

# **Accounting 2**

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Accounting 2

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## **Disclaimer**

It is vitally important that resource writers be provided with a clearly written and appropriate structured, that is, set out in topics, syllabus document. My aim in writing this textbook was to cover all of the content of the ATAR Accounting and Finance syllabus document, unit 2. I cannot guarantee that I have understood and correctly interpreted all aspects of this poorly set out syllabus document.

Yours sincerely

Ashley Doyle

# 1 Balance Day Adjustments

## Introduction

A business that is using accrual accounting will often have to change the amounts in some income and expense ledger accounts before the profit or loss is calculated. These entries are known as **balance day adjustments**.

Balance day adjustments are made to ensure that the correct amount of income and expense is included in the profit and loss ledger account and that all the current assets and current liabilities are shown in the balance sheet.

Balance day adjustments are recorded in the general journal and general ledger on the last day of an accounting period.

In this chapter we will examine these adjusting entries. In each example, for ease of understanding, the adjusting ledger entry will be made before its related general journal entry.

## Prepaid Expenses

A prepaid expense is a service paid for in advance.

An example of a prepaid expense is rent of office space paid on 1 February that will expire on 30 June.

A prepaid expense is debited to an asset ledger account when it is paid. At the end of an accounting period the prepaid expense that has been consumed is transferred to an expense ledger account.

### Example

On 1 October 2018 Furniture R Us paid \$2,400 for **12 months** motor vehicle insurance.

The insurance payment was recorded as an asset in the general ledger.

### Prepaid Insurance (asset)

2018		
Oct 1	Bank	2,400

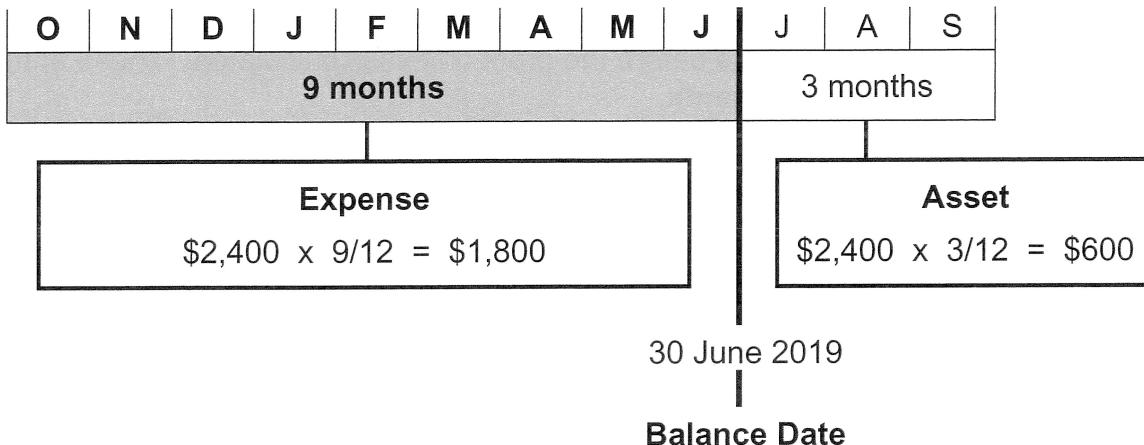
The insurance payment is an asset as the motor vehicle owned by Furniture R Us will be protected against damage or loss for the next 12 months.

Furniture R Us calculates its profit and loss each year ended 30 June.

### **Example continued**

On 30 June 2019 a total of 9 months or \$1,800 of the insurance payment has expired and is an expense and 3 months or \$600 of the insurance payment is still an asset.

This situation can be set out on a diagram:



An adjusting entry must be made in the accounting system of Furniture R Us to ensure that the \$1,800 of insurance expense is included in the profit and loss account for the year ended 30 June 2019.

#### **Step 1**

On 30 June 2019 the \$1,800 of insurance **expense** is removed from the prepaid insurance (asset) account, by crediting this account, and is transferred to an insurance expense account.

<b>Prepaid Insurance (asset)</b>			
2018		2019	
Oct 1	Bank	Jun 30	Insurance
			1,800
<b>Insurance (expense)</b>			
2019			
Jun 30	Prepaid Insurance	1,800	

#### **Step 2**

The prepaid insurance account is balanced off.

<b>Prepaid Insurance</b>			
2018		2019	
Oct 1	Bank	Jun 30	Insurance
			1,800
			<b>Balance c/d</b>
			600
Jul 1	Balance b/d		2,400
			600

**Step 3**

The \$1,800 of insurance expense is transferred to the profit and loss account.

