016

[B 1] Prepaid expense	1,800		
[B 2] Prepaid expense	300		
		c/d [I/S]	2,100
	2,100		**2,100**

Prepaid rent expense – 2017

Date	Particulars	Rs in '000'	Date	Particulars	Rs in '000'
1-jan-17	Opening prepaid-B1	600	31-dec-17	Expense – B1 (600+1,200+1,440/6 x 3)	2,520
1-jan-17	Opening prepaid-B2	150	31-dec-17	Expense – B2 (150+225+225+225+225/3 x 1)	900
1-March-17	Cash-B2 (900/4)	225	31-dec-17	Closing prepaid-B1 (1.440/6 x 3)	720
1-april-17	Cash – B1 (2,400/2)	1,200			
1-june-17	Cash – B2 (900/4)	225			
1-sep-17	Cash – B2 (900/4)	225			
1-oct-17	Cash – B1 (1,200 x 1.2)	1,440			
31-dec-17	Closing accrued-B2 (225/3 X 1)	75			
		4,140			**4,140**

Rent expense A/c-2017

[B 1] Prepaid expense	2,250		
[B 2] Prepaid expense	900		
		c/d [I/S]	3,420
	3,420		**3,420**

Q.1 Shangrila Enterprises (SE) expanded its production facility by installing a plant in 2019. Following information pertains to the plant:

(i) Two vendors A and B submitted their bid prices of Rs. 750 million and Rs. 800 million respectively. Due to better quality, vendor B was selected and after negotiations, price of the plant was finalized at Rs. 780 million.

(ii) The acquisition of the new plant was financed by selling an old plant having book value of Rs. 170 million for Rs. 140 million and remaining amount was arranged by selling investments held by SE.

(iii) Arrival of the plant was originally scheduled on 31 March 2019 at a freight of Rs. 3.5 million. However, the arrival date was rescheduled to 31 January 2019 by paying additional freight of Rs. 1.5 million. While transporting, the plant was slightly damaged and repaired at a cost of Rs. 2 million.

(iv) Site preparation work was completed at a cost of Rs. 5.8 million. This cost includes Rs. 1.2 million for demolition and reconstruction of the existing building structure.

(v) Installation work was carried out during the month of February 2019 at a cost of Rs. 5 million.

(vi) The plant was customized by altering some parts at a cost of Rs. 12 million. The alteration slows down the production process but is necessary to align the plant with existing production process.

(vii) On 1 March 2019, safety equipment for the use of staff operating the plant were purchased at a cost of Rs. 10 million. Expected useful life of the safety equipment is 5 years.

(viii) The plant was available for use on 1 May 2019 but due to unavailability of the required raw material, commercial production was delayed till 1 June 2019.

(ix) Residual values of the plant at the end of its useful life and economic life of 20 years and 25 years are estimated at Rs. 100 million and Rs. 40 million respectively.

Required:
Compute book value of the plant as at 31 December 2019. **(08)**
(Items ignored while computing cost of the plant should be mentioned as zero)

Q.2

IAS 1 'Presentation of Financial Statements' requires an entity to present an analysis of expenses recognised in profit or loss using a classification based on either their nature or their function within the entity, whichever provides information that is reliable and more relevant.

Required:
Prepare formats of statement of profit or loss giving analysis of expenses by their:

(a) nature **(03)**
(b) function **(03)**

Question 3

Q.3 Following information pertains to Paristan Brothers for the month of January 2020:

(i) Business travel expenses amounted to Rs. 85,000 were paid by the owner from his personal bank account.

(ii) A payment of Rs. 45,000 was made for repair of owner's personal vehicle.

(iii) A laptop costing Rs. 250,000 and having book value of Rs. 60,000 was sold for Rs. 100,000 on cash.

(iv) Tasnim, a creditor having balance of Rs. 1,500,000 has been admitted to the partnership. The balance payable is to be treated as his capital.

(v) Goods costing Rs. 180,000 were sold to the owner of the office building against office rent of Rs. 210,000 for the month of January 2020.

(vi) A debtor who was declared bankrupt, has paid Rs. 400,000 (i.e. 50% of the balance due) in full and final settlement. A specific provision at 60% of the balance due had already been made.

Required:

Show the effects, if any, of each of the above information in the form of accounting equation. **(08)**

Q.4 Select the most appropriate answer from the options available for each of the following Multiple Choice Questions (MCQs).

(i) 'Allowance for doubtful debts' account is:

(a) liability account (b) asset account
(c) contra asset account (d) expense account **(01)**

(ii) Which of the following does not require journal entry in periodic inventory method?

(a) Abnormal loss (b) Goods returned by a supplier
(c) Closing inventory (d) Normal loss **(01)**

(iii) For reconciling bank balances, unpresented cheques should be:

(a) added to balance of bank statement **and** deducted from balance of cash book
(b) deducted from balance of bank statement **or** added to balance of cash book
(c) deducted from balance of bank statement **and** added to balance of cash book
(d) added to balance of bank statement **or** deducted from balance of cash book **(01)**

(iv) Which of the following statement(s) is/are correct?

(I) Higher closing prepaid balance than previous year means that payment for the year exceeds the expense for the year.

(II) Higher closing accrued income balance than previous year means that receipt for the year exceeds the income for the year.

(a) Only (I) is correct (b) Only (II) is correct
(c) Both are correct (d) None is correct **(01)**

(v) Rent amounts totaling Rs. 150,000 were received during the year ended 31 December 2019. In this respect, opening and closing balances are as under:

	31 Dec 2019	**31 Dec 2018**
	---------- Rupees ----------	
Unearned rent	16,000	10,000
Rent receivable	13,000	17,000

What should be the rent income for the year ended 31 December 2019?

(a) Rs. 144,000 (b) Rs. 152,000 (c) Rs. 148,000 (d) Rs. 140,000 **(02)**

(vi) Office supplies purchased were mistakenly debited to Purchases account. This type of error is called:

(a) error of omission (b) compensating error
(c) error of principle (d) error of transposition

(01)

(vii) A transaction not recorded in any other books of original entry is recorded in:

(a) Sales day book (b) Purchases day book
(c) General journal (d) Cash book

(01)

(viii) On 1 February 2019, a loan of Rs. 6,000,000 was taken from a bank for acquisition of an office building. A portion of the building was rented out on 1 August 2019 at a monthly rent of Rs. 45,000. Interest is payable at 15% per annum on 31 January each year and rent is received half yearly in advance.

What amounts of interest payable and unearned rent should be shown in the statement of financial position as on 31 December 2019?

(a) Interest payable Rs. 900,000; Unearned rent Rs. 270,000
(b) Interest payable Rs. 825,000; Unearned rent Rs. 45,000
(c) Interest payable Rs. 450,000; Unearned rent Rs. 45,000
(d) Interest payable Rs. 825.000; Unearned rent Rs. 250,000 **(02)**

(ix) An entity acquired laptops in exchange of desktops which have carrying amount of Rs. 450,000 and fair value of Rs. 300,000 at the date of exchange. The list price of the laptops acquired is Rs. 600,000. The entity is also required to pay cash of Rs. 275,000 in this exchange transaction.

