*2026 EDITION*

**JUNYUAN SECONDARY SCHOOL**

# Principles of Accounts

Logical Learning. Life-Long Skill.

**We Nurture People of Accountability**

# Format & memory essence (Sec 4N)

**FOR N LEVEL SYLLABUS 7086**

| | |
|---|---|
| **Name** | |
| **Class** | |

☞ **Required to interpret the accounts but need not prepare the accounts.**

# Contents Page

# CHAPTER 1 INTRODUCTION TO ACCOUNTING

## TYPES OF BUSINESSES

- **Trading business** buys from suppliers and sells goods to customers.
  e.g. bookshop
- **Service business** provides services to its customers.
  e.g. cleaning service.

## ROLE OF ACCOUNTING & ACCOUNTANTS

### Role of Accounting

- Accounting provides accounting information for **decision making** by owners and other stakeholders.

### Role of Accountants

- Through providing accounting information for stakeholders' decision-making, accountants act as **stewards** of businesses.
- Accountants set up the **accounting information system** to collate, record, organise and report accounting information so that owners and other stakeholders can make decisions regarding the management of resources and the performance of businesses.
- They think critically, **solve problems**, adapt and meet the need for sophisticated accounting and business information.
- In the face of an evolving business environment and rapid technological advancement, accountants have to provide timely, relevant and credible information, based on **accounting theories**, which are easily and appropriately understood by stakeholders.

## PROFESSIONAL ETHICS

- **Integrity**: Being straightforward and honest in all professional and business relationships
- **Objectivity**: Not letting bias, conflict of interest or undue influence of others override professional judgement.
- **Importance of Professional Ethics**: Stakeholders rely on financial reports provided by accountants to make business decisions. If they are given false or inaccurate information about the business, they are likely to make poor decisions.

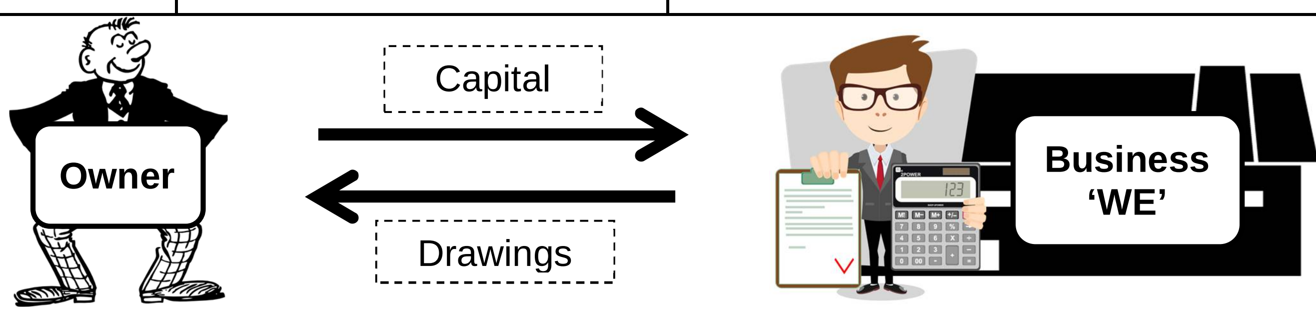
**STAKEHOLDERS**

Stakeholders are people with an interest or concern in a business.

| Stakeholder | Role | Decision needs |
|---|---|---|
| Owners | Contribute capital & expect profit distribution in return | Whether to continue investing in business, depending on the risks and returns |
| Managers | Work for the business and devise strategic plans to run the business efficiently | Whether to consider ways to improve the performance of the business |
| Employees | Work for the business and perform executive duties | Whether to continue working at the business |
| Lenders | Lend money to the business and expect it to be fully repaid with interest | Whether to grant loans to the business, depending on the business' ability to repay the principal amount and interest |
| Suppliers | Supply goods and/or provide services to the business | Whether to sell to the business on credit, depending on its ability to pay |
| Customers | Buy goods and/or engage services from the business | Whether to buy from the business, depending on its ability to provide goods and/or services that they need and good after-sales service |
| Government | Enforce tax regulations | Whether the business complies with the tax regulations and decides the amount of tax to collect |
| Competitors | Sell similar goods and/or provide similar services | Whether they are comparable to the business and how to improve their own performance |