<b>Insurance</b>			
2019		2019	
	Jun 30	Profit and Loss	1,800
Prepaid Insurance	1,800		

<b>Profit and Loss (extract)</b>			
2019		2019	
	Jun 30	Profit and Loss	1,800
Insurance	1,800		

If this adjusting entry was not made the profit for the year ended 30 June 2019 would have been overstated by \$1,800.

The word "overstated" means that the profit would have been incorrect and too large by the amount of \$1,800.

**Step 4**

The remaining prepaid insurance is a current asset in the balance sheet of 30 June 2019:

**Furniture R Us**  
**Balance Sheet (extract)**  
**as at 30 June 2019**

<b>Current Assets</b>	
Prepaid Insurance	600

**Step 5**

The following general journal entry is made to record the prepaid insurance adjustment:

**General Journal**

Date	Details	Debit	Credit
2019 Jun 30	Insurance Expense Prepaid Insurance <i>Insurance expense for the year.</i>	1,800	1,800

## Inventory of Supplies

Supplies are resources purchased for use within the business and will be consumed within one year.

Supplies include, for example, stationery used by an accountant and cleaning liquids consumed by a car detailing (car cleaning) business.

Supplies, when purchased, are debited to an asset ledger account. At the end of an accounting period the supplies that have been consumed are transferred to an expense ledger account.

### **Example**

Furniture R Us purchased \$5,000 of stationery supplies, including A4 paper and printer toner cartridges, during the year ended 30 June 2019.

The \$5,000 of stationery purchased was recorded as an asset in the general ledger:

#### **Stationery Supplies (asset)**

<b>2019</b>			
<b>Jun 30</b>		<b>Balance</b>	<b>5,000</b>

On 30 June 2019 a total of \$1,000 of this stationery was still unused.

The stationery expense for the year ended 30 June 2019, therefore, is:

$$\$5,000 - \$1,000 = \$4,000.$$

An adjusting entry must be made in the accounting records of Furniture R Us to ensure that the \$4,000 of stationery expense is included in the profit and loss account for the year ended 30 June 2019.

### **Step 1**

On 30 June 2019 the \$4,000 of stationery expense is removed from the stationery supplies account and is transferred to a stationery expense account.

#### **Stationery Supplies**

<b>2019</b>			
<b>Jun 30</b>		<b>Balance</b>	<b>5,000</b>
			<b>2019 Jun 30      Stationery Expense 4,000</b>

#### **Stationery Expense**

<b>2019</b>			
<b>Jun 30</b>		<b>Stationery Supplies</b>	<b>4,000</b>

**Step 2**

The stationery supplies account is balanced off:

**Stationery Supplies**

		2019			2019
		Jun 30	Balance	Jun 30	Stationery Expense
			5,000		
				<b>Balance c/d</b>	<b>1,000</b>
			<u>5,000</u>		<u>5,000</u>
	<b>Jul 1</b>		<b>Balance b/d</b>	<b>1,000</b>	

**Step 3**

The \$4,000 of stationery expense is transferred to the profit and loss account:

**Stationery Expense**

		2019			2019
		Jun 30	Stationery Supplies	Jun 30	Profit and Loss
		<u>4,000</u>		<u>4,000</u>	

**Profit and Loss (extract)**

		2019			2019
		Jun 30	Stationery	Jun 30	Profit and Loss
		<u>4,000</u>		<u>4,000</u>	

If this adjusting entry was not made the profit for the year ended 30 June 2019 would have been overstated by \$4,000.

**Step 4**

The remaining stationery supplies are a current asset in the balance sheet of 30 June 2019:

**Furniture R Us**  
**Balance Sheet (extract)**  
**as at 30 June 2019**

**Current Assets**

Prepaid Insurance	600
<b>Stationery</b>	<b>1,000</b>

The stationery will be consumed within the next 12 months.

The following general journal entry is made to record the stationery supplies adjustment:

**General Journal**

Date	Details	Debit	Credit
2019 Jun 30	Stationery Expense  Stationery Supplies  <i>Stationery expense for the year.</i>	4,000	4,000

## Accrued Expenses

Accrued expenses are expenses generated in an accounting period but have not been paid by the end of that period.

Expenses, such as, telephone calls, wages and electricity are usually recorded in an accounting system only when they are paid. Therefore, at the end of an accounting period it is likely that some expenses generated in that period will not have been recorded.

An adjusting entry must be made in the accounting system to ensure that the accrued expenses are included in the calculation of the profit or loss for the current period and shown in the balance sheet.

On balance day the relevant expense account is debited with the unpaid expense and an accrued expenses (liability) account is credited.

### Example

Furniture R Us paid a total of \$97,000 in wages between 1 July 2018 and 27 June 2019.

