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This file includes 3 Parts (all in this file)

1- Theoretical Questions
2- Exam Numericals
3- Book Numericals

IMPORTANT QUESTION

FOR FINANCIAL ACCOUNTING

Part 1 (Theoretical Questions)

0- Define balancing in accounting

Balancing means to equate both sides of the account, i.e., the debit and credit sides of an account must be equal/balanced.

1- Define Book Keeping

Bookkeeping is the recording of financial transactions, and is part of the process of accounting in business.Transactions include purchases, sales, receipts, and payments by an individual person or an organization/corporation

2- Define Services Business

A commercial enterprise that provides work performed in an expert manner by an individual or team for the benefit of its customers. The typical service business provides intangible products, such as accounting, banking, and consulting, cleaning, landscaping, education, insurance, treatment, and transportation services.

3-Define Return Outward

Return outwards refer to the goods returned by an organization to its suppliers. They are goods which were purchased from suppliers, however, because of being unsatisfactory or a different reason were returned back to the suppliers, they are also called Purchase returns.

4-Define Posting

Posting is the act of moving debit and credit account balances from individual journals to their corresponding ledgers. These ledgers are later used to create a trial balance used to generate the income statement, balance sheet, and other financial statements.

5-Define Narration

A narration is a description of the journal entry. It is a short description which provides details about an entry. As just debit and credit does not provide required information of the transaction, narration is a must. Thus narration provides information which is not reflected in the account.

6-Define Accounting Cycle

The accounting cycle is the process of accepting, recording, sorting, and crediting payments made and received within a business during a particular accounting period.Journal -> Trial -> General Ledger -> Cash Book and Bank reconciliation Statement ->Final Accounts

7-Define Rebate

Return of a portion of a purchase price by a seller to a buyer, usually on purchase of a specified quantity, or value, of goods within a specified period. Unlike discount (which is deducted in advance of payment), rebate is given after the payment of full invoice amount. For example: I bought a printer at an online store for sixty dollars and its purchase price ended up being forty dollars after I sent in a form for a rebate of twenty dollars two weeks later.

8- Define Revenue Expenditure

A revenue expenditure, also called an income statement expenditure, is a cost related to assets that are not capitalized because they will not provide a financial benefit in future periods. Revenue expenditures are more often called expenses.

9-Deine Trial Balance

A trial balance is a list of all the general ledger accounts (both revenue and capital) contained in the ledger of a business. This list will contain the name of each nominal ledger account and the value of that nominal ledger balance. Each nominal ledger account will hold either a debit balance or a credit balance. The debit balance values will be listed in the debit column of the trial balance and the credit value balance will be listed in the credit column. The trading profit and loss statement and balance sheet and other financial reports can then be produced using the ledger accounts listed on the same balance

10-Define Account Receivable

Accounts receivable is the money that a company has a right to receive because it had provided customers with goods and/or services. For example, a manufacturer will have an account receivable when it delivers a truckload of goods to a customer on June 1 and the customer is allowed to pay in 30 days.

11-Define Accounting Conventions

An accounting convention is a common practice used as a guideline when recording a business transaction. It is used when there is not a definitive guideline in the accounting standards that govern a specific situation. Thus, accounting conventions serve to fill in the gaps not yet addressed by accounting standards.

12-Define Reserve

When a company earns a profit at the end of a financial year, a certain portion of it is retained in the business to meet future contingencies, growth prospects etc. This amount of money kept aside is termed as Reserves. They help in fortifying the financial position of a company and can be used for various purposes such as expansion, stable dividend repayments, legal requirements, meeting contingencies, improving the financial situation, investments etc. It is also referred to as retained earnings.

13-Define Accrued Liabilities

Accrued liability means a company has incurred an expense for a good or service but has not paid for it yet. Accrued liabilities are expenses that a company incurs during a period but doesn’t pay in the same period. It can also be an obligation that a company has assumes in a period but has not received a corresponding invoice during the period.

14-Define Revenue Receipt

Revenue receipts are funds received by a business as a result of its core business activities. It leads to an overall increase in the total revenue of the company. These funds are generated from a firm’s operating activities hence they are shown inside trading and profit and loss account and not in a balance sheet. Few common examples are receipts from sale of good and services, discount received from creditors or suppliers, interests earned, dividends received, rent received, commission received, bad-debts recovered, income from other sources, etc. 15-BalancingBalancing is the Closing up of accounts at the end of an accounting period, by bringing the totals of their debit and credit sides into agreement, and thus to determine the profit or loss made during that period. The difference between the sum of the two sides of an account is called the balance.

16-Define Matching Concept

The matching concept is a founding principle of accounting. In general, it means that expenses are recorded (matched) with the income that is generated from those expenses. The matching principle requires that revenues and any related expenses be recognized together in the same period.

17- How many types of business transactions are there in accounting?

There are two types of transactions in accounting, i.e., revenue and capital.

18- What is the balance sheet?

It is a statement that states all the liabilities and assets of the company at a certain point.

19- Define fictitious assets

These are the assets that cannot be shown or touch. Fictitious assets can only be felt, such as goodwill, rights, etc.

20- What is the meaning of a perpetual or periodic inventory system?

In the perpetual inventory system, the accounts are adjusted on a continual basis. In this inventory system, the accounts are changed periodically.

21- What is the basic accounting equation?

Accounting is all about assets, liabilities, and capital. Therefore, the accounting equation is:

Assets = Liabilities + Owners Equity.

