Tutorial 2 – <u>The Cash Cycle</u>

<u>Section A:</u>

1. (a) What is the difference between **cash and credit transactions**?

- **Cash term**: Payment is made or collected immediately (upon purchase/sale)
- **Credit term**: Payment is made or collected at a future date, based on the credit period given, normally 30 days, 60 days, or 90 days.

(b) What is the difference between **trade discounts and cash discounts**?

- **Trade discount**: percentage reduction granted to a customer from the list price due to the purchase of a large quantity and to encourage bulk purchases (buy more).
- **Cash discount** (discount received and discount allowed): a percentage reduction granted to the customer in order to encourage prompt payment (earlier than the credit period given).

(c) What are the different **types of cash** in a business? Briefly explain.

- **Cash** - Cash in hand, kept in the office by main cashier
- **Bank** - Current account
- **Petty Cash** - Small amount kept by Petty Cashier

2. (a) What is the **purpose** of preparing a **three column cash book**? Briefly explain its format.

- The purpose of a three column cash book is to record all types of cash and cheque transactions.
- A three column cash book functions as the General Ledger accounts for cash account and bank account.

Format: The three-column Cash Book

Cash Book: Cash discount

Date	Particular	Folio	Discount Allowed	Cash	Bank	Date	Particular	Folio	Discount Received	Cash	Bank
			RM	RM	RM	March			RM	RM	RM
	Customer: A		100		2,300	31	Supplier: Fiction Store		100		2,300

- A three column cash book has three columns on each side - debit and credit side. One is used to record **cash** transactions, the second is used to record **bank** transactions and third is used to record **discounts received and allowed**.

(b) Why is the cash book both a book of prime entry and a ledger account? Explain.

- It is used to record all types of cash and cheque transactions.
- It functions as the General Ledger accounts for cash accounts and bank accounts. It is a combination of 4 "T" accounts which are Cash (cash in hand), Bank (cash at bank), Discount Allowed, and Discount Received.

(c) What is an **overdraft**? How does it work?

- Bank overdraft is a special loan that has been approved by the bank for the business to issue cheques more than the amount deposited into the current account.
- The bank overdraft facility will specify the maximum limit available for the business to use. Overdraft interest will be calculated based on the actual amount of bank overdraft balance, usually on a monthly basis.

3. Explain what is an **imprest system**? How does it work?

- The imprest system is a form of financial accounting to manage the petty cash. At the end of the period, the cashier will reimburse the petty cashier the amount of petty cash spent during the period so that the petty cashier will start with the same amount of the petty cash float.

4. The following are the **transactions of Axis Trading** in May:

Position: In (Dr) - Cash Inflow: e.g Sales, receives payment from TR
Position: Out (Cr) - Cash Outflow: e.g Purchases, buying other assets, all expenses

Particular (wording). Account name.
Dr   Electricity   20 (Electricity account)
Cr   Cash   20 (in the Cash Book)

Particular of each account: Opposite account's name.
Electricity account: Cash 20
Cash Book: Electricity

May
1   Start a business with **Cash in hand** RM800 and **Cash at bank** RM1,000 **(In)**
2   Purchased goods by cheque RM400 **(Out)**
2   Paid rates to Dewan Bandaraya Kuala Lumpur by cheque RM40 **(Out)**
4   Bought goods on credit from Zen & Co RM200 **(X)**
8   Sold goods to Todds on credit RM300 **(X)**
9   Cash sales RM80 **(In)**
10 Paid transport by cash RM12 **(Out)**
13 Credit sales to Todds RM300 **(X)**
14 Paid for stationery in cash RM16 **(Out)**
15 Introduced further capital RM1,000 by cheque **(In)**

16 Todds paid for the amount owing by cheque (RM 570), less 5% discount (calculate the amount) **(In)** 5% x 600 = 30
20 Withdrew cash (office, drawer, safe, purse/wallet) for own use (owner's personal use) RM120 **(Out) - Drawings (Equity)**
    5 categories (big categories) 5 concepts
    Specific account names: Drawings, Stationery, Capital, Rental, Rates, Purchases, Sales

24 Purchased goods with office cash RM28 **(Out)**
25 Paid Zen & Co a cheque in full settlement of the amount owing, less 5% discount (calculate the amount) **(Out)**
26 Sold goods on credit to Tali RM450 **(X)**
28 Paid transport by cash RM10 **(Out)**
30 Transferred cash from office (cash in hand) Cr to Dr bank RM400 **(contra)**
30 Credit purchase from Zen & Co RM300 **(X)**
31 Refund cash to Todds for returning empty containers for recycling RM5 **(Out)**
31 Bought office furniture, paid by cheque RM200 **(Out)**
31 Paid Samuel a cheque in settlement of outstanding invoice of RM700 and deducting RM35 cash discount **(Out) Invoice, settling an amount owed.**
31 Receive a cheque from Kenneth RM475 after deducting RM25 cash discount **(In) Cheque amount: 475**

Exact amount: payment was RM475
Invoice: 700 add:sales tax, GST tax, service tax
Less: Discount
Net: 700 - 35
(How much owed by customer/to supplier) Trade discount. Cash discount may come as a 2nd discount

Required:
(a) Enter the above transactions in a **three-column Cash Book** and close the Cash Book at the end of May (ignore those transactions that do not involve the Cash Book).
    see excel

(b) Post those items involving the Cash Book to the appropriate ledgers .
    see excel

Section B: Extra exercise questions (for students' own practice)

Question 1

Maxwell buys and sells machinery. During the month of March, the following receipts and payments occurred.