The wages paid were recorded in a wages expense ledger account:

#### Wages (expense)

2019			
Jun 27	Balance	97,000	

Furniture R Us owes \$1,400 in wages for the 28, 29, and 30 of June 2019. The \$1,400 of wages owing is an expense as defined in the Framework and should be included in the calculation of the profit or loss for the year ended 30 June 2019. An adjusting entry is required.

### Step 1

The wages expense account is debited with the \$1,400 of unpaid wages and the accrued expenses account is credited with \$1,400:

#### Wages (expense)

2019			
Jun 27	Balance	97,000	
30	Accrued Expenses	1,400	

#### Accrued Expenses (liability)

2019		
Jun 30	Wages	1,400

**Step 1 continued**

The accrued expenses account is credited because it is a liability. In this example it is an amount of money owing to the employees of Furniture R Us.

**Step 2**

The \$98,400 of wages expense for the year is transferred to the profit and loss account:

<b>Wages</b>			
2019		2019	
Jun 27	Balance	97,000	Jun 30 Profit and Loss 98,400
30	Accrued Expenses	1,400	
		98,400	98,400

<b>Profit and Loss (extract)</b>		
2019		
Jun 30 Wages	98,400	

If this entry was not made the profit for the year ended 30 June 2019 would have been overstated by \$1,400.

**Step 3**

The \$1,400 of accrued expenses is a current liability in the balance sheet of 30 June 2019:

**Furniture R Us**  
**Balance Sheet (extract)**  
**as at 30 June 2019**

**Current Liabilities**

Accrued Expenses	1,400
------------------	-------

Furniture R Us will pay the \$1,400 of wages in July 2019.

The following general journal entry is made to record the accrued expenses adjustment:

**General Journal**

Date	Details	Debit	Credit
2019 Jun 30	Wages Accrued Expenses <i>Accrued wages on balance date.</i>	1,400	1,400

## Payment of Accrued Expenses in the Next Accounting Period

The accrued expenses account is closed when the wages owing are paid in the next accounting period.

### Example

On 11 July 2019 Furniture R Us paid \$4,500 in wages including the \$1,400 of wages owing on 30 June 2019.

This payment was recorded in the general journal:

**General Journal**

Date	Details	Debit	Credit
2019 Jul 11	Accrued Expenses Wages Cash at Bank <i>Payment of wages.</i>	1,400 3,100 4,500	

The general journal entry is posted into the general ledger:

### Accrued Expenses

2019 Jul 11	Bank	1,400	2019 Jun 30	Wages	1,400
----------------	------	-------	----------------	-------	-------

### Wages

2019 Jul 11	Bank	3,100	
----------------	------	-------	--

### Cash at Bank

2019 Jul 11	Accrued Expenses/Wages	4,500
----------------	---------------------------	-------

## **Unearned Income**

Unearned income is money received from a customer for a service that will be performed in the future or money received from a customer for inventory that will be supplied in the future. Unearned income is also known as income received in advance or prepaid income.

### **Example**

VIP Photographers is a wedding photography business. Customers pay in advance for this service.

For the year ending 30 June 2019 VIP Photographers received \$67,000 of fees in advance, excluding GST. The \$67,000 in fees was posted to the credit side of an unearned income (liability) account:

#### **Unearned Income (liability)**

	2019		
	Jun 30	Bank	67,000

VIP Photographers, for the year ended 30 June 2019, performed wedding photography services to the value of \$59,000. An adjusting entry is required to record the fees income for the year.

## Step 1

On balance day, the \$59,000 of fees earned is transferred to a fees income account.

## Step 2

The unearned income account is balanced off:

**Step 3**

The \$59,000 in fees income is transferred to the profit and loss account:

		<b>Fees</b>		
<b>2019</b>			<b>2019</b>	
<b>Jun 30</b>	<b>Profit and Loss</b>	<b>59,000</b>	<b>Jun 30</b>	<b>Unearned Income</b>
↓				
<b>Profit and Loss (extract)</b>				
			<b>2019</b>	
			<b>Jun 30</b>	<b>Fees</b>
				<b>59,000</b>

If this adjusting entry was not made the profit for the period would have been understated by \$59,000.

**Step 4**

The \$8,000 in unearned income is a current liability in the balance sheet of 30 June 2019:

**VIP Photographers**  
**Balance Sheet (extract)**  
**as at 30 June 2019**

**Current Liabilities**

Unearned Income	8,000
-----------------	-------

Unearned income represents a service owing by VIP Photographers that will be provided within the next 12 months.