## ACCOUNTING THEORIES

| | Accounting theory | Definition | Application |
|---|---|---|---|
| 1 | Monetary theory | Only business transactions that can be measured in monetary terms are recorded. | Factors such as staff morale and loyalty are not recorded as it is not possible to determine a monetary value. |
| 2 | Historical cost theory | Transactions should be recorded at their original cost. | <u>Chapter 2 Accounting Information System</u><br>The transaction is recorded at the original cost that it occurred as stated on the source document. |
| 3 | Objectivity theory | Accounting information recorded must be supported by reliable and verifiable evidence so that financial statements will be free from opinions and biases. | <u>Chapter 2 Accounting Information System</u><br>A source document provides evidence so that transactions are recorded based on reliable and verifiable information. |
| 4 | Accounting entity theory | The activities of a business are separate from the actions of the owner. All transactions are recorded from the point of view of the business. | <u>Chapter 14 Owner's Equity</u><br>Resources contributed by the owner for business use are recorded as capital and withdrawal of business assets for personal use are recorded as drawings. |




<u>Consider:</u>
Do we record the following transactions in the business' books?

1. Owner withdrew money from <u>business</u> bank account to pay for <u>personal</u> expenses.
2. Owner withdrew money from <u>business</u> bank account to pay for <u>business</u> expenses.
3. Owner withdrew money from <u>personal</u> bank account to pay for <u>business</u> expenses.
4. Owner withdrew money from <u>personal</u> bank account to pay for <u>personal</u> expenses.

| | Accounting Theory | Definition | Application |
|---|---|---|---|
| 5 | Going concern theory | A business is assumed to have indefinite economic life unless there is credible evidence that it may close down. | <u>Chapter 5 Financial Statements</u><br>Financial statements are prepared to assess the performance and position of the business for continuity. |
| 6 | Accounting period theory | The life of a business is divided into regular time intervals to allow for meaningful reporting. | <u>Chapter 5 Financial Statements</u><br>**Financial statements** should be prepared at regular time intervals to provide timely information for stakeholders to make decisions.<br><br>The statement of financial **performance** is prepared periodically to inform stakeholders of the profitability of the business.<br><br>The statement of financial **position** is prepared periodically to provide information on how the resources are obtained and used in a business and the claim by the owner/s on the net assets of the business on a certain date. |
| 7 | Revenue recognition theory | Income is recognised when goods have been delivered or services have been provided. | <u>Chapter 6 Revenue and Income</u><br>Income is recognised when goods have been delivered or services have been provided. |
| 8 | Accrual basis of accounting | Business activities that have occurred, regardless of whether cash is paid or received, should be recorded in the relevant accounting period. | <u>Chapter 6 Revenue and Income</u><br>Income is recognised when goods are delivered or services are provided regardless whether payment is received.<br><br><u>Chapter 7 Cost of Sales and Expenses</u><br>Expenses are recognised when incurred regardless whether payment is made. |