The laptops should be initially recognized at:

(a) Rs. 300,000 (b) Rs. 575,000 (c) Rs. 450,000 (d) Rs. 600,000 **(01)**

Q.5 Kallar Traders (KT) deals in various consumer products. KT follows perpetual inventory system and uses first-in-first-out (FIFO) method to measure cost of its inventory. Following information for the month of January 2020 pertains to one of its products Beta:

Date	Description
01-Jan	Opening inventory: 2,800 units @Rs. 140,000 1,200 units @ Rs. 62,400
03-Jan	Purchased 3,000 units on cash having a list price of Rs. 60 per unit at a trade discount of 5%.
08-Jan	Sold 2,900 units on 30 days' credit for Rs. 266,800 subject to 2% discount on payment within 10 days.
15-Jan	Sold 1,800 units on credit at a list price amounted to Rs. 171,000 and allowed a discount thereon at 5%.
20-Jan	Returned 500 damaged units purchased on 3 January 2020. The return amount was set-off against balance payable to the supplier.
25-Jan	Purchased 3,000 units for Rs. 174,000 against issuance of a post-dated cheque.
30-Jan	Purchased 2,000 units on credit for Rs. 120,000. These units were collected by KT's transporter on 30 January 2020 and received at warehouse on 3 February 2020.

As per physical inventory count carried out on 31 January 2020:

- 100 units were found expired and can be sold as scrap at Rs. 20 per unit; and
- 600 units were found short and it was determined that these units were stolen by employee who left the job.

Required:

(a) Prepare inventory ledger card for product Beta for the month of January 2020. **(08)**

(b) Prepare accounting entries from the above information. ***(Narrations are not required)*** **(07)**

Question 6

Following information pertains to Zahrba Stationers (ZS) for the month of January 2020:

PURCHASES DAY BOOK		
Date	**Name of supplier**	**Rs. in '000**
06-Jan	Satpara & Co. (SC)	1,500
17-Jan	Ravi Traders (RT)	1,714
28-Jan	Balistan Brothers (BB)	856
		4,070

SALES DAY BOOK		
Date	**Name of customer**	**Rs. in '000**
02-Jan	Skardu & Sons (SS)	1,800
04-Jan	Gilgit Limited (GL)	2,000
25-Jan	Keenjhar Enterprises (KE)	1,137
		4,937

CASH BOOK							
Date	**Description**	**Cash**	**Bank**	**Date**	**Description**	**Cash**	**Bank**
		--- Rs. in '000 ---				**--- Rs. in '000 ---**	
01-Jan	Balance	110	-	01-Jan	Balance	-	180
02-Jan	Sales	290	-	05-Jan	Purchases	250	-
08-Jan	GL - net of 5% discount	-	1,900	09-Jan	SC - net of 4% discount	-	1,440
10-Jan	SS	-	1,590	12-Jan	Utility bills	98	-
18-Jan	Scrap sale		25	16-Jan	Petty cash	-	50
20-Jan	Bank	200	-	20-Jan	Cash	-	200
26-Jan	Sales	295	-	25-Jan	Repair & maintenance	67	-
				27-Jan	Long-term-loan	-	100
				28-Jan	RT	-	1,378
				31-Jan	Balance	**480**	**167**
		895	**3,515**			**895**	**3,515**

Additional information

(i) The petty cash fund was established during the month. As at 31 January 2020 petty cash balance in hand was Rs. 20,000.

(ii) Repair and maintenance payment includes Rs. 25,000 paid for repair of owner's premises.

(iii) Payment of loan amount includes interest of Rs. 15,000.

(iv) The cheque issued to RT was presented to the bank in February 2020.

(v) On 29 January 2020, goods costing Rs. 100,000 purchased from BB were found damaged and returned.

(vi) A part of goods sold on cash to Haleji & Sons on 26 January 2020 for Rs. 70,000 were returned on 31 January 2020 and the amount due was paid on 4 February 2020.

(vii) Other assets and liabilities as at 1 January 2020, are as under:

	Rs. in '000
Fixed assets – net (Cost Rs. 1,600,000)	1,254
Trade debtors	2,423
Inventory	850
Trade creditors	1,800
Long-term-loan	800

Required:

Prepare trial balance for the month ended 31 January 2020. ***(Preparation of ledger accounts is not necessary)(15)***

Q.7

Hanna Traders (HT) is a partnership with two partners A and Zee. Following is the summarized trial balance of HT for the year ended 31 December 2019:

Rs. in million

Description	Debit	Description	Credit
Property, plant and equipment	140	Accumulated depreciation	64
Inventories – 1 Jan 2019	35	Trade payables	30
Trade receivables	48	Other payables and accruals	8
Cash and bank balances	3	Capital account – A	67
Prepayments	6	Capital account – Zee	45
Other receivables	4	Current account – Zee	2
Provision for doubtful receivables	3	Sales	315
Purchases	170	Other income	6
Import duties	39		
Returns	7		
Freight in	5		
Operating expenses	52		
Financial charges	5		
Depreciation expense	16		
Current account – A	4		
	537		**537**

Additional information:

(i) Physical inventories as at 31 December 2019 were valued at Rs. 30 million.

(ii) Goods costing Rs. 3 million were issued to A but not recorded. A informed that:

- goods costing Rs. 2 million were distributed to potential customers as samples; and
- goods costing Rs. 1 million were gifted to one of his friends.

(iii) Sales commission of Rs. 8 million was paid to Zee during the year which was charged to operating expenses.

(iv) Operating expenses include insurance premium of Rs. 4 million that pertained to an insurance policy expiring on 31 March 2020.

(v) On 1 August 2019, Rs. 6 million was received being 50% advance payment against a maintenance contract valid up to 31 March 2020. Remaining amount is due on completion of the contract. The amount received was credited to other payables.

(vi) Due to a calculation error, prepaid rent has been over recorded by Rs. 2 million.

(vii) Rs. 2 million received in full and final settlement of a previously written off balance of Rs. 5 million, was credited to trade receivables. HT maintains provision for doubtful receivables at 4% of the year-end balance.

(viii) A fully depreciated machine costing Rs. 28 million was sold for Rs. 10 million through an agent who is entitled for a sale commission of 5%. The sale proceeds was received on 20 January 2020. Nothing has been recorded in this respect.

Under the partnership agreement:

(i) A is entitled for a monthly salary of Rs. 1 million whereas Zee is entitled for 6% commission on net sales.

(ii) Remaining profit would be shared by A and Zee in the ratio of 3:2 respectively.

(iii) To expand the business, 20% of appropriated profits is transferred to capital accounts.

Required:

(a) Prepare statement of profit or loss for the year ended 31 December 2019. **(08)**

(b) Show how HT's profit for the year ended 31 December 2019 would be shared between the partners. **(08)**

Prepare statement of financial position as at 31 December 2019. **(04)**

Question 8

Following draft statement of financial position as on 31 December 2019 of Naltar Establishment (NE) is under review:

Assets	Rs. in '000	Equity & liabilities	Rs. in '000
Fixed assets – net	22,590	Opening capital	32,240
Current assets:		Net profit for the year	9,360
Stock	15,320		41,600
Trade receivables	19,730	**Current liabilities:**	
Drawings	1,400	Trade payables	17,332
Cash & bank	3,850	Other payables	2,680
	40,300	Suspense account	798
		Discount received	480
			21,290
	62,890		62,890

The following matters are identified:

(i) Goods costing Rs. 5,800,000 received on 31 December 2019 were included in the year-end physical count. However, these goods were recorded in purchases day book on 5 January 2020 on receipt of the invoice.