An appropriate general journal entry is made to record the balance day adjustment:

**General Journal**

Date	Details	Debit	Credit
2019 Jun 30	Unearned Income Fees <i>Fees income for the year.</i>	59,000	59,000

## Accrued Income

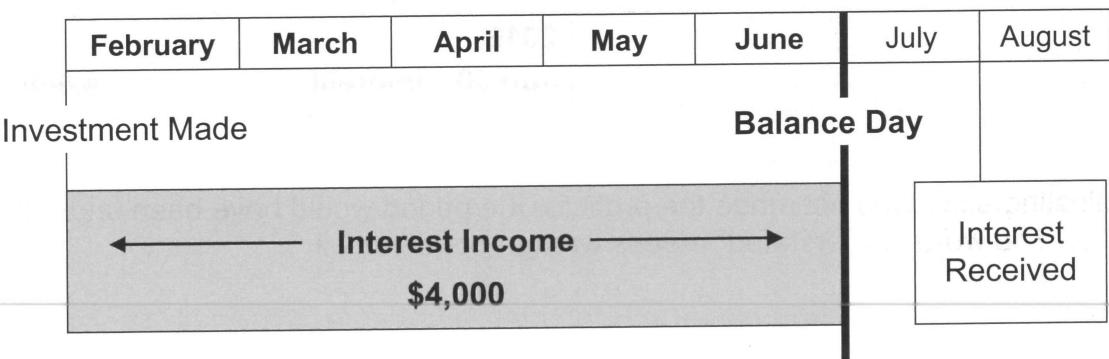
Accrued income is an amount of money owing to a business, from an income transaction, that has not been received by balance date.

### Example

On 1 February 2019 the A1 Business College invested \$80,000 with a bank for a six months fixed term. The interest will be received on 31 July 2019.

The interest income from 1 February to 30 June 2019 was \$4,000.

This situation can be set out in a diagram:



The \$4,000 of interest income should be included in the profit and loss account for the year ended 30 June 2019. In order to do this we must make a balance day adjustment.

### Step 1

An accrued income account is debited with \$4,000 and an interest income account is credited:

#### Accrued Income (asset)

2019		
Jun 30	Interest	4,000

#### Interest Income

2019			
	Jun 30	Accrued Income	4,000

The accrued income account is an asset. It is an amount of money owing to the business.

The interest income account is credited because, as the name suggests, it is income.

## Step 2

This balance day adjustment ensures that the correct amount of interest income is transferred to the profit and loss account for the year ended 30 June 2019:

<b>Interest Income</b>			
<b>2019</b>		<b>2019</b>	
<b>Jun 30 Profit and Loss</b>	<b>4,000</b>	<b>Jun 30 Accrued Income</b>	<b>4,000</b>
<b>Profit and Loss (extract)</b>			
		<b>2019</b>	
		<b>Jun 30 Interest</b>	<b>4,000</b>

If this adjusting entry was not made the profit for the period would have been understated by \$4,000. The word “understated” means wrong and too small.

## Step 3

The accrued income account is a current asset in the balance sheet of 30 June 2019:

**A1 Business College  
Balance Sheet (extract)  
as at 30 June 2019**

**Current Assets**

Accrued Income	4,000
----------------	-------

Accrued income is a current asset as it represents an amount of money owing to the business that will be received within the next 12 months.

An appropriate general journal entry is made to record the balance day adjustment:

**General Journal**

Date	Details	Debit	Credit
2019 Jun 30	Accrued Income  Interest Income  <i>Accrued interest on balance date.</i>	4,000	4,000

## Accrued Income in the Next Accounting Period

The accrued income ledger account is closed when the interest is received in the next accounting period.

### Example

On 31 July 2019 the A1 Business College received \$5,000 of interest. This interest included the \$4,000 of accrued interest to 30 June 2019.

This cash inflow was recorded in the general journal:

**General Journal**

Date	Details	Debit	Credit
2019 Jul 31	Cash at Bank Accrued Income Interest Income <i>Interest received.</i>	5,000	4,000 1,000

The general journal entry is posted into the general ledger:

**Cash at Bank**

2019 Jul 31	Accrued Income/Interest	5,000
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**Accrued Income**

2019 Jun 30	Interest	4,000	2019 Jul 31	Bank	4,000
----------------	----------	-------	----------------	------	-------

**Interest Income**

2019 Jul 31	Bank	1,000
----------------	------	-------

The above entry cancels the temporary asset, accrued income.

## Doubtful Debts

A business, at regular intervals of time, should review its debtors and should identify any debtors who are unlikely to pay their accounts.

It is important that the accounts receivable information shown in the balance sheet includes both the total amount owing from the debtors and the amount of money that is likely to be received from the debtors.

A debt that is unlikely to be paid is known as a **doubtful debt**. A doubtful debt is an expense to a business. A doubtful debt is not the same as a bad debt. A bad debt will definitely not be paid. A doubtful debt is unlikely to be paid but there is some possibility that the money owing will be received.