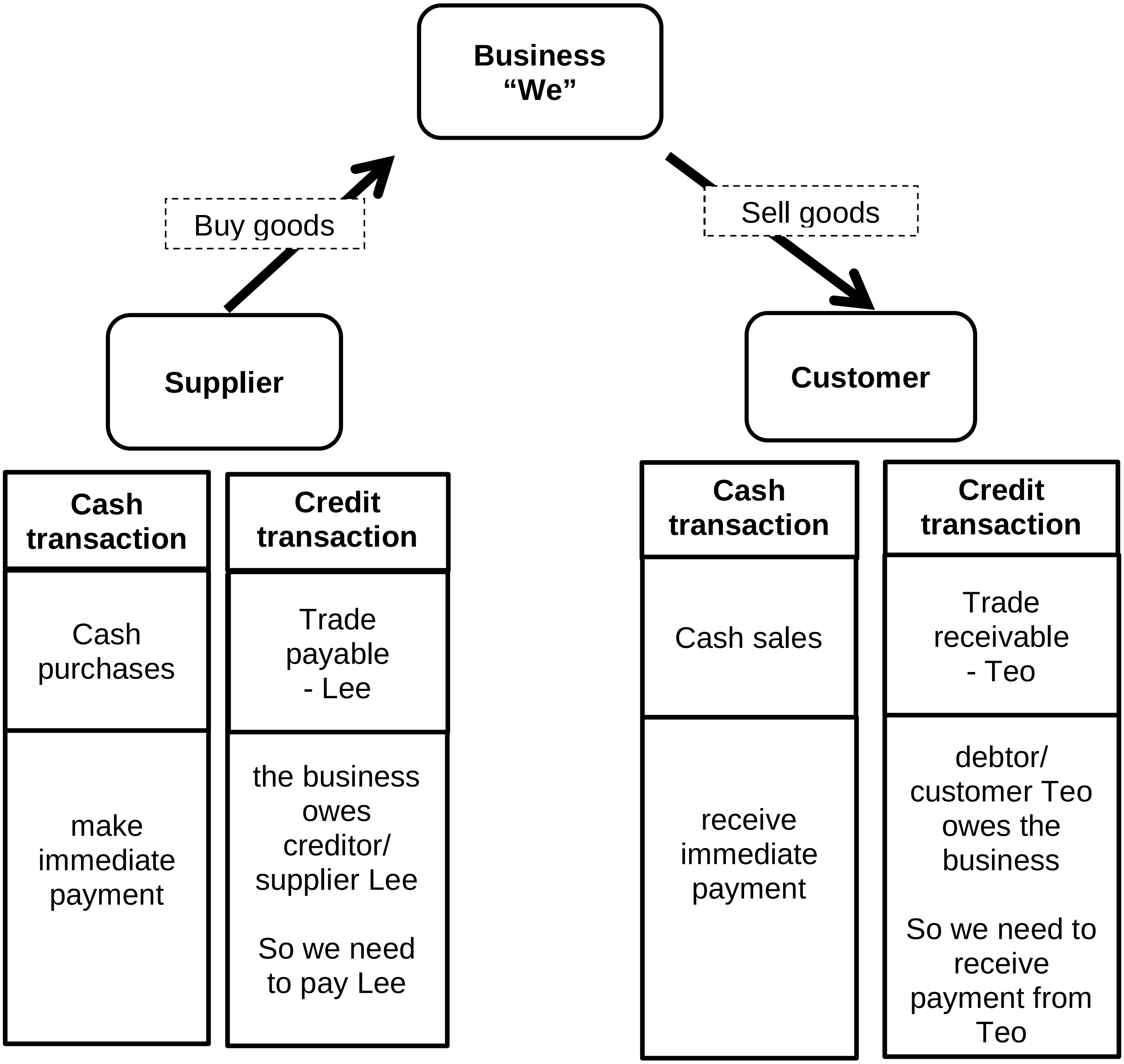
| | Accounting Theory | Definition | Application |
|---|---|---|---|
| 9 | Matching theory | Expenses incurred must be matched against income earned in the same period to determine the profit for the period. | Chapter 7 Cost of Sales and Expenses<br>The cost of sales must be matched against the sales revenue earned from selling the inventory in the same accounting year to determine the gross profit.<br><br>Other costs incurred to generate revenue and other income must be matched against revenue and other income earned in the same accounting year to determine the profit for the year.<br><br>Chapter 10 Trade receivables<br>As the increase in allowance for impairment of trade receivables is a likely expense, it should be recorded in the same accounting year as the sales revenue earned to obtain a true and fair profit for the year.<br><br>Chapter 11 Non-current assets (NCA)<br>Depreciation expense, which is a portion of the cost of the NCA, should be matched against the income earned from using the NCA in the same year to obtain a true and fair profit for the year. |
| 10 | Prudence theory | The accounting treatment chosen should be the one that least overstates assets and profit and least understates liabilities and losses. | Chapter 9 Inventories<br>Inventory is valued at the lower of cost and net realisable value so that profits and assets are not overstated.<br><br>Chapter 10 Trade receivables<br>The allowance for impairment of trade receivables is reported in the statement of financial position as a deduction against the trade receivables book value so that assets are not overstated.<br><br>Chapter 11 Non-current assets<br>Non-current assets should be valued at their net book value, which is cost less accumulated depreciation so that profits and assets are not overstated. |

| | Accounting Theory | Definition | Application |
|---|---|---|---|
| 11 | Consistency theory | Once an accounting method is chosen, this method should be applied to future accounting periods to enable meaningful comparison. | <u>Chapter 11 Non-current assets</u><br>The depreciation method and rate of depreciation used by the business must be consistent from period to period so that its financial performance can be meaningfully compared across financial periods. |
| 12 | Materiality theory | Financial information is material to the financial statements if it would change the opinion or view of a reasonable person. | <u>Chapter 11 Non-current assets (NCA)</u><br>If the amount spent on a NCA is insignificant to decision making, it does not have to be reported as an NCA even though its benefits last for more than one accounting year.<br><br>It can be classified as a revenue expenditure and reported as an expense in the statement of financial performance. |

# CHAPTER 2 ACCOUNTING INFORMATION SYSTEM

## TYPES OF BUSINESS TRANSACTIONS

- **Cash transactions:** Payment is made <u>immediately</u> during a cash sale or purchase
- **Credit transactions:** Payment is <u>delayed</u> during a credit sale or purchase



## ACCOUNTING CYCLE

- Stage 1: Identify and record
  **Source documents** are used to record transactions in the **journal** daily. Journal entries are posted to the **ledger**.