22- Name different branches of accounting

There are three branches of accounting:

1. Financial accounting
2. Management accounting
3. Cost accounting

23- Define depreciation and its types

Depreciation can be defined as the value of an asset that is decreasing as it is in use. It has two types, such as:

1. Straight line method
2. Diminishing value method
3. Annuity method
4. Depletion method
4. Written down value method.

24- Define fair value in accounting

Fair value is the measurement of liabilities and assets according to the current value of the market. It shows the estimated price at which any assets are sold. Liability shows third party transactions under the current condition of the market.

25- What are the rules for debit and credit for different accounts to increase the amount in your business accounts?

The rules for debit and credit for different accounts are:

For a capital account, credit to increase it and debit to decrease it.

For an asset account, debit to increase it and credit to decrease it.

For a liability account, credit to increase it and debit to decrease it.

For an expense account, debit to increase it, and credit to decrease it.

For an income account, credit to increase it and debit to decrease it.

26- What is General ledger account?

The general ledger account is an account used to record all the information. It can be expenses and income types that are recorded into separate accounts.

In this account debits and credits, transactions are entered in one place and kept balanced.

27- What is the general classification of accounts that usually ledger account involve?

The general classification of accounts that usually ledger account involves are:

Assets: cash, accounts receivable

Liabilities: accounts payable, loans payable

Stockholders' equity: common stock

Operating revenues: revenues through sales

Operating expenses: rent expense, salaries expense

Non-operating revenues and gains: investment income, gain on disposal of equipment

Non-operating revenues and losses: interest expense, loss on disposal of equipment

28- Mention whether the account "Cash" will be credited or debited when a company pays a bill?

The account "Cash" will be credited when a company pays a bill.

29- What is the main difference between accumulated depreciation and depreciation expense?

The difference between accumulated depreciation and depreciation expense is that:

Accumulated depreciation is the total amount of depreciation that has been taken on a company's assets up to the date of the balance sheet.

Depreciation expense is the amount of depreciation that is reported on the income statement.

30- List out some of the examples for liability accounts?

Some of the examples of liability accounts are:

Accounts payable

Accrued expenses

Short-term loans payable

Unearned or deferred revenues

Installment loans payable

Current portion of long-term debt

Mortgage loans payable

31- How to adjust entries into account?

Entries can be adjusted into account by sorting entries into five categories:

Accrued expenses: Expenses have been incurred, but the vendor's invoices are not generated or processed yet

Accrued revenues: Revenues have been earned, but the sales invoices are not generated or processed yet.

Deferred revenues: Money was received in advance of having been paid or earned.

Deferred expenses: Money was paid for a future expense.

Depreciation expense: An asset purchased in one period must be allocated to expense in each of the accounting periods of the asset's useful life.

32- What are the activities that are included in the Cash Flow Statement?

The cash flow statement showcase the cash generated and used during the year or months. Various activities that are involved for the cash flow are

Operating activities: Business activities accounting to cash

Investing activities: Sale and purchase of equipment or property

Financial activities: Purchase of stock and own bonds

Supplemental information: exchange of significant items that don't involve cash

33- List out things that fall under intangible assets

Things that fall under intangible asset are:

Patents

Copyrights

Trademarks

Brand names

Domain names

34- What is a trial balance in accounting?

In accounting, the trial balance is an accounting report that lists the balances in each of an organization's general ledger accounts. This is done at the end of the posting journal entry to ensure that there are no posting errors.

35- Explain the term account payable

Account payable is referred to as the amount the company owes to its suppliers, its employees, and its partners. In other words, it is the basic cost levied on the company to run a business process that is outstanding.

Account payable for one company may be account receivable for another firm or company.

36- What does the financial statement of the company include?

Financial statement of the company includes various information like:

Balance Sheet (Assets, liabilities, and equity)

Income statement (Profit or Loss statement)

Equity statement

Cash flow statement

37- What is working capital?

Working capital is a financial metric that calculates the resources available to the company to finance its day-to-day operations. It is typically calculated by deducting current liabilities from current assets.

38- What is ledger?

A ledger can be referred to as an accounting book that keeps the record of journal entries in chronological order to individual accounts. The process of recording this journal entries is known as posting.

39- Mention the types of ledgers

There are three types of ledger

General ledger

Debtors ledger

Creditors ledger

40- What are liabilities?

Liability can be defined as an obligation towards another company or party. It may consist of delivering goods, rendering services, or paying money. They are the opposite of assets, and it may include:

Account payable

Interest and dividend payable

Bonds payable

Consumer deposits

Reserves for federal taxes

Short term loans

41- what is the basic difference between asset, equity, and liabilities?

Asset describes what financial institute (bank) or people owe.

Liabilities is something you owe people or organization.

Equity is something you own, for example, the amount of your house loan you paid off.

42- Define fixed asset

Fixed asset are assets which are tangible in nature. It is not used to sell in the near future and from which future benefits are derived.

IMPORTANT QUESTION

FOR FINANCIAL ACCOUNTING

Part 2 (NUMERICALS)

Q1#) A list of accounts for Maple Inc. at December 31, 2010, follows:

Accounts Receivable	$ 2,359	Land	$20,000
Advertising Expense	4,510	Purchase Discounts	800
Buildings and Equipment, Net	55,550	Purchases	40,200
Capital Stock	50,000	Retained Earnings, January 1, 2010	32,550
Cash	590	Salaries Expense	25,600
Depreciation Expense	2,300	Salaries Payable	650
Dividends	6,000	Sales	84,364
Income Tax Expense	3,200	Sales Returns	780
Income Tax Payable	3,200	Transportation-In	375
Interest Receivable	100	Utilities Expense	3,600
Inventory:			
January 1, 2010	6,400		
December 31, 2010	7,500		

Required:

i. Determine Cost of Goods Sold (COGS) for December 31, 2010.
ii. Determine Net Income for December 31, 2010.
iii. Prepare a balance sheet dated December 31, 2010.