### Methods of Calculating the Doubtful Debts Expense

Doubtful debts is an expense that must be estimated. A number of methods can be used to estimate the doubtful debts expense. These methods are set out below.

#### Individual Review of Debtors

All debtor accounts are reviewed and those debtors that are likely to turn into bad debts are identified.

##### **Example**

Perth Traders has recently reviewed the status of each of its debtor accounts. This review has identified the following debtors as probable future bad debts:

Cold Traders	2,000
Hot Traders	7,000
	<hr/>
	\$9,000

Both of these debts have been outstanding (owing) for more than six months.

#### Percentage of Net Credit Sales Method

When this method is used the doubtful debts expense is a percentage of the net credit sales for an accounting period.

##### **Example**

The management of WA Traders, based on past experience and taking into account the current economic conditions, expects that about 2 percent of its net credit sales for the year will turn into bad debts.

The net credit sales for the year were \$100,000. Therefore, WA Traders has decided that its doubtful debts expense is:

$$2\% \times \$100,000 = \$2,000.$$

## Percentage of Aged Debtors Method

This method requires the use of a table in which the debtors are divided into different categories based on the number of days each debt has been outstanding (owing).

It is assumed that a percentage of some of the categories of debtors will turn into bad debts.

The likely bad debts in each category are added together to arrive at the doubtful debts expense.

### Example

West Coast Traders has divided its debtors into the following categories based on the length of time each debt has been outstanding:

Less than 30 days	30 to 60 days	61 to 90 days	91 to 120 days	More than 120 days
\$30,000	\$27,000	\$24,000	\$18,000	\$9,000

A percentage doubtful debts expense, based on past experience, is attached to each class of debt owing for 30 days or more:

Less than 30 days	30 to 60 days	61 to 90 days	91 to 120 days	More than 120 days
\$30,000	\$27,000	\$24,000	\$18,000	\$9,000
	1%	2%	3%	8%

The doubtful debts expense is equal to:

30 to 60 days	\$27,000	x	1%	=	\$270
61 to 90 days	\$24,000	x	2%	=	\$480
91 to 120 days	\$18,000	x	3%	=	\$540
120 plus days	\$9,000	x	8%	=	\$720
<b>Total</b>				<b>\$2,010</b>	

## Accounting Treatment of Doubtful Debts

The doubtful debts expense is recorded in the general journal and general ledger.

### **Example**

On 30 June 2018 the accounts receivable of Action Traders was \$740,000. On that date the management of the business reviewed each of its debtors and identified the following two debtors as unlikely to pay their accounts:

Inept Traders	\$5,000
Wild Traders	4,000
	<hr/>
	\$9,000

Therefore, the doubtful debts expense is \$9,000.

### **Step 1**

The following general ledger entry is made to record the doubtful debts adjustment:

A + E = L + EQ + I

#### **Doubtful Debts**

<b>2018</b>	
Jun 30	<b>Allowance for Doubtful Debts</b>

#### **Allowance for Doubtful Debts**

<b>2018</b>	
	<b>Jun 30 Doubtful Debts</b>

### **Debit Entry**

Doubtful debts is debited because it is an expense.

### **Credit Entry**

Allowance for doubtful debts is credited because it is a negative asset.

The credit entry in the allowance for doubtful debts account **indirectly** reduces the balance of accounts receivable. It is not possible to simply credit accounts receivable with the doubtful debts because these debts have not been written off as bad debts and the money owing might still be received.

**Step 2**

The doubtful debts expense is transferred to the profit and loss account:

**Doubtful Debts**

2018		2018	
Jun 30	Allowance for Doubtful Debts	Jun 30	Profit and Loss
	9,000		9,000

**Profit and Loss (extract)**

2018	
Jun 30	Doubtful Debts
	9,000

**Step 3**

The allowance for doubtful debts account is a negative asset. It is subtracted from accounts receivable in the balance sheet:

**Action Traders**  
**Balance Sheet (extract)**  
**as at 30 June 2018**

**Current Assets**

Accounts Receivable	740,000
Less Allowance for Doubtful Debts	(9,000) 731,000

**Step 4**

The following entry is made in the general journal:

**General Journal**

Date	Details	Debit	Credit
2018 Jun 30	Doubtful Debts Allowance for Doubtful Debts <i>Creation of an allowance for doubtful debts.</i>	9,000	9,000

## Adjusting an Allowance for Doubtful Debts

Where there is an **existing** allowance for doubtful debts, the bad debts cannot be written off to the profit and loss account as they were included, as doubtful debts, in a previous accounting period's profit and loss account. The bad debts must be written off against the allowance for doubtful debts. After the balance of the allowance for doubtful debts account has been reduced to zero, any remaining bad debts are transferred to the profit and loss account.