- Stage 2: Adjust
  The ending balances of ledger accounts are listed in a **trial balance**. Any adjusting entries are recorded in the journal and posted to the ledger. Accounts are adjusted at least once in a financial year.

- Stage 3: Report
  Based on adjusted trial balance, **financial statements** are prepared at least once in a financial year.

- Stage 4: Closing
  After the financial statements are finalised, income, expenses, income summary, drawings and dividends accounts are closed. Accounts are closed once at end of financial year.

## ACCOUNTING INFORMATION SYSTEM

It is a system that a business uses to collect, store and process accounting data.

| | Components | Purpose |
|---|---|---|
| 1 | Source documents | A source document provides proof that transactions have occurred. |
| 2 | Journal | A journal is a daily record of transactions containing details from source documents. |
| 3 | Ledgers | Journal entries are posted to ledger accounts.<br>A ledger account is a consolidation of transactions relating to a specific asset, liability, equity, income or expense item. |
| 4 | Trial balance | A trial balance provides a summary of ending balances of each ledger account at a specified date to check for errors. |
| 5 | Financial statements | A statement of financial performance provides a report on income earned and expenses incurred to determine the profit or loss for the period.<br><br>A statement of financial position provides a report on assets, liabilities and equity at a specified date to show how resources are obtained and funded. |

## SOURCE DOCUMENTS

**Purpose**
A source document is a written document that provides details of a transaction and proves that the transaction has taken place.

The **seller issues** source documents to the buyer. The **buyer receives** the original copy while the seller keeps a duplicate so that both parties would be clear about the details of the transactions.

**Application of Accounting Theory**

1. **Objectivity theory** – a source document provides evidence so that transactions are recorded based on reliable and verifiable information.

2. **Historical cost theory** – The transaction is recorded at the original cost that it occurred as stated on the source document.

| Source document | Purpose | Transaction / Keywords |
|---|---|---|
| Receipt | Acknowledges payment received from customers | Received cash or cheque |
| Payment voucher | To seek approval before making payment | Paid cash or cheque |
| Remittance advice | Informs credit supplier that payment by cheque has been made for specific invoice(s) | Only for payment to credit supplier |
| Bank statement | Prepared by the bank to check and tally against the business records of its cash at bank account | Bank amounts paid or received through:<br>• standing order<br>• credit transfer<br>• direct debit<br>• dishonoured cheque<br>• bank charges |
| Invoice | Informs credit customers of the amount owed for goods or services provided. | • Sold goods/NCA on credit<br>• Purchased goods/NCA on credit |
| Debit note | Increases the amount owed by credit customers. | • Undercharged customer<br>• Undercharged by supplier |
| Credit note | Reduces the amount owed by credit customers. | • Goods returned by customer<br>• Goods returned to supplier<br>• Overcharged customer<br>• Overcharged by supplier |

# CHAPTER 3 ELEMENTS OF FINANCIAL STATEMENTS & ACCOUNTING EQUATION

## ELEMENTS OF FINANCIAL STATEMENTS

- **Assets** are resources a business owns or controls that are expected to generate future benefits.

- **Liabilities** are obligations owed by a business to others that are expected to be settled in the future.

- **Equity** is the claim by the owner on the net assets of a business, where net assets is total assets less total liabilities. Equity consists of capital contributed by the owner and the profit generated by the business.

- **Income** are earnings from the activities of a business, which consist of sales revenue, service fee revenue and other income.

- **Expenses** are costs incurred to earn income in the same accounting period, which consist of cost of sales and other expenses.

## ACCOUNTING EQUATION

Basic: **Assets = Liabilities + *Equity***

**Assets = Liabilities + *[Capital + Profit for the year – Drawings]***

Expanded: **Assets = Liabilities + *[Capital + (Income – Expenses) – Drawings]***

Note: Rearranging the equation
Assets + Expenses + Drawings = Liabilities + Income + Capital