#Solution#

COGS:

***Beginning inventory: 6,400**

Purchases	+ 40,200
Purchase Discounts	- 800
Transportation-In	+ 375

***Net Purchase: 39,775**

***Ending Inventory: 7,500**

COGS = Beginning Inventory + Net Purchase – Ending Inventory

COGS = 6,400 + 39,775 – 7,500

***COGS = 38,675**

Net-Income:

Advertising Expense	4,510
Depreciation Expense	2,300
Salaries Expense	25,600
Utilities Expense	3,600
Income-Tax Expense	3,200

***Total Expense: 39,210**

Sales	+ 84,364
Sales Return	- 780
COGS	- 38,675

***Total Revenue: 44,909**

Net-Income: Total Revenue – Expense

Net-Income: 44,909 – 39,210

***Net-Income = 5,699**

Balance Sheet:

O.C:

O.C. => Capital Stock + Retained Earning = 50,000 + 32,550 = 82,550

Withdraw:

Withdraw => Dividends = 6,000

O.E:

O.E => O.C. + Net-Income – Withdraw

O.E = 82,550 + 5,699 – 6,000

***O.E = 82,249**

Assets		Liability + O.E	
Cash	590	**Liabilities:**	
Inventory	7,500	Salaries Payable	650
Account Receivable	2,359	Income-Tax Payable	3,200
Interest Receivable	100		
Land	20,000	**O.E:**	
Building & Equipment, Net	55,550	O.E.	82,249
TOTAL	86,099	TOTAL	86,099

Problem 1

TRANSACTION ANALYSIS, JOURNALIZING, POSTING TO THE ACCOUNTS & TRIAL BALANCE

1) The business received $30,000 cash that Gillen invested to begin her travel agency.
2) Gillen paid $20,000 cash for land to be used as an office location.
3) Gillen purchased $500 in office supplies on account payable. → Payment of 3
4) Gillen paid $300 on the account payable created in transaction 3.
5) Gillen remodeled her home with personal funds and a loan from Nations Bank. → not business activity
6) Gillen withdrew $2,100 cash for personal living expenses.
→ from Business

ASS #01 cash↑ o.c↑

* Problem #01 :-

Date	G.J	Debit	Credit
1-May	cash	30,000	
	O.C		30,000
2-May	land	20000	
	cash		20,000
3-May	off sup	500	
	A/P		500
4-May	A/P	300	
	cash		300
5-May	O.W	2100	
	cash		2100

• T.accounts →

cash

30,000	300
	2100
	20000
7600	

land

20,000	
20,000	

O.C

	30000
	30000

off sup

500	
500	

A/P

	500
300	
	200

O.W

2100	
2100	

Trial Balance:-

T. Balance	Debit	Credit
cash	7600	
Land	20000	
O/S sup	500	
A/P		200
O.C		30000
O.W	2100	
	30200	30200

Problem 2

Expanded Problem Including Revenues and Expenses

Let's account for the revenues and expenses of the law practice of Jeff Hatton, Attorney, for the month of July 20X1

1) Jeff Hatton invested $10,000 cash in a business bank account to open his law practice
2) Hatton performed service for a client and collected $3,000 cash → Revenue
3) Hatton performed service for a client and billed the client for $500 on account receivable.
4) Hatton earned $700 service revenue by performing legal service for a client. The client paid Hatton $300 cash immediately. Hatton billed the remaining $400 to the client on account receivable.
5) Hatton paid the following cash expenses: office rent, $900; employee salary, $1,500; and utilities, $500.
6) Hatton received a telephone bill for $120 and will pay this expense next week.
7) Hatton collected $200 cash from the client established in transaction 3.
8) Hatton paid the telephone bill that was received and recorded in transaction 6.
9) Hatton withdrew $1,100 cash for personal use.

* Problem # 02 :-

	G.J	Debit	Credit
1-May	Cash	10,000	
	O.C		10,000
2-May	Cash	3,000	
	ser Rev		3,000
3-May	A/R	500	
	ser Rev		500
4-May	Cash	300	
	A/R	400	
	ser Rev		700
5-May	off rent	900	
	emp sal	1,500	
	utilities	500	
	cash		2900
6-May	telp exp	120	
	A/P		120
7-May	cash	200	
	A/R		200
8-May	A/P	120	
	cash		120
9-May	O.W	1,100	
	cash		1,100

Cash

10,000	2,900
3,000	1,100
300	120
200	
9380	

O.C

	10,000
	10,000

Ser Rev

	3000
	500
	700
	4200

A/R

500	200
400	
700	

offs rent

900	
900	

emp sal

1500	
1500	

utilit

500	
500	

rep exp

120	
120	

A/P

120	120
	0

O.W

1100	
1100	

* Trial Balance

General Journal	Debit	Credit
Cash	9380	
A/R	700	
~~off~~ A/P		0
~~O.W~~ O.C		10,000
O.W	1100	
Ser Rev		4200
off rent	900	
emp sal	1500	
utilities	500	
telp exp	120	
	14200	14200

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IMPORTANT QUESTION

FOR FINANCIAL ACCOUNTING

Part 3 (TOPIC WISE)

QUESTION on Accounting Equation

Q: Tom Jones is the owner and operator of Jones Enterprise, a motivational consulting business. At the end of its accounting period, December 31, 2009, Jones Enterprise has assets of $760,000 and liabilities of 240,000.