(ii) Year-end physical count sheets include a third party stock of Rs. 1,320,000.

(iii) Goods sold on credit at a trade discount of 10% were recorded at gross amount of Rs. 6,400,000.

(iv) An unidentified credit of Rs. 294,000 appearing in the bank statement was accounted for in the suspense account. It was discovered that the credit was a settlement of an old outstanding balance previously written off. The amount was net of 2% bank charges.

(v) A cheque of Rs. 500,000 issued by a customer as an advance was dishonored and returned by the bank on 31 December 2019. No entry was made on return of cheque.

(vi) Operating expenses include insurance premium of Rs. 900,000 paid during the year, out of which Rs. 200,000 pertain to owner's residential premises. The policy is valid up to 30 June 2020.

(vii) An upgradation of a plant to improve quality and efficiency was completed on 1 July 2019 at a cost of Rs. 2,500,000. The cost was charged to repair and maintenance expense.

(viii) Total sales of 26 December 2019 as per sales day book was Rs. 167,000. This was posted in trade receivable control account as Rs. 671,000. Trial balance was balanced by taking the difference to the suspense account.

Other information:

NE uses periodic stock method. The plant is depreciated at 20% using diminishing balance method.

Required:

Prepare corrected statement of financial position as on 31 December 2019. **(17)**

Answers

A.1

Shangrila Enterprises

Book value of the plant as at 31 December 2019

			Rs. in million
Initial cost of the plant:			
(i)	Cost of the plant		780.00
(ii)	Sale of old plant/investments		-
(iii)	Freight charges	3.50+1.50	5.00
	Repair of plant damages		-
(iv)	Preparation of site	4.6+1.2	5.80
(v)	Installation work		5.00
(vi)	Customization of the plant		12.00
(vii)	Purchase of safety equipment		-
Initial cost			**807.80**
Depreciation for 2019		(807.80–100)×1/20×8/12	(23.59)
Book value of the plant as at 31December 2019			**784.21**

A.2

(a)

Analysis of expenses by nature		
Description	**Rs.**	
Revenue		x
Other income		x
Changes in inventories	x	
Raw materials and consumables used/Purchases	x	
Employee benefits expense/Salaries	x	
Depreciation and amortization expense	x	
Other expenses	x	
Total expenses		(x)

(b)

Analysis of expenses by function	
Description	**Rs.**
Revenue	x
Cost of sales	(x)
Gross profit	**x**
Other income	x
Distribution costs	(x)
Administrative expenses	(x)
Other expenses	(x)
Profit	**x**

A.3 Paristan Brothers

Accounting equation

S.No.	Head of account	Assets	=	Equity	+	Liabilities
		---------- Rupees [Increase/(Decrease)] ----------				
(i)	Travel expenses			(85,000)		
	Capital			85,000		
(ii)	Drawings			(45,000)		
	Bank/Cash	(45,000)				
(iii)	Bank/Cash	100,000				
	Accumulated depreciation	190,000				
	Fixed assets	(250,000)				
	Gain on sale of fixed assets			40,000		
(iv)	Trade creditors					(1,500,000)
	Capital			1,500,000		
(v)	Rent expense			(210,000)		
	Sale			210,000		
	Cost of sales			(180,000)		
	Inventory	(180,000)				
(vi)	Bank/Cash	400,000				
	Bad Debts			(400,000)		
	Account receivable	(800,000)				
	Provision	480,000				
	Bad Debts			480,000		

Journal Entries [not required for extra information]

(i)	Travel expense	85,000	
	Capital		85,000
(ii)	Drawings	45,000	
	Bank/Cash		45,000
(iii)	Bank/Cash	100,000	
	Accumulated depreciation (250,000-60,000)	190,000	
	Asset		250,000
	Gain on disposal (Bal.)		40,000
(iv)	Trade creditors	1,500,000	
	Capital		1,500,000
(v)	Rent expense	210,000	
	Cost of sales	180,000	
	Sales		210,000
	Inventory		180,000
(vi)	Bank/Cash	400,000	
	Bad debts	400,000	

	Debtor (400,000 / 50% x 100%)		800,000
	Allowance for doubtful debts (800,000 x 60%)	480,000	
	Bad debts		480,000

A.4 (i) **(c)** Contra asset account

(ii) **(d)** Normal loss

(iii) **(b)** Deducted from balance of bank statement or added to balance of cash book

(iv) **(a)** Only (I) is correct

(v) **(d)** Rs. 140,000

(vi) **(c)** Error of principle

(vii) **(c)** General journal

(viii) **(b)** Interest payable Rs. 825,000; Unearned rent income Rs. 45,000

Rs. 575,000

(ix) **(b)** (300,000+275,000)

Workings:

iv.

Prepaid expense

b/d	100	Expense	400
Cash	500		
		c/d	200

Accrued income

b/d	100	Cash	400
Income	500		
		c/d	200

v.

Unearned rent / rent receivable

b/d	17,000	b/d	10,000
Income	14,000	Cash	150,000
c/d	16,000	c/d	13,000

viii.

interest payable 6,000 x 15% x 11/12 = 825,000

Unearned income:

45,000 x 6/6 x 1 = 45,000

A.5 Kallar Traders

(a) Inventory ledger card for the month of January 2020 - Beta

Date	Description	Receipts			Issuances			Balance		
1-1-2020	Balance							2,800	50	140,000
								1,200	52	62,400
3-1-2020	Purchases	3,000	57	171,000				2,800 1,200 3,000	50 52 57	140,000 62,400 171,000
8-1-2020	Sales				2,800 100	50 52	140,000 5,200	1,100 3,000	52 57	57,200 171,000
15-1-2020	Sales				1,100 700	52 57	57,200 39,900	2,300	57	131,000
20-1-2016	Purchase Return	(500)	57	(28,500)				1,800	57	102,600
25-1-2016	Purchase	3,000	58	174,000				1,800 3,000	57 58	102,600 174,000
31-1-2016	Shortage	(600)	57	(34,200)				1,200 3,000	57 58	68,400 174,000

Valuation of stock as on 31-01-2020:				
Damaged units	100	57	20	2,000
Good units	1,100	57	90.25*	62,700
Good units	3,000	58	90.25*	174,000
				238,700
Latest selling price	= 171,000 x 95% / 1,800 = 90.25			

(b) **General Journal**

Date	Description		Debit	Credit
			Rupees	
03-Jan-2020	Inventory Cash	3,000×60×0.95	171,000	 171,000
08-Jan-2020	Cost of sales Inventory Account receivable Sales	140,000+5,200	145,200 266,800	 145,200 266,800
15-Jan-2020	Cost of sales Inventory Account receivable Sales	57,200+39,900 171,000×0.95	97,100 162,450	 97,100 162,450

20-Jan-2020	Trade payable Inventor y	500×60×0.95	28,500	28,500
25-Jan-2020	Inventory Account payable		174,000	174,000
30-Jan-2020	Goods in transit Account payable		120,000	120,000
31-Jan-2020	Stock loss Inventor y		34,200	34,200