## KEYWORDS TO IDENTIFY ACCOUNT NAMES

| Keywords | Account Name |
|---|---|
| ▪ Cheque<br>▪ Dishonoured cheque<br>▪ Bank<br>▪ Receipt | Cash at bank |
| ▪ Cash | Cash in hand |
| ▪ Took for own / personal / private use<br>*(Not for office / business use)* | Drawings |
| ▪ For resale<br>▪ Goods / stock | Inventory |
| ▪ Credit customer<br>▪ Sold goods on credit<br>▪ Debtor | Trade receivable |
| ▪ Credit supplier<br>▪ Bought goods on credit<br>▪ Creditor | Trade payable |
| ▪ Computer<br>▪ Machinery<br>▪ Printer | Equipment |
| ▪ Tables and chairs<br>▪ Shelves<br>▪ Cupboard | Fixtures and fittings |
| ▪ Received<br>▪ Earned | __________ income |
| ▪ Paid<br>▪ Incurred | __________ expense |

# CHAPTER 4 DOUBLE-ENTRY RECORDING

## DOUBLE ENTRY SYSTEM

The double entry system states that there must be **<u>at least two</u>** accounts recorded for every business transaction. The total **<u>debit</u>** and total **<u>credit</u>** values are always **<u>equal</u>.**

## CONCEPT OF DEBIT & CREDIT

" **A**fter **E**very **D**inner, **L**et's **I**nnovate **C**reatively"

| Dr | **A**ssets | Cr |
|---|---|---|
| + | | - |

1. Premises / Land & Property
2. Equipment
3. Fixtures and fittings
4. Motor vehicle
5. Inventory *(goods/stock/for resale)*
6. Cash at bank *(cheque)*
7. Cash in hand *(cash)*
8. Trade receivables
9. Prepaid expense
10. Income receivables

| Dr | **L**iabilities | Cr |
|---|---|---|
| - | | + |

1. Loan from bank
2. Mortgage
3. Bank overdraft
4. Trade payables
5. Expense payables
6. Income received in advance

| Dr | **E**xpenses | Cr |
|---|---|---|
| + | | |

1. Cost of sales
2. Utilities expense
3. Repairs and maintenance
4. Insurance expense
5. Advertising expense
6. Salaries expense
7. Rent expense
8. Commission expense
9. Stationery
10. Discount allowed
11. Bank charges
12. Interest on loan

| Dr | **I**ncome | Cr |
|---|---|---|
| | | + |

1. Sales revenue
   *(income earned from selling goods)*
2. Service fee revenue
3. Commission income
4. Rent income
5. Discount received
6. Interest on fixed deposit

| Dr | **C**apital | Cr |
|---|---|---|
| | | + |

Owner's contribution of personal assets for business use

| Dr | **D**rawings | Cr |
|---|---|---|
| + | | |

Owner's takings of business assets for his personal use

## JOURNAL ENTRIES

**Journal**

| | Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|---|
| | 2025 | | | |
| Dr entry | Jan 14 | Trade payable John | 2 000 | |
| Cr entry | | Cash at bank | | 2 000 |
| Narration | | *The business paid trade payable John* | | |
| | | *$2000 cheque.* | | |
| | | | | |
| | Jan 26 | Cash at bank | 3 000 | |
| | | Capital | | 3 000 |
| | | *Owner contributed $3000 into the* | | |
| | | *business bank account.* | | |

Purpose of narration: Helps in recalling the background of each transaction without having to refer to the source documents.

*Note: The Dr entry is always presented first in the Journal.*

## LEDGER ACCOUNTS

this means Cr CAB 2000

Dr/Cr must be indicated in the Bal column

Heading and Particulars are NEVER the same!

**Cash at Bank Account**

| 2024 | Particulars | Dr $ | Cr $ | Bal $ | |
|---|---|---|---|---|---|
| Jan 1 | Balance b/d | | | 10 000 | Dr* |
| 14 | Trade payable John | | 2 000 | 8 000 | Dr |
| 26 | Capital | 3 000 | | 11 000 | Dr |
| 2025 | | | | | |
| Feb 1 | Balance b/d | | | 11 000 | Dr* |

* Only the first and last running balance are required

## CLOSING OF LEDGER ACCOUNTS

At the end of each month, running balances of **all** ledger accounts are bought down (balance b/d) to the next month.

At the end of each year, income and expenses accounts are closed and transferred to income summary account.