Use the accounting equation to calculate the answers in each of the following:

a) Tom Jones, capital, as of December 31, 2009

b) Tom Jones, capital, as of December 31, 2010, assuming that assets increased by $120,000 and liabilities increased by $72,000 during 2010

c) Tom Jones, capital, as of December 31, 2010, assuming that assets decreased by $60,000 and liabilities increased by $21,600 during 2010

d) Tom Jones, capital, as of December 31, 2010, assuming that assets increased by $100,000 and liabilities decreased by $38,400 during 2010

e) Net income during 2010, assuming that as of December 31, 2010, assets were $960,000, liabilities were $156,000, and there were no additional investments or withdrawals.

SOLUTIONS

a) and b):

	ASSETS =	OWNER'S EQUITY +	*LIABILITIES*
December 31, 2009	$760,000	a) $520,000	$240,000
Changes during 2010	+ $120,000		+ $72,000
December 31, 2010	$880,000	b) $568,000	$312,000

To get the answer for a) above, we simply use the basic accounting equation.

ASSETS = OWNER'S EQUITY + LIABILITIES

If we turn this around to make owner's equity the subject, then:

OWNER'S EQUITY = ASSETS - LIABILITIES

So we take the assets and minus the liabilities.

In other words, $760,000 - $240,000 = $520,000

For b) we first add the changes to assets and liabilities to get their new balances. Then we work out the new balance of owner's equity in the same way: $880,000 - $312,000 = $568,000

The answers below for c) and d) basically work in the exact same way - get the new balance of assets and liabilities and then use these new balances to work out the new balance of equity.

c):

	ASSETS =	OWNER'S EQUITY +	*LIABILITIES*
December 31, 2009	$760,000	**$520,000**	$240,000
Changes during 2010	- $60,000		+ $21,600
December 31, 2010	**$700,000**	**c) $438,400**	**$261,600**

d):

	ASSETS =	OWNER'S EQUITY +	*LIABILITIES*
December 31, 2009	$760,000	**$520,000**	$240,000
Changes during 2010	+ $100,000		- $38,400
December 31, 2010	**$860,000**	**d) $658,400**	**$201,600**

e):

	ASSETS =	OWNER'S EQUITY +	*LIABILITIES*
December 31, 2009	$760,000	**$520,000**	$240,000
Changes during 2010 (net income)		**e) $284,000**	
December 31, 2010	$960,000	**$804,000**	$156,000

This last part (e) is a bit trickier than the previous ones.

What you have to do is first calculate the new balance of owner's equity.

The net income (also simply known as net profit) is the change for the year, and is the difference between the old and new balances of owner's equity.

In other words, \$804,000 - \$520,000 = \$284,000

Question on
Basic Accounting Journal Entries Exercise

Q: On March 1, 2008, Giny Tyler established Seltzer Reality. Ginny completed the following transactions during the month of March:

a. Opened a business bank account with a deposit of 30,000 from personal funds.
b. Purchased supplies (pens, file folders, papers, etc.) on account, 2,650.
c. Paid creditor on account, 1,500.
d. Earned sales commissions, receiving cash, 36,750.
e. Paid rent on office and equipment for the month, 5,200.
f. Withdrew cash for personal use, 8,000.
g. Paid automobile expenses (including rental charge) for month, 2,500, and miscellaneous expenses, 1,200.
h. Paid office salaries, 9,250.
i. Determined that the cost of supplies on hand was 900; therefore, the cost of supplies used was 1,750.

Indicate the effect of each transaction.

a). Cash on hand.......30,000.00
Investment................30,000.00
To record investment by owner.

b). Supplies..............2,650.00
Accounts Payable.............2,650.00
To record purchase supplies on account.

c). Accounts Payable........1,500.00
Cash........................1,500.00
To record payment to creditor.

d). Cash...................36,750.00
Sale commission...............36,750.00
To record earned sale commission.

e). Rent expense..............5,200.00
Cash............................5,200.00
To record paid for office and equipment rental

f). Withdraw................8,000.00
Cash..........................8,000.00
To record withdraw by owner.

g). Rent expense...............2,500.00
Miscellaneous expense......1,200.00
Cash............................3,700.00
To record payment for automobile & miscellaneous expense.

h). Salaries expense.........9,250.00
Cash..........................9,250.00
To record payment for office staff salaries.

i). Supplies expense...........1,750.00
Supplies on hand................1,750.00
To record supplies expense for march.

Question on Journal Entries and Ledger

Q: Mr Robert commenced business on 1st January, 2011 with a capital of $100,000 in cash. On the same date he opened the bank account in ADCB and deposited $20,000. During the month of January 2011 the following transactions took place:

Jan 1 Bought goods for cash 70,000

2 Sold goods to Steve Co. (Credit) 38,000

15 Sold goods for cash 9,000

21 Steve Co. paid by cheque 35,000

22 Stationery bill paid by cheque 2,000

22 Telephone bill by cash 500

31 Paid rent by cash 2,000

Paid salaries by cash 3,000

Withdrew cash personal use 5,000

Required:
Record journal entries for the transactions and post them to ledgers.