### **Example**

On 30 June 2018 Action Traders established an allowance for doubtful debts of \$9,000.

The following transactions occurred in the year ended 30 June 2019:

31 March      \$4,000 owing from Wild Traders was written off as a bad debt.

30 June      The allowance for doubtful debts was to be set at \$7,000.

The following steps are necessary to record these transactions.

---

### **Step 1**

The bad debts are written off in the general ledger:

<b>Bad Debts</b>			
<b>2019</b>			
<b>Mar 31</b>	<b>Accounts Receivable</b>		<b>4,000</b>

<b>Accounts Receivable</b>			
<b>2019</b>			
<b>Mar 1</b>	Balance (assumed)	800,000	<b>2019</b>
			<b>Mar 31</b>
			<b>Bad Debts</b>
			<b>4,000</b>

---

### **Step 2**

The \$4,000 of bad debts written off in March 2019 cannot be transferred to the profit and loss account for the year ended 30 June 2019.

The \$4,000 of bad debts was included in the \$9,000 of doubtful debts expense written off to the profit and loss account in 2018.

### Step 2 continued

The \$4,000 of bad debts, therefore, is transferred to the allowance for doubtful debts account:

<b>Bad Debts</b>					
2019			2019		
Mar 31	Accounts Receivable	4,000	Jun 30	Allowance for Doubtful Debts	4,000
<b>Allowance for Doubtful Debts</b>					
2019			2018		
Jun 30	Bad Debts	4,000	Jun 30	Doubtful Debts	9,000

### Step 3

On 30 June 2019 the required balance of the allowance for doubtful debts account is \$7,000.

To obtain this closing balance a further entry for doubtful debts must be made. The size of this doubtful debts adjustment can be calculated by reconstructing the allowance for doubtful debts account.

The \$7,000 required closing balance is entered on the debit side of the allowance for doubtful debts account:

<b>Allowance for Doubtful Debts</b>					
2019			2018		
Jun 30	Bad Debts	4,000	Jun 30	Doubtful Debts	9,000
	<b>Balance c/d</b>	<b>7,000</b>			

### Step 4

The debit side of the allowance for doubtful debts account is totalled at \$11,000. The same total is entered on the credit side:

<b>Allowance for Doubtful Debts</b>					
2019			2018		
Jun 30	Bad Debts	4,000	Jun 30	Doubtful Debts	9,000
	<b>Balance c/d</b>	<b>7,000</b>			
		<b>11,000</b>			<b>11,000</b>

**Step 5**

The difference between the two sides of the allowance for doubtful debts account is a ~~debit~~ \$2,000 missing figure. This \$2,000 missing figure is the amount by which the allowance for doubtful debts account must be increased to leave it with a balance of \$7,000. This \$2,000 amount is a further entry for doubtful debts:

**Allowance for Doubtful Debts**

2019		2018			
Jun 30	Bad Debts	4,000	Jun 30	Doubtful Debts	9,000
	Balance c/d	7,000			
		<hr/>			
		11,000			11,000

**Doubtful Debts**

2019	
Jun 30	Allowance for Doubtful Debts 2,000

**Step 6**

These ledger entries are supported by a series of general journal entries.

**Entry 1**

Purpose: to write off the bad debts:

**General Journal**

Date	Details	Debit	Credit
2019 Mar 31	Bad Debts Accounts Receivable <i>Amount owing from Wild Traders written off as a bad debt.</i>	4,000	4,000

**Entry 2**

Purpose: to transfer the bad debts to the allowance for doubtful debts account:

**General Journal**

Date	Details	Debit	Credit
2019 Jun 30	Allowance for Doubtful Debts Bad Debts  <i>Transfer of bad debts.</i>	4,000	4,000

**Entry 3**

Purpose: to set the allowance for doubtful debts balance at \$7,000:

**General Journal**

Date	Details	Debit	Credit
2019 Jun 30	Doubtful Debts Allowance for Doubtful Debts  <i>Allowance for doubtful debts set at \$7,000.</i>	2,000	2,000

## Questions



Questions 1 to 4: prepaid expenses adjustment

### Question 1

On 1 May 2019 the Oz Business College paid \$39,000 rent of office space for the **next 6 months**. The prepaid rent was recorded in an asset ledger account:

**Prepaid Rent (asset)**

2019						
May 1	Bank		39,000			

The Oz Business College calculates its profit or loss each year ending 30 June. That is, balance date is 30 June.

### Required

- 1 What is the rent **expense** for the year ending 30 June 2019?