A.6

Zahrba Stationers
Trial balance for the month of January 2020

Description		Debit	Credit
		----- Rs. in '000 -----	
Cash		480	
Bank		167	
Sales	4,937+290+295		5,522
Trade debtors	2,423+4,937−2,000−1,590	3,770	
Other income (scrap sale)			25
Purchases	4,070+250	4,320	
Trade creditors	1,800+4,070−1,500−1,378−100		2,892
Utility expenses		98	
Petty cash in hand		20	
Repair and maintenance	67−25	42	
Long term loan	800−100+15		715
Sales return		70	
Other payable			70
Purchase return			100
Interest expense		15	
Drawings		25	
Petty cash expenses	50−20	30	
Fixed assets		1,600	
Accumulated depreciation	1,600−1,254		346
Opening inventory		850	
Capital	110+1,254+2,423+850−180−1,800−800		1,857
Discount allowed		100	
Discount received			60
		11,587	**11,587**

Workings:
Accounting entries:

			Rs. "000"
Purchases		4,070	
	Creditors control a/c		4,070
Debtors control a/c		4,937	
	Sales		4,937
Cash		290	
	Sales		290
Bank		1,900	
Dis allowed (1,900/95 x 5)		100	
	Debtor control a/c		2,000
Bank		1,590	
	Debtor control a/c		1,590
Bank		25	
	Scrap sales		25
Cash		200	
	Bank		200
Cash		295	
	Sales		295
Purchases		250	
	Cash		250
Creditors control a/c		1,500	
	Dis. Received		60
	Bank		1,440
Utility bills		98	
	Cash		98
Petty cash		50	
	Bank		50
Repair & Maintenance		67	
	Cash		67
Long term loan		85	
Interest expense		15 (Point iii)	
	Bank		100
Creditor control a/c		1,378	
	Bank		1,378
Petty expense	30		
	Petty cash		30
Drawings	25		
	Repair & Maintenance		25
Creditor control a/c	100		
	Purchase return		100
Sales return	70		
	Payable to Haleji & sons		70

A.7

a)

Hanna traders
Statement of profit or loss
For the year ended 31-12-2020

	"Rs in Million"
Sales (315 – 7)	308
Cost of sales (N – 1)	(216)
Gross profit	92
Other income (N – 2)	23.5
Selling and admin expenses (N – 3)	(66.5)
Financial charges (Given)	(5)
Net profit	44

Note 1:

Cost of sales:	
Opening inventory	35
Purchases (170 – 2 – 1)	167
+ Import duties	39
+ Freight inwards	5
- Closing inventory	(30)
	216

Note 2:

Other income:	
Given	6
Gain on disposal	10
Maintenance contract	7.5
	23.5

Note 3:

Selling and admin expenses:	
Operating expenses (52 – 8 – 1)	43
Free sampling	2
Bad debts (5 – 2)	3
Rent expense	2
Depreciation	16
Commission expense	0.5
	66.5

b) **Appropriation account**
For the year ended 31-12-2019

	Total	A	Zee
Salary to A (1 x 12)	12	12	
Commission to Zee (308 x 6%)	18.48		18.48
Residual profit (44 – 12 – 18.48)	13.52	8.11 (3/5)	5.4 (2/5)
Total	44	20.11	23.89
20% Transferred to capital a/c	(8.8)	(4.02)	(4.78)
Remaining transferred to current a/c	35.2	16.09	19.11

Current a/c

	A	Zee		A	Zee
b/d	4	-	b/d	-	2
Drawing	1	8	Profit	16.09	19.11
c/d	11.09	13.11			

Capital a/c

	A	Zee		A	Zee
			b/d	67	45
			Profit	4.02	4.78
c/d	71.02	49.78			

c) **Hanna traders**
Statement of financial position
As on 31-12-2019

		“Rs in Million”
Assets:		
Non - Current assets		
Property, Plant & equipment [(140 – 28) – (64 – 28)]		76
Current assets:		
Stock		30
Trade receivables (50 – 2)		48
Prepayments (6 – 2)		4
Prepaid income		1
Other receivables		4
Receivable against machine		10
Maintenance income receivable		1.5
Cash and Bank		3
Total assets		177.5
Equity and Liabilities:		
Capital – A	71.02	
– Zee	49.78	120.8

Current a/c – A	11.09	
– Zee	13.11	24.20
		145.0
Current liabilities:		
Trade payables		30
Other payables and acemals (8 – 6)		2
Commission payable		0.5
Total equity and liabilities		177.5

Working:

Free samples/Advertisement	2	
Purchases		2
Drawing - A	1	
Purchases		1
Drawing - Zee	8	
Operating exp		8
Prepaid insurance	1	
Operating expense		1

1-1-2018 1-8-2019 31-12-2019 31-3-2020

6/50 x 100 = 12
12/8 x 5 =7.5

Other payables	6		
Income receivable	1.5		
		Maintenance income	7.5
Rent exp	2		
		Prepaid rent	2
Trade receivables	2		
		Bad debts	2
Receivable	10		
Acc. dep	28		
		PPE	28
		Gain	10
Commission exp	0.5		
		Payable	0.5
10 x 5% = 0.5			

Debtor A/C

Unadjusted b/d	48		
Bad debts	2	c/d	50

Allowance A/C

b/d	3	Bad debts	2
c/d [50 x 4% = 2]	2		

Bad debt	5	
Allowance		5

A.8 Naltar Establishment

Statement of financial position as at 31 December 2019

		Rs. in '000
Assets		
Fixed assets	22,590+2,500–250	24,840
Current assets:		
Closing stock	15,320–1,320	14,000
Trade receivables	19,730–640–504	18,586
Prepaid Insurance		350
Cash & bank	3,850–500	3,350
		36,286
		61,126
Equity & liabilities		
Opening capital		32,240
Net profit for the year	**(W-1)**	5,174
Drawings	1,400+200	(1,600)
Net equity		35,814
Current liabilities:		
Trade payables	17,332+5,800	23,132
Other payables	2,680–500	2,180
		25,312
		61,126

W-1: Corrected net profit for the year		**Rs. in '000**
Balances as per draft financial statements		9,360 Cr.
Corrections:		
(i) Purchases of Dec. 2019 recorded in Jan. 2020		(5,800) Dr.
(ii) Cost of Sales		(1,320) Dr.
(iii) Goods sold recorded at gross of 10% trade discount	6,400×10%	(640) Dr.
(iv) Clearance of unidentified credit taken to suspense account:		
- Bank charges	(294/98x2)	(6) Dr.
- Recovery of previously written off balance	(294/98x100)	300 Cr.
(vi) Insurance premium paid pertains to:		
- Owner		200 Cr.
- Insurance	700/2	350 Cr.
(vii) Upgradation cost of a plant charged to repair and maintenance:		
- Repair and maintenance expense		2,500 Cr.

- Depreciation expense	(2,500×20% x6/12)	(250) Dr.
Discount received		480 Dr.
Revised net profit		**5,174**

W-2

Purchases	5,800						
Creditor		5,800					
Cost of sale	1,320						
Sock		1,320					
Sales	640						
Debtor		640					
[6,400 x 10%]							
Bank	294		Bank	294		Suspense	294
Bank charges	6		Suspense		294	Bank Charges	6
Bad debts		300				Bad debts	300
(Required)			**(Posted)**			**(Rectifying)**	
Advance from customer	500						
Bank		500					
Drawings	200						
Operating expense		200					
Prepaid Insurance	350						
Operating expense		350					
[700 / 2]							
Fixed assets	2,500						
Repair and maintenance		2,500					
Depreciation	250						
Acc. Depreciation		250					
(2,500 x 20% x 6/12)							
Debtor	167		Debtor	671		Suspense	504
Sales		167	Sales		167	Debtor	504
			Suspense		167		
(Required)			**(Posted)**			**(Rectifying)**	

ICAP Study text

Extra theoretical discussion (Intro)

Chart of accounts

This is a list of accounts created by a business to be used to organise its financial transactions into identified categories of assets, liabilities, income and expenses.