Solution:

Journals:

Jan 1 Dr Cash on hand 80,000
Dr Bank 20,000
Cr Capital 100,000

Note that in most accounting questions you won't have to account for "Cash on hand" and "Bank" in separate accounts. In most questions I just combine these into "Bank." But in this question they specifically talk about opening the bank account with $20,000 of the $100,000, which indicates they kept cash on hand in addition to the bank account, which needs to be accounted for.

1 Dr Purchases/Inventory 70,000
Cr Cash on hand 70,000

Note that it's "Purchases" for a periodic system of inventory and "Inventory" if it's the perpetual system. See the tutorial on perpetual and periodic inventory for more information.

2. Dr Debtors 38,000
Cr Sales 38,000

15. Dr Cash on hand 9,000
Cr Sales 9,000

21. Dr Bank 35,000
Cr Debtors 35,000

22. Dr Stationery expense 2,000
Cr Bank 2,000

22. Dr Telephone expense 500
Cr Cash on hand 500

31. Dr Rent expense 2,000
Cr Cash on hand 2,000

31. Dr Salaries 3,000
Cr Cash on hand 3,000

31. Dr Drawings 5,000
Cr Cash on hand 5,000

Ledger:

Dr — Cash on hand — Cr

2011		$	2011		$
Jan 1	Capital	80,000	Jan 1	Purchases/inventory	70,000
15	Sales	9,000	22	Telephone expense	500
			31	Rent	2,000
			31	Salaries	3,000
			31	Drawings	5,000
				Balance c/f	8,500
		89,000			89,000
Feb 1	Balance b/f	8,500			

Dr — Bank — Cr

2011		$	2011		$
Jan 1	Capital	20,000	Jan 22	Stationery	2,000
21	Debtors	35,000		Balance c/f	53,000
		55,000			55,000
Feb 1	Balance b/f	53,000			

Dr — Capital — Cr

			2011		$
			Jan 1	Cash on hand	80,000
			1	Bank	20,000
					100,000

Dr — Purchases / Inventory — Cr

2011		$			
Jan 1	Cash on hand	70,000			

Dr — Debtors control — Cr

2011		$	2011		$
Jan 2	Sales (SJ)	38,000	Jan 21	Bank	35,000
				Balance c/f	3,000
		38,000			38,000
Feb 1	Balance b/f	3,000			

Dr — Sales — Cr

			2011		$
			Jan 2	Debtors	38,000
			Jan 15	Cash on hand	9,000
					47,000

Dr	Stationery expense		Cr
2011		$	
Jan 22	Bank	2,000	

Dr	Telephone expense		Cr
2011		$	
Jan 22	Cash on hand	500	

Dr	Rent expense		Cr
2011		$	
Jan 31	Cash on hand	2,000	

Dr	Salaries		Cr
2011		$	
Jan 31	Cash on hand	3,000	

Dr	Drawings		Cr
2011		$	
Jan 31	Cash on hand	5,000	

Question on Creditors, Purchases, Cost of Goods Sold

Balances at 31 January 2009:
Debtors control account............................$32,400
Creditors control account..........................$25,200
Inventory..$30,000

Balances at 28 February 2009:
Debtors control account............................$24,000
Creditors control account..........................$29,160
Inventory..$36,000

Extract from cash payments journal at 28 February 2009:
Payments to creditors................................$41,040

Additional Information:
a) Gross profit mark-up is 20% on cost
b) Inventory is kept on the perpetual system
c) All purchases and 80% of sales are on credit

Required:
a) Calculate purchases.
b) If purchases during February were $39,000 what is the Cost of Goods Sold for February?

a) First of all, remember that "purchases" sometimes consists of both cash and credit purchases. In this example, however, it says, "all purchases and 80% of sales are on credit." This is a bit confusing, but if you read it carefully it means that all purchases here are on credit.

So how do we get all purchases or all credit purchases here?

If you reconstructed the creditors control T-account the answer would be the "balancing figure" in the T-account (the final missing figure there).

What I mean is, we can use the opening and closing balances of the creditors control, as well as the cash paid to them ("Payments to creditors") to get the credit purchases during the month.

Here's how I like to look at it:
- We started out owing the creditors control $25,200.
- We purchased a certain amount from them during the month (missing or balancing figure). This increases how much we would owe them. More purchases on credit means more owing.
- We also paid them $41,040 during February for these credit purchases. This reduces how much we owe.
- At the end of the month (after all this) we owed them $29,160.

Now if you're not familiar with constructing a T-account to get a missing or balancing figure, you can also put the above items in the form of an equation:

Closing balance creditors control = Opening balance creditors control + Credit Purchases - Payments to Creditors

\$29,160 = \$25,200 + Credit Purchases - \$41,040

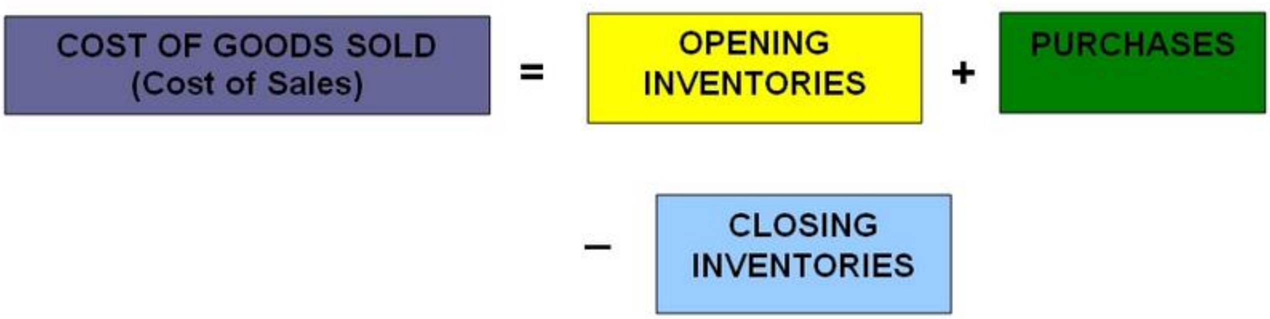
If we switch this around and make Credit Purchases the subject:

Credit Purchases = \$29,160 - \$25,200 + \$41,400
= \$45,360

Since credit purchases make up 100% of the purchases, the full purchases figure is also \$45,360 .

b) Any time a question asks for the **Cost of Goods Sold** (or Cost of Sales - same thing) then there is a very good chance you will need to use the **Cost of Goods Sold formula.**

The cost of goods sold formula is:



Here's how we use it in this question:

Cost of Goods Sold = Opening inventory + Purchases - Closing Inventory
= \$30,000 + \$39,000 - \$36,000
= \$33,000

Question on
Basic Journal Entries Question

Create journal entries for the following transactions (Rs. = Rupees = Indian currency):

1. Harish started business with cash Rs. 10000
2. Bought goods from Manohar Rs. 5000
3. Purchase fittings for cash Rs. 800
4. Sold goods to Charanjeet Rs. 1600
5. Paid Manohar Rs. 3000
6. Sold goods Vadva Ram Rs. 2000
7. Received from Charanjeet Rs. 1540 and allowed him discount Rs. 60
8. Paid wages Rs. 80
9. Bought goods for cash Rs. 600

10. Sold goods to Ramesh Rs. 3400
11. Purchase goods from Purchotam Ra. 2600
12. Paid Manohar in settlement Rs. 1900 and discount allowed by him Rs. 100
13. Paid carriage from goods and sold Rs. 40
14. Paid wages Rs. 80
15. Bought goods Manohar Rs. 3000
16. Bought goods for cash Rs. 800
17. Sold goods Vadva Ram Rs. 3600
18. Vadva Ram paid on account Rs. 4000
19. Purchase goods from Harbans Rs. 1500
20. Sold goods for cash Rs. 1600
21. Paid wages Rs. 80
22. Paid to Harbans Rs. 1440 and discount allowed by him Rs. 60
23. Sold goods to Charanjeet Rs. 2600
24. Bought goods for Manohar Rs. 1400
25. Bought goods for cash Rs. 1460
26. Paid on account to Manohar Rs. 1460
27. Received from Charanjeet Rs. 4000
28. Paid wages Rs. 80
29. Paid for electric lighting Rs. 100
30. Paid rent Rs. 160
31. Harish drew for personal use Rs. 300
32. Purchases Rs. 80
33. General expense Rs. 190

34. Carriage outwards Rs. 60

Solution:

Here are the journal entries for the above:

1. Dr Bank 10,000
Cr Capital 10,000

Bank is an asset , which increases on the left side of the accounting equation (debit). This investment by the owner in the business is known as capital, which is a form of owner's equity . Owner's equity increases on the right side of the accounting equation (credit). See our tutorial on the journal entry for an equity investment by the owner for a full example and explanation of this type of transaction.

2. Dr Purchases 5,000
Cr Creditors 5,000

In this example I am assuming the business is using the periodic inventory system , so we debit the purchases account (not the inventory account). Since the purchases are on credit, we have liabilities . Since liabilities increase on the right side, we credit the creditors.

3. Dr Fittings 800
Cr Bank 800

Fittings are fixed pieces of equipment inside a business or house which can be removed if needed. Examples include a ceiling lamp or a tap/faucet. Fittings are assets for the business. Since these assets are increasing, we do an entry on the left side of the accounting equation (debit). Bank is decreasing since it is a payment and so is credited. See the tutorial on the journal entry for purchasing an asset for a full example of this kind of transaction.

4. Dr Debtors 1,600
Cr Sales 1,600

A credit sale means that there will be income, which is credited. The debit goes to debtors (or "accounts receivable," an asset), which means that debtors is increasing. See the tutorial on the journal entry for income on credit for a full example.

5. Dr Creditors 3,000
Cr Bank 3,000

In this case we are paying the debt to our supplier. A payment means our bank is decreasing, which occurs on the right side (credit). Creditors (a liability) decreases too, which means this is debited. See our tutorial on the journal entry for paying a debt for a full example.

6. Dr Debtors 2,000
Cr Sales 2,000

Same as 4 above - credit sale.

7. Dr Bank 1,540
Dr Discount allowed (expense) 60
Cr Debtors 1,600

Since we're receiving money, our bank increases, which means we debit it. Debtors (accounts receivable) also decreases, since this debt to our business is being paid. The discount our business is giving is an expense and so is debited.

8. Dr Wages 80
Cr Bank 80

Wages are an expense and so are debited. Bank is decreasing and so gets a credit. See our tutorial on the journal entry for expenses paid by cash for a full example.

9. Dr Purchases 600
Cr Bank 600

Same as 2 above except that this is a cash purchase, so our bank is decreasing (credit).

10. Dr Debtors 3,400
Cr Sales 3,400

Same as 4 and 6 above.

11. Dr Purchases 2,600
Cr Creditors 2,600

Same as 2 above.