## DOUBLE ENTRY RECORDING

**Capital contribution from Owner**

| | Dr $ | Cr $ |
|---|---|---|
| Cash in hand/ Cash at bank/ Inventory/ Equipment (A+) | xxx | |
| Capital (C+) | | xxx |

**Drawings taken by Owner**

| | Dr $ | Cr $ |
|---|---|---|
| Drawings (D+) | xxx | |
| Cash in hand/ Cash at bank/ Inventory/ Equipment (A-) | | xxx |

**Borrowing of Loan**

| | Dr $ | Cr $ |
|---|---|---|
| Cash in hand/ Cash at bank (A+) | xxx | |
| Loan from XXX Bank (L+) | | xxx |

**Repayment of Loan**

| | Dr $ | Cr $ |
|---|---|---|
| Loan from XXX Bank (L-) | xxx | |
| Cash in hand/ Cash at bank (A-) | | xxx |

**Payment for Expenses**

| | Dr $ | Cr $ |
|---|---|---|
| Rent expense/ Stationery/ Salaries and wages/ Utilities (E+) | xxx | |
| Cash in hand/ Cash at bank (A-) | | xxx |

**Receipt from Income**

| | Dr $ | Cr $ |
|---|---|---|
| Cash in hand/ Cash at bank (A+) | xxx | |
| Interest income/ Commission income/ Rent income (I+) | | xxx |

**Purchase of Non-Current Assets**

| | Dr $ | Cr $ |
|---|---|---|
| Furniture/ Equipment/ Motor vehicle (A+) | xxx | |
| Cash in hand / Cash at bank (A-)/ Trade payable-XXX (L+) | | xxx |

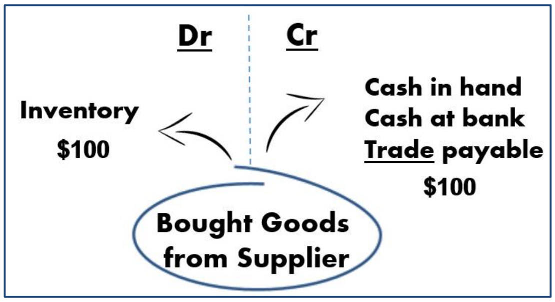
**Transfer of funds: Withdrawal for office use**

| | Dr $ | Cr $ |
|---|---|---|
| Cash in hand (A+) | xxx | |
| Cash at bank (A-) | | xxx |

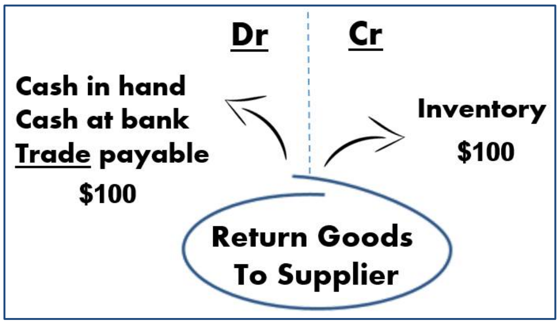
**Transfer of funds: Deposit business funds**

| | Dr $ | Cr $ |
|---|---|---|
| Cash at bank (A+) | xxx | |
| Cash in hand (A-) | | xxx |

## Between Business and Supplier Jack

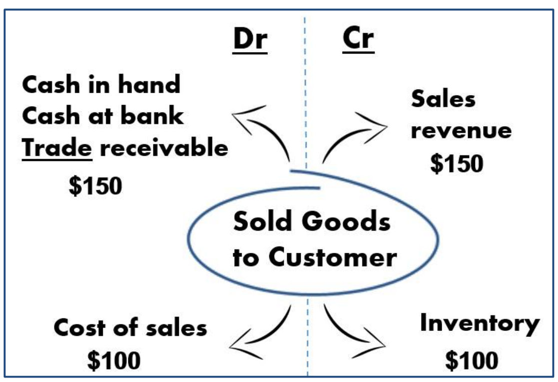



| | Dr $ | Cr $ |
|---|---|---|
| Inventory (A+) | 100 | |
| Cash in hand (A-)/<br>Cash at bank(A-)/<br>Trade payable-Jack(L+) | | 100 |

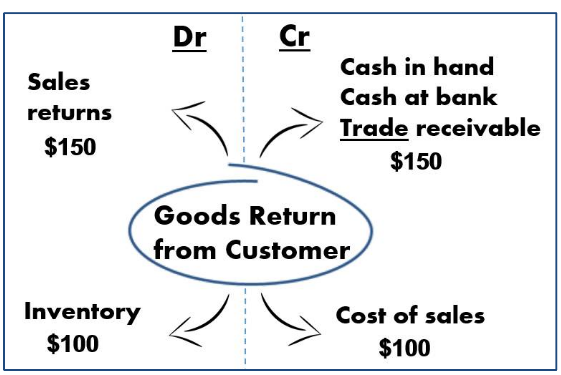



| | Dr $ | Cr $ |
|---|---|---|
| Cash in hand (A+)/<br>Cash at bank (A+)/<br>Trade payable-Jack (L-) | 100 | |
| Inventory (A-) | | 100 |