Each general ledger account is identified by a unique code and heading. This allows a business to generate instructions and policies to be followed by those members of staff responsible for recording information.

The list is typically arranged in the order of the customary appearance of accounts in the financial statements, statement of financial position general ledger accounts followed by statement of comprehensive income general ledger accounts. The structure and headings in the list aim to result in consistent posting of transactions.

A company might have complete freedom in designing its chart of accounts (within the boundaries set by the rules of accounting). In some countries, the government might issue a generic chart of accounts from which a business selects those codes that are appropriate to its needs.

The aim of the chart is to ensure that all transactions are recognised in accordance with the requirements of the business.

Illustration: Chart of accounts

Each major heading in the financial statements might be given a range of codes from which codes can be selected for individual general ledger accounts:

	Code range		**Code range**
Non-current assets	100-199	Income	600-699
Current assets	200-299	Expenses	700-799
Non-current liabilities	300-399		
Current liabilities	400-499		
Equity	500-599		
Individual ledger accounts within the above range for non-current assets:			
Non-current assets	Code		
Land	110		
Office buildings	120		
Warehouses	130		
Factories	140		

The organisation will maintain appropriate chart of accounts in order to cater the present and future monetary transactions with an objective of coming up with timely, accurate and meaningful financial reporting. The chart of accounts will act as a guiding and referring tool to the finance personnel while they post accounting entries to their respective head of accounts. In order to keep a vigilant control over accounting framework of the organization, no accounting personnel is allowed to make amendment (including opening a new head of account) in the chart of accounts unless specific written approval thereof is duly sanctioned by the Head of Finance.

Vouchers & Forms

The finance personnel will be responsible to record and maintain financial records, related correspondence, accounts, statements, supports, etc. pertaining the organization. For effective and accurate maintenance of accounting records, a set of internal documents, forms have been designed which will be used for initiating and recording financial transactions.

Payment Voucher

Payment can be made after approval of payment voucher. Payment voucher will be supported with bills or other relevant supporting documents. Such supports will be scrutinized by the finance department prior to their submission for sanction of payment before the approving authority.

All cash payments will be recorded through cash payment vouchers and all bank payments will be recorded through bank payment vouchers

Receipt Voucher

Receipt voucher will be prepared to record the receipts and collections in bank accounts.

Cash receipt transactions will be recorded through cash receipts.

Journal Voucher

Journal voucher (JV) is prepared to evidence the authorization to record non-cash transactions. A non-cash transaction is one which does not involve the actual receipt and payment of cash but the recognition of which in the books of account is fundamental to properly reflect the operating results and financial position of the organization. As a pre-requisite of the accrual basis of accounting, all accruals will be recorded on a monthly basis. Such accounting entries will be recorded through JVs.

Books of Accounts / Records

In addition to the above mentioned different types of vouchers, the organization will keep and maintain the following information / record:

- Cash / Bank Book
- General Ledger
- Salary Register
- Bank Statements & Reconciliation's
- Fixed Assets Register
- Employee Personal Files
- Invoices
- Bank Deposit Slips
- Cheque Books
- Purchase Orders and invoices
- Sale Orders
- Invoices
- Any other record and information considered necessary.

Pre numbering entries

All entries will be allotted sequential numbers so as to ensure completeness and proper authorization thereof. Any entry recorded out of the prescribed sequence would require immediate and thorough scrutiny to dispel the impression of any deliberate event. A written report of such inquiry will need to be submitted to the Head of Finance, who would then decide future course of action.

Review of accounting entries

All accounting entries will be submitted to the Head of Finance for his approval. Such entries will not be considered unless they are supported through documentary evidences originating such transaction(s). After necessary approval, such entries should be posted in their relevant head of account. If this is not possible due to peculiar nature of the transaction, the matter should be referred to the superior personnel for proper guidance.

Segregation of Duties

In order to keep a meaningful check over the affairs of organization, segregation of duties is a must, whenever practicable. Segregation of duties means distributing the execution of one activity over more than one person in order to ensure that no single individual is capable of handling the whole of a transaction individually. If it is not practical to segregate any duty due to its operational nature and / or limited staff members, the management should ensure that all transactions are duly authorized and supported with all necessary documents and properly recorded in books of account in a timely manner.

Correction of entries

Ensure that in case of omission, error of disposition / classification, etc. the correction should always be routed through JV. To confirm this procedure in the computerized accounting software, access controls have been placed which prohibits and restricts the individual responsible for data entry from re-entering and accessing the recorded data.

Audit Trail

At the time of approving the accounting entry, the Head of Finance will ensure that adequate and reliable audit trial of the subject transaction exists and that the entry would be easily auditable at the time of internal or external audit. Such audit trial would, ideally, start from the financial statements and end up at the related source document(s).

Custody of Accounting Records

All the accounting records, including but not limited to ledgers, statements, accounts, vouchers, invoices, banking records, record of procurement and sales, etc. should be in the custody of the accounting personnel. The Head of Finance should ensure that adequate facilities exist for custody of accounting records. **Such records should be kept and maintained for a minimum 5 years from the relevant year-end.**

The content of financial statements might vary depending on whether a business is a sole trader, partnership of company. However, the basic process used to record transactions is similar for all types of entity. The techniques used is called double entry bookkeeping and is explained in detail later.

Financial reporting by sole traders and partnerships

The financial statements of a sole trader are private and do not have to be disclosed, except to the tax authorities. These must be prepared according to accepted accounting principles and practice, but need not conform to all the requirements of accounting standards.

Similarly, the financial statements of a business partnership are private and do not have to be disclosed.

Financial reporting by companies

The financial statements of a company are prepared for the shareholders of the company and are usually subject to audit. Audit is the examination of the financial statements by an independent expert who expresses an opinion as to whether they are fairly presented (show a true and fair view).

Company Act requires that every company shall send its financial statements to every member and every person who is entitled to receive notice of general meeting and are filed with a registrar, where they can be accessed and read by any shareholder / members. Moreover, every company shall prepare and keep at its registered office books of account and other relevant books and papers and financial statements for every financial year which give a true and fair view of the state of the affairs of the company

Companies whose shares are traded on a listed stock market in Pakistan make their financial statements generally available to the public, often on the company's web site.

Therefore, the financial statements of a company are subject to more regulation than those of a sole trader or a partnership.

Regulation of financial reporting

Generally accepted accounting principles

Financial reporting is regulated and controlled for every company who are required to file it. Regulations help to ensure that information reported in financial statements has the required qualities and content.

The concepts, principles, conventions, laws, rules and regulations that are used to prepare and present financial statements are known as ***Generally Accepted Accounting Principles*** or ***GAAP***.

The main sources of GAAP in a jurisdiction are:

- Company Act, 2017; and
- IFRS / Specialised Financial Statements (for banks, insurance, mutual funds / SMEs)

GAAP varies from country to country, because each country has its own legal and regulatory system. For example, there is a US GAAP etc.