12. Dr Creditors 2,000
Cr Bank 1,900
Cr Discount received (income) 100

In this case we are receiving a discount. This is counted as income, meaning we credit it. Our liability (debt) to our supplier is decreasing. Since liabilities increase on the right side, they decrease on the left, so are debited. The payment means bank is decreasing, so it gets a credit.

13. Dr Carriage on goods 40
Cr Bank 40

"Carriage" means "transport costs." It is an expense.

14. Dr Wages 80
Cr Bank 80

Same as 8 above.

15. Dr Purchases 3,000
Cr Creditors 3,000

Same as 2 and 11 above.

16. Dr Purchases 800
Cr Bank 800

Same as 9 above.

17. Dr Debtors 3,600
Cr Sales 3,600

Same as 4, 6 and 10 above.

18. Dr Bank 4,000
Cr Debtors 4,000

We are receiving money, so our bank increasing means we debit it. The credit is to the debtors (accounts receivable), which means we are recording this asset decreasing. See the tutorial on the journal entry for when a debtor pays for a full example and explanation.

19. Dr Purchases 1,500
Cr Creditors 1,500

Same as 1, 11, 15 above.

20. Dr Bank 1,600
Cr Sales 1,600

A cash sale means we record income on the right side of our accounting equation (credit) and our bank increasing means we make an entry on the left side to this account (debit). See the tutorial on the cash income journal entry for a full example.

21. Dr Wages 80
Cr Bank 80

22. Dr Creditors 1,500
Cr Bank 1,440
Cr Discount received (income) 60

Same as 12 above.

23. Dr Debtors 2,600
Cr Sales 2,600

24. Dr Purchases 1,400
Cr Creditors 1,400

25. Dr Purchases 1,460
Cr Bank 1,460

26. Dr Creditors 1,460
Cr Bank 1,460

27. Dr Bank 4,000
Cr Debtors 4,000

Same as 18 above.

28. Dr Wages 80
Cr Bank 80

29. Dr Electric lighting 100
Cr Bank 100

Electric lighting is an expense and so is debited.

30. Dr Rent 160
Cr Bank 160

Rent is also an expense.

31. Dr Drawings 300
Cr Bank 300

Drawings is the opposite of capital (owner's equity investment in a business). It means owner's equity, which is on the right side of our accounting equation, is now decreasing. So drawings occurs on the left side (debit). The credit is to bank, which means it is decreasing (a payment).

32. Dr Purchases 80
Cr Bank 80

There was no mention for this transaction if the purchases were made with cash or on credit. I assumed it was a cash purchase.

33. Dr General expense 190
Cr Bank 190

34. Dr Carriage outwards 60
Cr Bank 60

Carriage outwards is a transport expense of goods going out from the business.

Company Trial Balance and Financial Statements Question

Security Services Inc. as of January 1, 2016 had the following normal balances:

Cash 74,210
Accounts receivable 13,500
Supplies 200
Prepaid rent 3,200
Merchandise inventory (24 @ $265; 1 @ $260) 6,620
Land 4000
Accounts payable 1,950
Unearned revenue 980
Salaries payable 1,000
Common stock 50,000
Retained earnings 47,800

The following transactions took place during 2016 for Palicio Security Services:
1. Paid the salaries payable from 2015.
2. On March 1, 2016, Palicio established a $100 petty cash fund to handle small expenditures.
3. Paid $4,800 on May 1, 2016, for one year's lease on the company van in advance.
4. Paid $7,200 on May 2,2016 for one year's office rent in advance.
5. Purchased $400 of supplies on account.
6. Purchased 100 alarm systems for $28,000 cash during the year.
7. Sold 102 alarm systems for $57,120. All sales were on account.
(Compute cost of goods sold using the FIFO cost flow method)
8. Paid $2,100 on accounts payable during the year.
9. Replenished the petty cash fund on August 1. At this time, the petty cash fund had only $7 of currency left. It contained the following receipts: office supplies expense $23, cutting grass $55, and miscellaneous $14.
10. Billed $52,000 of monitoring services for the year.
11. Paid installers and other employees a total of $25,000 cash for salaries.
12. Collected $89,300 of accounts receivable during the year.
13. Paid $3,600 of advertising expense during the year.
14. Paid $2,500 of utilities expense for the year.
15. Paid a dividend of $10,000 to the shareholders.

Required:

1. Prepare the trial balance as at Dec 31, 2016 for Palicio Security Services Inc.

2. Prepare the income statement, statement of changes in equity and balance sheet for Palicio Security Services Inc.

A:

This is actually a pretty tricky and advanced accounting question. You should only try it if you have a pretty good understanding of the following topics (click for a tutorial on each):

- The Trial Balance,
- Financial Statements and
- Inventory (including the FIFO Method and Cost of Goods Sold).

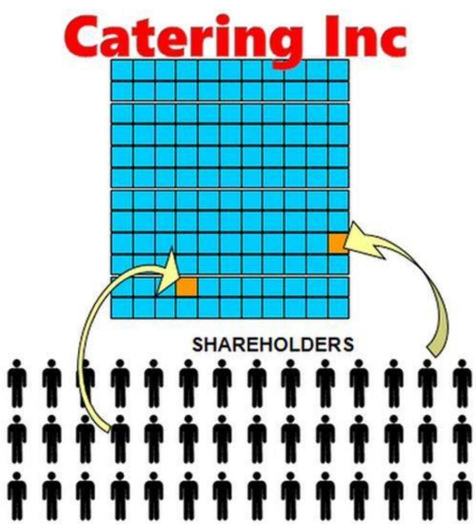
Additionally, this question also deals with **prepaid expenses** and **income received in advance** , which are concepts I don't go into detail about on this website (I only cover these topics in detail in my basic accounting books).