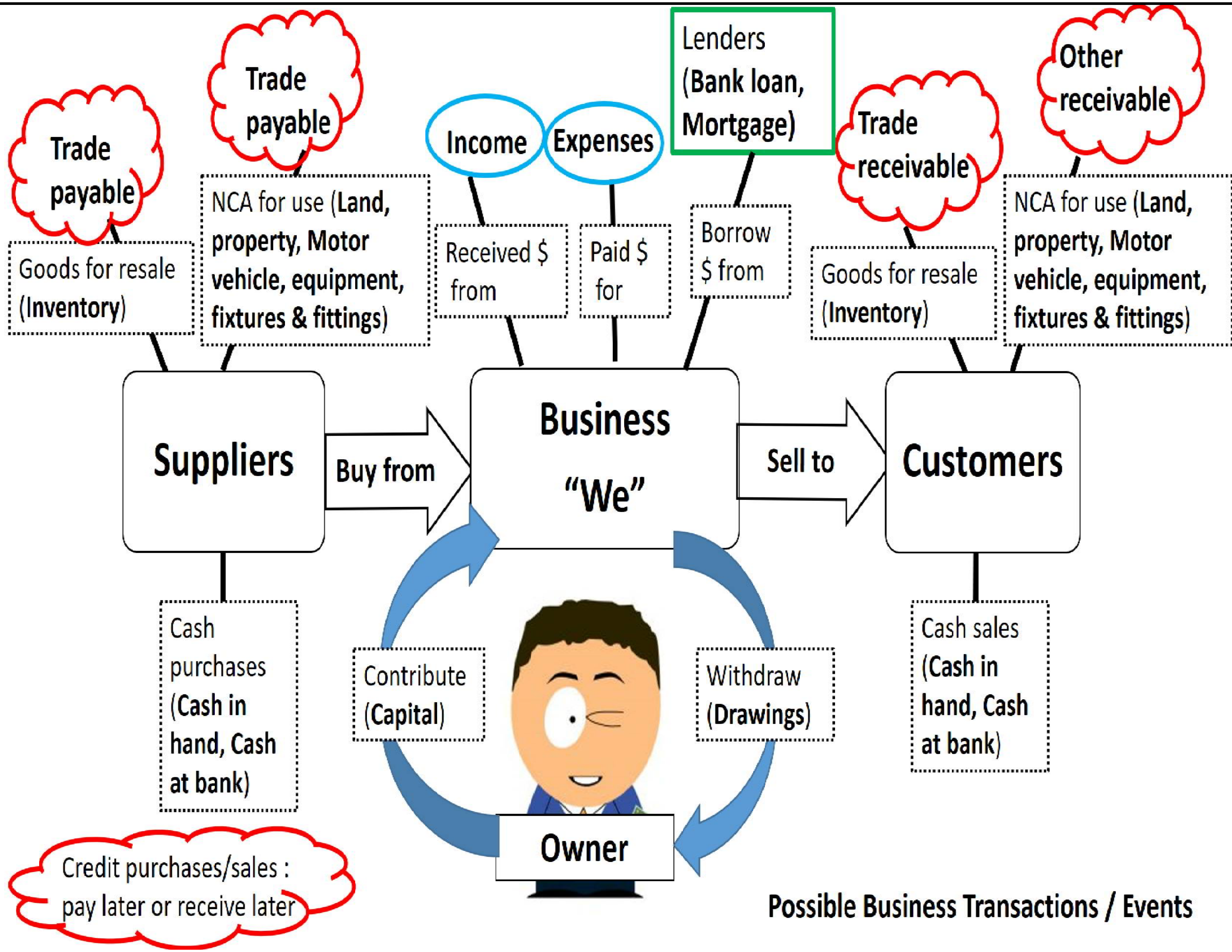
## Between Business and Customer Tom




| | Dr $ | Cr $ |
|---|---|---|
| Cash in hand (A+)/<br>Cash at bank (A+)/<br>**T**rade receivable-Tom (A+) | 150 | |
| **S**ales revenue (I+) | | 150 |
| | | |
| **C**ost of sales (E+) | 100 | |
| **I**nventory (A-) | | 100 |




| | Dr $ | Cr $ |
|---|---|---|
| **S**ales returns (I-) | 150 | |
| Cash in hand (A-)/<br>Cash at bank (A-)/<br>**T**rade receivable-Tom (A-) | | 150 |
| | | |
| **I**nventory (A+) | 100 | |
| **C**ost of sales (E-) | | 100 |