IFRS

The accountancy profession has developed a large number of regulations and codes of practice that professional accountants are required to use when preparing financial statements. These regulations are **accounting standards**.

Many countries and companies whose shares are traded on the world's stock markets have ***adopted International Financial Reporting Standards*** or ***IFRS***. These are issued by the International Accounting Standards Board (IASB).

THE CONCEPTUAL FRAMEWORK FOR FINANCIAL REPORTING

Introduction

Financial Statements are prepared and presented for external users by many entities around the world. These financial reports are based on estimates, judgements and models rather than exact depictions. The Conceptual Framework establishes the concepts that underlie those estimates, judgements and models.

Financial statements are prepared in accordance with approved accounting standards as applicable in Pakistan. Approved accounting standards comprise of such International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) and Islamic Financial Accounting Standards (IFAS) issued by the Institute of Chartered Accountants of Pakistan (ICAP) as are notified under the Companies Act, 2017. In case requirements of IFRS differ with Companies Act, 2017 the provisions or directives of the Companies Act, 2017 shall prevail. However, since CAF 1 is an introductory subject, therefore, requirements of Companies Act are not discussed.

Objective

The Conceptual Framework sets out the concepts that underlie the preparation and presentation of financial statements for external users. Its purpose is:

- to assist the IASB in the development of future IFRSs and in its review of existing IFRSs;
- to assist the IASB in promoting harmonisation of regulations, accounting standards and procedures relating to the presentation of financial statements by providing a basis for reducing the number of alternative accounting treatments permitted by IFRSs;
- to assist national standard-setting bodies in developing national standards
- to assist preparers of financial statements in applying IFRSs and in dealing with topics that have yet to form the subject of an IFRS;
- to assist auditors in forming an opinion on whether financial statements comply with IFRSs; and
- to assist users of financial statements in making sound economic decisions;

This Conceptual Framework is not an IFRS and nothing in the Conceptual Framework overrides any specific IFRS. On very rare occasions there may be a conflict between the Conceptual Framework and an IFRS. In those cases, the requirements of the IFRS prevail over those of the Conceptual Framework.

Scope

The Conceptual Framework deals with:

- the objective of financial reporting;
- the qualitative characteristics of useful financial information;
- the definition, recognition and measurement of the elements from which financial statements are constructed; and
- concepts of capital and capital maintenance.

Objective of general purpose financial statements

The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity.

Those decisions involve buying, selling or holding equity and debt instruments, and providing or settling loans and other forms of credit.

In order to make these decisions the users need information to help them assess the prospects for future net cash inflows to an entity.

In order to assess an entity's prospects for future net cash inflows, users need information about:

- the resources of the entity;
- claims against the entity; and
- how efficiently and effectively the entity's management have discharged their responsibilities to use the entity's resources. (This information is also useful for decisions by those who have the right to vote on or otherwise influence management performance).

1. ACCOUNTING CONCEPTS

Relevance

Information must be relevant (i-e. capable of making a difference in the decisions made by users). Information is relevant if it can be used for predictive and/or confirmatory purposes.

- It has **predictive value** if it helps users to predict what might happen in the future.
- It has **confirmatory value** if it helps users to confirm the assessments and predictions they have made in the past.

For example, revenue information for the current year, which can be used as the basis for predicting revenues in future years, can also be compared with revenue predictions for the current year that was made in past years.

The relevance of information is affected by its materiality.

ENHANCED QUALITATIVE CHARACTERISTICS OF USEFUL FINANCIAL INFORMATION

Introduction

Information must have certain characteristics in order for it to be useful for decision making. The *IASB Conceptual Framework* describes:

- fundamental qualitative characteristics; and
- enhancing qualitative characteristics

Fundamental qualitative characteristics

The fundamental qualitative characteristics are;

- relevance; and
- faithful representation

Enhanced qualitative characteristics of useful financial information

The qualitative characteristics that enhance the usefulness of information that is relevant and a faithful representation are:

- comparability;
- verifiability
- timeliness; and
- understandability

Enhancing qualitative characteristics

Comparability

Comparability enables users to identify and understand similarities in, and differences among, items

Information about a reporting entity is more useful if it can be compared with similar information about other entities and with similar information about the same entity for another period or another date.

Consistency is related to comparability but is not the same. Consistency refers to the use of the same methods for the same items, either from period to period within a reporting entity or in a single period across entities. Consistency helps to achieve the goal of comparability.

Verifiability

This quality helps to assure users that information faithfully represents the economic phenomena it purports to represent.

- Verifiability means that different knowledgeable and independent observers could reach consensus that a particular depiction is a faithful representation.
- Quantified information need not be a single point estimate to be verifiable. A range of possible amounts and the related probabilities can also be verified.

Verification can be direct or indirect.

- Direct verification means verification through direct observation, e.g. by counting cash or inventory.
- Indirect verification means checking the inputs to a model, formula or other technique and recalculating the outputs using the same methodology. For example, the carrying amount of inventory might be verified by checking the inputs (e.g. costs) and recalculating the closing inventory using the same assumption (e.g. FIFO).

Timeliness

This means having information available to decision-makers in time to be capable of influencing their decisions.

Understandability

Information is made understandable by classifying, characterising and presenting it in a clear and concise manner.

Financial reports are prepared for users who have a reasonable knowledge of business and economic activities and who review and analyse the information diligently.

Cost constraint on useful information

Cost is a pervasive constraint on the information that can be provided by financial reporting. Reporting financial information imposes costs, and it is important that those costs are justified by the benefits of reporting that information.

The benefits obtained from financial information should exceed the cost of obtaining and providing it. Information should not be provided if the cost is not worth the benefit.

Since it is difficult to measure the benefits of financial information, the setters of accounting standards must use their judgement in deciding whether certain items of information should be provided in the financial statements (and if so, in how much detail).

Petty cash Book

Definition of petty cash

Petty cash is cash (notes and coins) held by a business to pay for small items of expense, in situations where it is more convenient to pay in notes and coin than to pay through the bank account. Petty cash might be used, for example, to pay for bus fares, taxi fares, tea and coffee for the office, and so on.

Recording petty cash transactions

When petty cash transactions take place, for example petty cash is spent on tea and coffee for the office, the entity needs to record both an expense, and a reduction in the asset "petty cash".

These entries are made in the main ledger accounts as follows:

Illustration: x

	Debit	Credit
Office expenses	X	
Petty cash		X

Although the amounts involved in petty cash are, for most businesses, very small, the **"cash in the tin"** (cash in the drawer) is one of the easiest assets to be stolen or "lost".

Usually the responsibility for looking after the petty cash is assigned to an accounts clerk who will pay out any cash to a person as long as that person is able to present an invoice for an amount spent. The accounts clerk will also maintain a petty cash book. This is a book of prime entry and is summarised and posted to the general ledger on a periodic basis,

Imprest system

A very common petty cash system is called the imprest system. Under this system a set amount is established (say Rs.10,000). This set amount is called the imprest.

At any moment in time, the petty cash balance plus the amounts on the bills should sum to the imprest. Periodically the invoices are removed and replaced by cash to re-establish the imprest in cash.

Example:

A business uses an imprest system to control its petty cash.

The imprest is set at Rs. 10,000.

At the start of the month there is Rs. 10,000 cash in the petty cash tin.

An amount of Rs. 600 is paid to compensate for a payment made out of on behalf of the business.