Here are some brief explanations though: **Prepaid expenses** are expenses you paid too early. Because it is paid too early it is as if you are owed the amount you paid, and the prepaid expense essentially is a **debtor/receivable** (an asset account).

In a similar way, **income earned in advance** means you have been paid money before delivering the services/products, and so it is as if you owe this amount. Thus, income earned in advance is a

creditor/payable .

Note also that in this exercise we are dealing with a **company** or **corporation** , not a simple sole proprietor. With a corporation there are some new terms and concepts.



First of all there are many owners in a corporation and these owners are called

Also, each of the shareholders owns **shares** in the corporation, which is also known as **common stock** .

Finally, instead of "drawings," we have **dividends** that are paid to all the shareholders from the accumulated profits (AKA **retained earnings**).

Okay, so now that we've cleared up all those terms, here's the solutions, starting with the trial balance:

Trial balance for Palicio Security Services Inc. on the 31st of December 2016		
Description	**Debit $**	**Credit $**
Land	4,000	
Cash ** (calculation below)	79,217	
Accounts Receivable (13,500 + 57,120 + 52,000 - 89,300)	33,320	
Merchandise inventory (opening balance)	6,620	
Supplies (200 + 400)	600	
Prepaid Office Rent (3,200 - 3,200 + (7,200 x 4/12 months))	2,400	
Prepaid Motor Lease (4,800 x 4/12 months)	1,600	
Accounts Payable (1,950 + 1,000 - 1,000 + 400 - 2,100)		250
Un-earned revenue		980
Common Stock		50,000
Retained Earnings		47,800
Purchases	28,000	
Office Supply Expense	23	
Cutting Grass Expense	55	
Miscellaneous Expense	15	
Office Rent Expense (3,200 + (7,200 x 8/12 months))	8,000	
Motor Van Lease Expense (4,800 x 8/12)	3,200	
Salaries	25,000	
Advertising	3,600	
Utilities	2,500	
Dividends Paid	10,000	
Monitoring Services Income		52,000
Sales		57,120
TOTAL	**208,150**	**208,150**

Notes:

** Cash includes $100 petty cash. Calculation of cash balance:

74,210 - 1,000 - 4,800 - 7,200 - 28,000 - 2,100 - (100 - 7) - 25,000 + 89,300 - 3,600 - 2,500 - 10,000

= 79,217

The opening balance of prepaid rent ($3,200) has been expensed out during 2016 as we have assumed this rent (that was paid the previous year) applies to the 2016 year. This is a likely assumption as there was a new prepaid rent cash payment on 2 May, 2016.

It is not stated in the question whether the unearned revenue of $980 at the beginning of 2016 was actually earned during the year. In this solution we have assumed that the unearned revenue still remains unearned at the end of 2016. However, it is quite acceptable to treat this as having been earned during 2016. If treating it as earned during 2016 one would add $980 to revenue and remove the unearned revenue account ($980 - $980).

Income statement Palicio Security Services Inc. for the period ending 31st of December 2016		
	$	$
Sales		57,120
Cost of goods sold (see note below)		(28,180)
Opening inventories	6,620	
Purchases	28,000	
Less: Closing inventories	(6,440)	
Gross profit		28,940
Other income:		
Monitoring Service Revenue		52,000
Other expenses:		(42,393)
Office Supplies	23	
Cutting Grass	55	
Miscellaneous	15	
Office Rent	8,000	
Motor Vehicle Lease	3,200	
Salaries	25,000	
Advertising	3,600	
Utilities	2,500	
NET PROFIT		38,547

Calculation of Cost of Sales and Closing Inventory (FIFO Basis):

Opening Balance of Merchandise Inv. (24 Units @ $265 + 1 Unit @ $260) **$6,620**

Purchased during the year 100 Units @ $280 **$28,000**

Total available for sale 124 + 1 Units (125 Units) **$34,620**

Sold*(Cost of Sales) 102 Units **$28,180**

Closing Balance of Merchandise Inv. 23 Units @ $280 **$6,440**

***Cost of Sales** 102 Units (24 Units @ $265) + (1 Unit @ $260) + (77 Units @ $280) = **$28,180**

Statement of Changes in Equity of Palicio Security Services Inc. for the period ended 31st of December 2016		
	Retained Earnings $	Common Stock $
Balance at the beginning of the year	47,800	50,000
Profit for the year	38,547	
Capital contributed during the year		0
Less dividend paid	(10,000)	
Balance at the end of the year	76,347	50,000

Balance sheet for XYZ business on the 31st of December 2016		
	$	$
ASSETS		
Non-current assets		4,000
Land and buildings	4,000	
Current assets		123,577
Closing Inventory (See note above)	6,440	
Debtors/receivables (33,320 + 2,400 + 1,600)	37,320	
Bank and cash (includes $100 petty cash fund)	79,217	
Supplies	600	
TOTAL ASSETS		127,577
EQUITY AND LIABILITIES		
Owner's equity		126,347
Capital	50,000	
Retained Earnings	76,347	
Current liabilities		1,230
Creditors/payables (250 + 980)	1,230	
TOTAL EQUITY AND LIABILITIES		127,577

Note that the prepayments (prepaid office rent and prepaid motor lease) have been included under debtors/receivables. Likewise, the income received in advance ("unearned revenue" of $980) has been included under creditors/payables.

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