March

1 Balances as per Cash Book: Bank RM2,100; Cash RM1,010 **(In)**
3 Cash sales paid into bank RM620 **(In)**
4 Cash purchases RM380 **(Out)**
6 Paid an electricity bill of RM660 by cheque **(Out)**
9 Sales by cheque RM530 **(In)**
10 Drew a cheque for RM400 in respect of wages **(Out)**
12 Cash sales RM440 **(In)**
15 Paid RM190 in cash for travelling expenses **(Out)**
16 Paid water bill by cheque RM560 **(Out)**
19 Drawings by cheque RM300 **(Out)**
20 Purchases by cheque RM470 **(Out)**
21 Paid postage of RM30 in cash **(Out)**
22 Paid cash of RM450 into the bank **(contra)**
24 Introduced further capital of RM650 by cheque **(In)**
25 Purchased a delivery vehicle for RM4,000 and paid by cheque **(Out)**
26 Received a cheque for RM3,500 from Morris as a three year loan **(In)**
28 Paid road tax and insurance on delivery vehicle of RM430 in cash **(Out) Cr Cash 430**
29 Withdrew cash of RM330 from bank for office use **(contra)**
30 Received cheque from Kenny RM475 after deducting RM25 cash discount   **(In)**
30 Received cheque from Donny RM722 after deducting RM38 cash discount **(In)**

31 Paid Sammy a cheque in settlement of outstanding invoice of RM700, and deducting RM35 cash discount **(Out)**
31 Paid Gracey a cheque in settlement of outstanding invoice of RM360, and deducting RM18 cash discount **(Out)**
31 Received a cheque from Joy for RM1,254 after deducting cash discount of RM66. However, the cash discount was wrongly deducted (not allowed). Joy needs to **pay up for the shortfall of RM66** very soon.

Required:
(a) Enter the above transactions in a **three-column Cash Book** and close the Cash Book at the end of March (ignore those transactions that do not involve the Cash Book).
      see excel

(b) Post those items involving the Cash Book to the appropriate <u>ledgers</u>.
      see excel
(T-accounts: Stationery account, Sales account, Purchases, Capital, Drawings)

Question 2

Vincent K is a sole trader who records all his cash and bank transactions in a three-column Cash Book. On 1 August, his **cash in hand was RM68** but he had a **bank overdraft of RM1,692**.

The following are her transactions for the month of August:

August

2 Received a cheque of RM160 from Patrick in **full settlement** of a debt of RM168 **(In)**

10 Cash sales paid directly to bank RM2,086 **(In)**

12 Drew a cheque RM75 in favour of Winifred Engineering, in settlement of an outstanding debt **(Out)**

14 Paid RM35 cash for stationery **(Out)**

16 Paid Frederick Sung the sum of RM86 by cheque in **settlement** of an amount owed to him of RM90 **(Out)**

18 Drew a cheque for office cash RM150 **(contra)**

20 Cash sales RM1,120; cash kept in the office safe **(In)**

21 Received interest of RM60 and paid this into the bank **(In)**
The sales of the previous day were also banked in - from cash to bank **(contra)**

24 Paid telephone charges by cheque RM147 **(Out)**

26 Received a cheque of RM704 from Benny Chan in **settlement** of his account amounting to RM720 **(In)**

28 Paid RM40 out of cash for office expenses **(Out)**

30 Paid RM254 to Larry Heng by cheque in **full settlement** of the RM270 balance on his account **(Out)**

30 The bank notified Vincent K that it had charged RM20 bank charges to his account **(Out)**

Required:

(a) State three (3) purposes for preparing a Cash Book.
- Record all types of cash and cheque transactions.
- Functions as the General Ledger accounts for cash account and bank account.
- Allowing managers and company accountants to budget their cash effectively

(b) Define the two (2) types of cash discounts in the 3-column Cash Book and the purpose of a cash discount.
- **Discount Allowed** - A reduction in price of goods or services, which is allowed by a seller to a buyer at the expense of the seller
- **Discount Received** - A reduction in purchase price received by the buyer, on the goods bought or services availed from the seller
- **Purpose of cash discount** - A percentage reduction granted to the customer in order to encourage prompt payment (earlier than the credit period given).

(c) Draw up the **3-column Cash Book** of Vincent K for the month of August. Balance up the cash and bank columns, bringing down the balances on 1 September.
see excel

(d) Total up the two discount columns and post the amounts to the relevant accounts in the General Ledger.
see excel