After this transaction the petty cash tin will contain Rs.9,400 cash and a bill of Rs.600. These two amounts add back to the imprest.

Example:

ShanIndustries keeps an analysed petty cash book using the imprest system. The imprest amount is Rs.2,000. The following information is available for the month of June 2016.

2016 June		Rs.	Voucher Number
1	Balance	2,000	
6	Paid window cleaner	200	1
8	Bought pens and pencils	100	2
11	Paid for bus fare	60	3
16	Paid for printer cartridge	400	4
18	Purchased envelops	270	5
20	Paid for coffee and milk for office staff	70	6
22	Bought printing papers	80	7
23	Paid taxi fare	200	8
24	Paid office cleaner	170	9
26	Paid for biscuits and tea	100	10
28	Purchased paper pins	40	11
29	Paid for petrol	70	12

Required

Write up the petty cash book for the month of June 2016 for Shan Industries. Balance the petty cash book and carry down the balance. Show the restoration of imprest as on July 1 2016.

Shanzay Industries
Petty Cash Book

Date	Details	Total received	Date	Details	Vo	Total paid	Cleaning	Stationery	Travel expenses	Postage	Food
		Rs.				Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
2016			2016								
June 1	Balance b/d	2,000	June 6	Window cleaner	1	200	200				
			8	Pens and pencils	2	100		100			
			11	Bus fare	3	60			60		
			16	Printer cartridge	4	400		400			
			18	Envelops	5	270				270	
			20	Coffee and milk	6	70					70
			22	Printing paper	7	80		80			
			23	Taxi fare	8	200			200		
			24	Office cleaner	9	170	170				
			26	Biscuits and tea	10	100					100
			28	Paper pins	11	40		40			
			29	Petrol	12	70			70		
						1,760	370	620	330	270	170
			30	Balance c/d		240					
						2,000					
2016											
July 1	Balance b/d	240									
	Cash	1,760									

The purpose of depreciation

It is important to understand the purpose of depreciation. **Depreciation is an application of the accruals concept or matching concept.**

When a non-current asset is purchased the cost is:

- taken to the non-current asset account at cost and
- shown in the statement of financial position.

The cost is capitalised. However this asset is used within the business in order to earn profits. Therefore some element of its original cost must be charged to the statement of comprehensive income ('charged to profit and loss') each period in order to match the 'consumption' of the cost or value of the assets with the income that the asset is generating.

Depreciation is the element of the cost of the non-current asset that is charged to the statement of comprehensive income each period.

Inventories:

SCOPE AND EXPLANATION

Introduction

There are generally three reasons companies maintain inventories:

- Meeting variation in production demand;
- Economies of scale in procurement;
- Guarding against price increases and stock outs

Inventory is a key component of calculating cost of goods sold (COGS) and is a key driver of profit and current assets. Because changes in materials prices affect the value of a company's inventory, it is important to understand how a company accounts for its inventory. Common inventory accounting methods include first in, first out (FIFO) and Weighted Average method.

Given the significant costs and benefits associated with inventory, companies spend considerable amounts of time calculating what the optimal level of inventory should be at any given time and changes in inventory levels can send mixed messages to investors.

Increases in inventory may signal that a company is not selling effectively, is anticipating increased sales in the near future or has an inefficient purchasing department. On the other hand, declining inventories may signal that the company is selling more than it expected, is experiencing a blockage in its supply chain, is expecting lower sales or is becoming more efficient in its purchasing activity.

Definitions

Inventories are assets that are:
- held for sale in the ordinary course of business;
- in the process of production for such sale; or
- in the form of materials or supplies to be consumed in the production process or in the rendering of services.

Net realisable value (NRV) is the estimated selling price less the estimated costs of completion and the estimated costs necessary to make the sale.

Cost of inventories is;

- all costs incurred in bringing the inventories to their present location and condition excluding abnormal waste, storage costs, administrative overheads unrelated to production, selling costs and interest cost when inventories are purchased with deferred settlement terms.
- Costs of purchase of inventories comprise the purchase price (less trade discounts, rebates, duty drawbacks and similar items), irrecoverable taxes, freight inwards, handling and other costs directly attributable to their acquisition.
- Costs of conversion in finished goods include costs directly related to the units of production, such as direct labour and systematically allocated fixed and variable production overheads incurred in producing finished goods.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Explanation of defined terms

Inventories are

held for sale in the ordinary course of business

Inventories are those assets (finished goods) of an entity which are sold in the normal course of business normally within one year from the balance sheet date. Assets which are held for sale but are not traded in the normal course of business cannot be classified as inventories.

in the process of production for such sale;

The goods which have undergone some production process but are not in the intended selling condition are termed as work in process. **Work in process is also part of the inventories.**

in the form of materials or supplies to be consumed in the production process or in the rendering of services (i-e raw material). **The raw materials used for the production of goods are also classified as inventories.**

Note

Goods that are in transit where risk and rewards is transferred to the buyer are also categorised as inventory (either finished goods or raw material)

Net realisable value (NRV)

Net realizable value is the expected selling price in the ordinary course of business minus any costs of completion, disposal and transportation.

To illustrate, let's assume that a company's cost of its inventory is Rs.55,000. However, at the end of the accounting year the inventory can be sold for only Rs.50,000 provided that the company spends an additional Rs.5,000 in packaging and shipping expense. Hence, the inventory's net realizable value is Rs.45,000 (50,000 - 5,000).

When the net realizable value of a company's inventory is less than its cost, the company's balance sheet should report the net realizable value. In our example, the inventory will be reported at Rs.45,000 and the income statement will report a Rs.5,000 loss on the write down of inventory.

Example:

Sage Pvt. Ltd (SPL) manufactures and sells 1300 CC. Motor Cars to its customers for Rs.1,500,000 per car. The stock of cars was included in the closing inventory as of 31 December 2019 at a cost of Rs.1,000,000 per car. The competitor launched the new 1300 CC hybrid cars on 31 December 2019 for Rs.1,800,000 per car.

During the final audit the auditors noted that the subsequent selling price for the Cars at 15th January 2020 was Rs.1,400,000 per car. Furthermore, inquiry reveals that during the physical stock take, a car is damaged. Accordingly, SPL in the following week, spent a total of Rs.500,000 for repairing.

Required:

Compute the amount of:

- Net realizable value of the damaged cars
- inventory write-down (loss) to the cars

Solution:

Net realisable value = [Rs.1,400,000 (selling price) – Rs.500,000 (repair)]

= Rs.900,000

Inventory write-down = [Rs.1,000,000 (carrying amount) – Rs.900,000 (NRV)]

= Rs.100,000

Points to consider

Sales tax on purchases (input tax) is eventually recovered from tax authorities in the form of adjustment to output tax, therefore it must not form part of the inventory cost.

Storage costs of raw materials requiring further processing may be included in the cost of inventory. However, storage cost of finished goods is not included in the cost of inventory as it does not contribute to bringing the inventory to its present location and condition.

Cost model should be used for inventory having similar nature and use to the entity. Difference in geographical location is not sufficient to justify using a different cost model.

Fixed production overheads should be allocated to items of inventory on the basis of normal production capacity.

Materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost.

The basic requirement for counting an item in inventory is economic control rather than physical possession (substance over form). Therefore, when a company purchases inventory, the item is included in the inventory even if the purchaser does not have physical possession of those items.