May	June	July	August	September	October
<b>Expense</b>	<b>Asset</b>				
1 May 2019	30 June 2019				
Paid	<b>Balance Date</b>				

$$\frac{6}{\text{---}} \times \$39,000 = \$$$

- 2 Prepare the general journal entry to record the **rent expense** for the year ending 30 June 2019.

**General Journal**

Date	Details	Debit	Credit

**Question 1 continued****Required**

- 3 Carry out the balance day adjustment in the general ledger.

**Prepaid Rent (asset)**

2019 May 1	Bank	39,000			

**Rent Expense**


- 4 Complete the profit and loss ledger account for the year ended 30 June 2019.

**Profit and Loss**

2019 Jun 30	Wages	30,000	2019 Jun 30	Fees	51,000
	Advertising	2,000			

- 5 If this balance day adjustment had not been carried out the **profit** would have been:

- a understated (wrong and too low) by \$13,000
- b overstated (wrong and too high) by \$13,000

- 6 Prepare the current assets section of the balance sheet on 30 June 2019.

**Oz Business College  
Balance Sheet (extract)  
as at 30 June 2019**

<b>Current Assets</b>	

**Question 1 continued****Required**

- 7 If this balance day adjustment had not been carried out the **prepaid rent** in the balance sheet on 30 June 2019 would have been:

- a understated by \$13,000
- b overstated by \$13,000

**Solution Check**

Profit = \$6,000

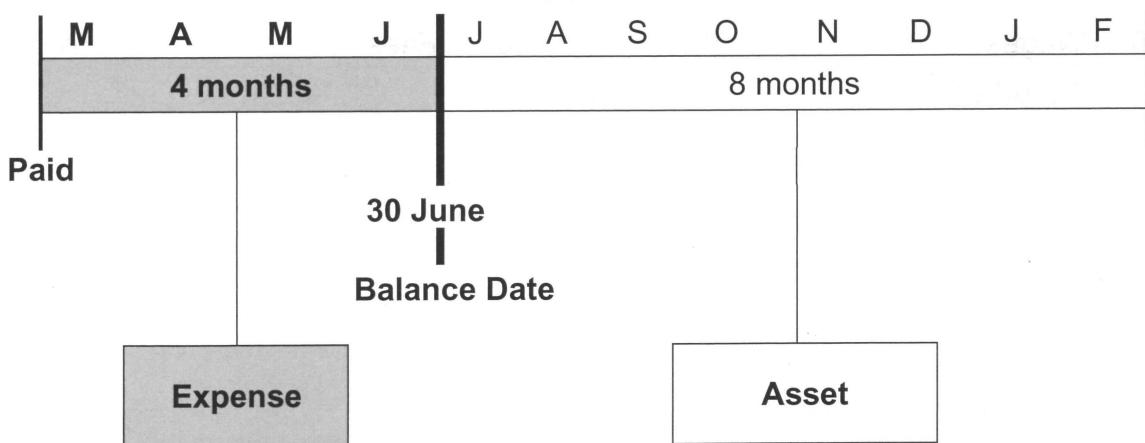
**Question 2**

On 1 March 2019 Car Care paid \$2,400 for a **12 months** insurance policy.

Car Care calculates its profit or loss each year ending 30 June.

**Required**

- 1 Calculate the **insurance expense** for the year ending 30 June 2019.

**Insurance expense**

$$\frac{1}{12} \times \$2,400 = \$$$

**Question 2 continued****Required**

- 2 Prepare the general journal entry to record the **insurance expense** for the year ending 30 June 2019.

**General Journal**

Date	Details	Debit	Credit

- 3 Carry out the balance day adjustment in the general ledger.

**Prepaid Insurance (asset)**

2019 Mar 1	Bank	2,400			


- 4 Complete the profit and loss ledger account for the year ended 30 June 2019.

**Profit and Loss**

2019 Jun 30	Wages	24,200	2019 Jun 30	Fees	29,000
	Telephone	1,000			

- 5 If this balance day adjustment had not been carried out the **profit** would have been:

- a understated (wrong and too low) by \$800
- b overstated (wrong and too high) by \$800

## Question 2 continued

## **Required**

- 6 Prepare the current assets section of the balance sheet on 30 June 2019.

**Car Care**  
**Balance Sheet (extract)**  
as at 30 June 2019

Current Assets	

- 7 If this balance day adjustment had not been carried out the **prepaid insurance** in the balance sheet on 30 June 2019 would have been:

a overstated by \$800      b understated by \$800

8 Carry out the rent balance day adjustment for Nannup Traders.

**Nannup Traders  
Trial Balance (extract)  
as at 30 June 2022**

Ledger Account Title	Debit	Credit
Prepaid rent	27,000	

## **Additional Information**

The rent expense for the year ended 30 June 2022 was \$26,100.