To the extent that service providers have inventories, they measure them at the costs of their production. These costs consist primarily of the labour and other costs of personnel directly engaged in providing the service, including supervisory personnel, and attributable overheads.

Illustration:

Brad Shaw & Co. imports raw materials from China worth Rs.1 million. They paid Rs.80,000 as import duties and Rs.20,000 as import taxes (the import taxes were subsequently refunded by the local government). They paid Rs.50,000 for transportation of the materials from China and another Rs.10,000 as port handling charges for loading the materials at China.

Marketing expenses were Rs.10,000 and the general administrative overheads amounted to Rs.5,000. What will be the value of inventories as per IAS 2?

Solution	**Rs in thousands**
Materials	1,000
Non-refundable import duties	80
Transportation	50
Handling	10
Total	1,140

Marketing and selling costs, general overheads and refundable taxes are not permitted as a cost of inventory.

<u>Cost Formulas</u>

For non-interchangeable items use Specification identification method

For inter changeable items use either;

- FIFO, or
- Weighted Average Cost method.

Cost measurement techniques:

Standard Cost Method

This method takes into account normal levels of materials and supplies, labour, efficiency and capacity utilisation. They are regularly reviewed and if necessary, revised in the light of current conditions.

Retail Method

It is often used in the retail industry for measuring inventories of large numbers of rapidly changing items with similar margins for which it is impracticable to use other costing methods. The cost of the inventory is determined by reducing the sales value of the inventory by the appropriate percentage gross margin.

Recognition of Expenses

Carrying amount of inventories sold during the period to be shown as Cost of goods sold in the period in which the related revenue is recognised.

Write down to NRV as expense in the period.

Explain the situation when the cost of inventories may not be recoverable

The cost of inventories may not be recoverable if those inventories are either;

- damaged,
- wholly or partially obsolete,
- their selling prices have declined
- the estimated costs of completion or
- the estimated costs to be incurred to make the sale have increased.

The practice of writing inventories down below cost to net realisable value is consistent with the view that assets should not be carried in excess of amounts expected to be realised from their sale or use. Inventories are usually written down to net realisable value item by item.

Valuation of inventory

Basic rule

The valuation of inventory can be extremely important for financial reporting, because the valuations affect both the cost of sales (and profit) and also total asset values in the statement of financial position. Inventory must be measured in the financial statements at the **lower** of:

- cost, or
- net realisable value (NRV).

Net realisable value is the amount that can be obtained from disposing of the inventory in the normal course of business, less any further costs that will be incurred in getting it ready for sale or disposal. This is simply the expected revenue from the sale of inventory after deducting any further costs that are necessary in order to sell the inventory. For example, if a company has raw material costing Rs.50 million, which will be sold as finished products for Rs.80 million after additional Rs.10 million of labour costs are incurred for completion, its NRV will be Rs.70 million (Rs.80 million – Rs.10 million).

Net realisable value is usually higher than cost. Inventory is therefore usually valued at cost. However, when inventory loses value, perhaps because it has been damaged or is now obsolete, net realisable value will be lower than cost.

The cost and net realisable value should be compared for each separately-identifiable item of inventory, or group of similar inventories, rather than for inventory in total.

Example:

A business has four items of inventory. A count of the inventory has established that the amounts of inventory currently held, at cost, are as follows:

	Rs.		
	Cost	Sales price	Selling costs
Inventory item A1	8,000	7,800	500
Inventory item A2	14,000	18,000	200
Inventory item B1	16,000	17,000	200
Inventory item C1	6,000	7,500	150

The value of closing inventory in the financial statements:			
	Lower of:	Rs.	
A1	8,000 or (7,800 – 500)	7,300	
A2	14,000 or (18,000 – 200)	14,000	
B1	16,000 or (17,800 – 500)	16,000	
C1	6,000 or (7,000 – 200)	6,000	
Inventory valuation		43,300	

Current assets

IAS 1 states that an asset should be classified as a current asset if it satisfies **any** of the following criteria:

- The entity expects to realise the asset, or sell or consume it, in its normal operating cycle.
- The asset is held for trading purposes.
- The entity expects to realise the asset within 12 months after the reporting period.
- It is cash or a cash equivalent unless the asset is restricted from being used for at least 12 months after the reporting date. (Note: An example of 'cash' is money in a current bank account. An example of a 'cash equivalent' is money held in a term deposit account with a bank.)

All other assets should be classified as non-current assets.

This definition allows inventory or trade receivables to qualify as current assets, even if they may not be realised into cash within 12 months, provided that they will be realised in the entity's normal operating cycle or trading cycle.

The operating cycle of an entity is the time between the acquisition of assets for processing and their realisation in cash or cash equivalents. When the entity's normal operating cycle is not clearly identifiable, it is assumed to be twelve months. This is almost always the case.

Current liabilities

IAS 1 also states that a liability should be classified as a current liability if it satisfies **any** of the following criteria:

- The entity expects to settle the liability in its normal operating cycle.
- The liability is held primarily for the purpose of trading. This means that all trade payables are current liabilities, even if settlement is not due for over 12 months after the end of the reporting period.
- It is due to be settled within 12 months after the end of the reporting period.
- The entity does **not** have the unconditional **right** to defer settlement of the liability for at least 12 months after the end of the reporting period.

All other liabilities should be classified as non-current liabilities.

Illustration:

If a company obtains a five-year bank loan, where none of the loan principal is repayable until the end of the loan period, the loan will be a non-current liability for the first four years and will then become a current liability in fifth year when it is repayable within 12 months.

Accrued expenses (and deferred income) are current liabilities as these are monies due to a third party but not yet paid; for example, wages payable

Service Organizations

Service organizations do not sell goods but provides services to its clients by using the innovative and technical skillset and expertise of its personnel. Examples include investment banking, consulting, audit, accounting and advisory firms.

Difference between the financial statements of Manufacturing/Trading company and Service Company

Financial Statements of Merchandise/trading Company	Financial Statements of Service Company
A large percentage of the assets comprise inventory.	A large percentage of the assets comprise Receivables/cash.
They have less cash on hand than service businesses as their capital is tied up in relatively illiquid assets.	The funds of service companies are usually tied up towards accounts receivable.
Such companies' income statement shows calculation of costs of goods sold.	There is no line item for the cost of goods sold in the income statement of service

Example: Statement of financial position of an advertising agency

Statement of Financial Position at June 30, 2018

	2018
	Rs. in '000'
Non-current assets	
Property, plant and equipment	20,300
Goodwill	50,000
Website and domains	58,250
Current assets	
Cash and bank	120,000
Short term investments	50,000
Trade receivables	150,000
Prepayments	5,000
Total assets	**478,550**
Equity Liabilities	
Capital	410,205
+ Profit	416,800
- Drawings	(350,000)
	477,005
Non-current liabilities	
Loans	405
Current liabilities	
Trade and other payables	900
Bank overdraft	140
Total Equity Liabilities	**478,550**

Example: Statement of comprehensive income of an advertising agency

Statement of comprehensive income for the year ended June 30, 2018

	Rs. in '000'
Revenue	628,000
Cost of revenues	(200,000)
Gross profit	**428,000**
Other income	15,000
Research and development expenses	(10,000)
Selling and admin expenses	(15,000)
Finance expense	(1200)
Net profit	**416,800**