## **Profit and loss account entry**

## Profit and Loss (extract)

2022 Jun 30	Rent				
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## Balance sheet entry

## Nannup Traders Balance Sheet (extract) as at 30 June 2022

<b>Current Assets</b>	

## Solution Check

**Profit = \$3,000**

**Question 3**

**Cooee Costume Hire  
Trial Balance (extract)  
as at 30 June 2019**

Ledger Account Title	Debit	Credit
Prepaid Rent	\$39,100	

**Additional Information**

Rent **expense** for the year ending 30 June 2019 was \$38,400.

**Required**

- 1 Prepare the general journal entry to record the **rent expense** for the year ending 30 June 2019.

**General Journal**

Date	Details	Debit	Credit

- 2 Carry out the balance day adjustment in the general ledger.

**Prepaid Rent**

2019 Jun 30	Balance	39,100			


- 3 Record the rent expense in the profit and loss ledger account.

**Profit and Loss (extract)**


**Question 3 continued****Required**

- 4 Prepare the current assets section of the balance sheet on 30 June 2019.

**Cooee Costume Hire  
Balance Sheet (extract)  
as at 30 June 2019**

<b>Current Assets</b>	

- 5 On 1 September 2026 Bob Cat Rentals paid \$1,980 + \$198 GST = \$2,178 for a 12 months insurance policy. The prepaid insurance in the balance sheet on 30 June 2027 was:
- a \$330
  - b \$1,650
  - c some other amount
- 
- 6 On 1 April 2025 Joe's Pizzas paid 6 months rent in advance. Joe's Pizzas calculates its profit or loss each year ended 30 June. The annual rental is \$7,320 + \$732 GST = \$8,052. The prepaid rent in the balance sheet of 30 June 2025 was:
- a \$2,440
  - b \$1,830
  - c some other amount
- 7 A prepaid expense:
- a contains future economic benefits
  - b exists because of a past transaction
  - c is under the control of a business
  - d all of the above
- 8 On 30 June 2028 a business had the following items: prepaid rent \$1,900, cash at bank \$3,200, loan from bank \$5,400, inventory \$11,400, accounts payable \$7,200, GST payable \$1,600, accrued expenses \$1,400, motor vehicle \$8,100, GST credits \$1,400 and accounts receivable \$3,700. The total current assets of the business on this date were:
- a \$22,700
  - b \$21,600
  - c some other amount



### Questions 4 to 6: inventory of supplies adjustment

#### Question 4

On 1 July 2018 the Wrightway Business College paid \$900 for stationery, including paper, printer cartridges and pens.

The stationery purchased was recorded in a stationery supplies ledger account:

**Stationery Supplies (asset)**

2018			
Jul 1	Bank	900	

During the year ending 30 June 2019 a total of \$700 of stationery was consumed.

That is, the stationery **expense** for the year is \$700.

#### Required

- 1 Prepare the general journal entry to record the stationery expense for the year ending 30 June 2019.

**General Journal**

Date	Details	Debit	Credit

- 2 Carry out the balance day adjustment in the general ledger.

**Stationery Supplies (asset)**

2018				
Jul 1	Bank	900		

**Stationery Expense**


**Question 4 continued****Required**

- 3 Complete the profit and loss ledger account.

**Profit and Loss**

2019 Jun 30	Wages	4,000	2019 Jun 30	Fees	8,000
	Advertising	1,300			

- 4 If the supplies adjustment had not been carried out the **profit** for the year ended 30 June 2019 would have been:
- a understated by \$700
  - b overstated by \$700
- 5 Prepare the current assets section of the balance sheet on 30 June 2019.

**Wrightway Business College**  
**Balance Sheet (extract)**  
**as at 30 June 2019**

Current Assets	

- 6 If the supplies adjustment had not been carried out the **supplies (asset)** in the balance sheet on 30 June 2019 would have been:
- a understated by \$700
  - b overstated by \$700

**Solution Check**

Profit = \$2,000

## Question 5

**Redmond Business College**  
**Trial Balance (extract)**  
as at 30 June 2019

Ledger Account Title	Debit	Credit
Stationery Supplies	3,700	
Prepaid Rent	8,400	

## **Additional Information**

- a Stationery expense for the year was \$3,500.
  - b Rent expense for the year was \$8,100.

The business calculates its profit or loss each year ending 30 June.

## **Required**

- 1 Prepare the general journal entries to record the stationery and rent expenses for the year ending 30 June 2019.

## **General Journal**

- 2 Carry out the balance day adjustments in the general ledger.

## Stationery Supplies

2019 Jun 30	Balance	3,700			

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