**Possible Business Transactions / Events**

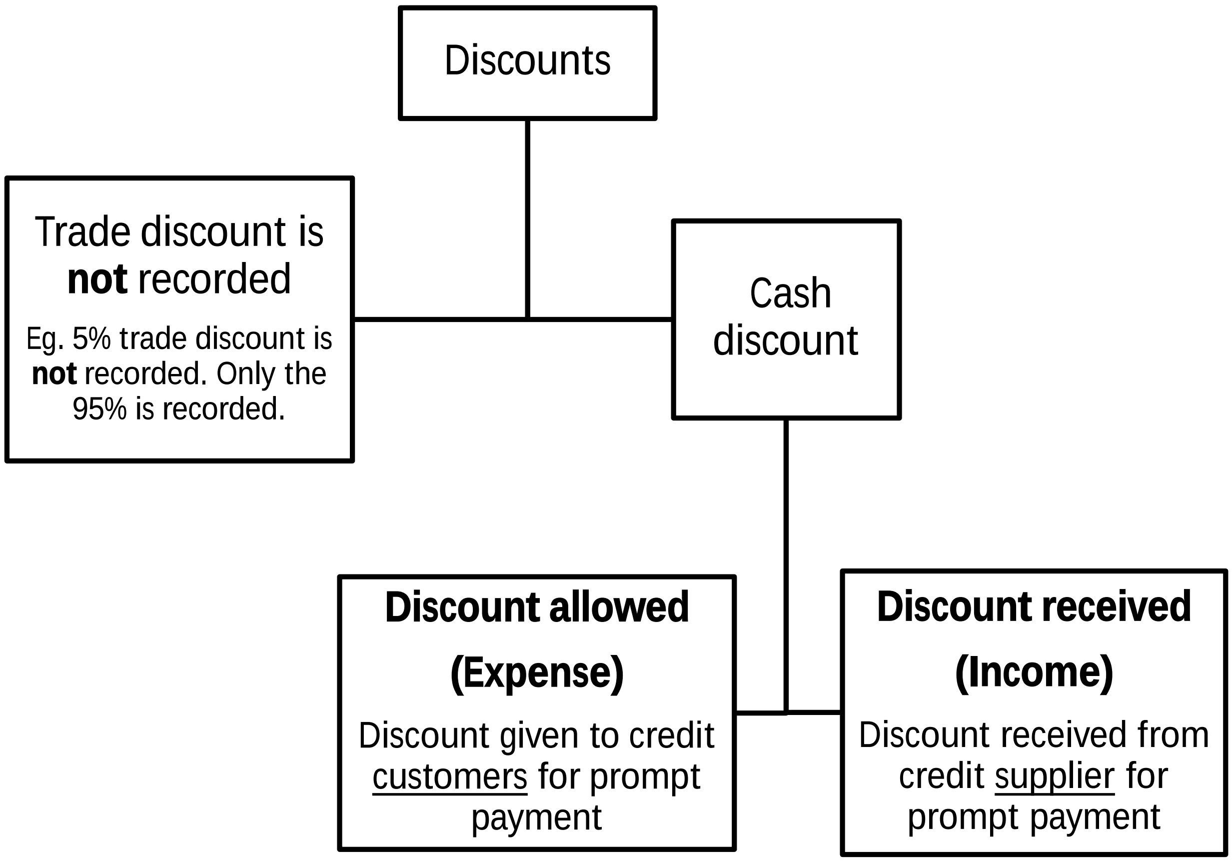
## TRADE DISCOUNT AND CASH DISCOUNT

| | | Trade Discount | Cash Discount |
|---|---|---|---|
| 1 | *Definition (what is…?)* | Reduction to the **list price** | Reduction to the **invoiced price** |
| 2 | *Purpose (why give?)* | **To encourage:**<br>• **customers to buy in bulk**<br>• **customer patronage**<br>• **customer loyalty** | **To encourage credit customers to pay promptly, by a specified date** |
| 3 | *When given?* | Given at the **point of sale**<br><br>…means given when the order is placed and sale is confirmed | Given at the **point of payment**<br><br>…means given when cash/cheque is received |
| 4 | *How to record?* | Trade discount is **not recorded**<br><br>Eg. 5% trade discount is not recorded. Only the 95% is recorded. | **Recorded as discount allowed or discount received**<br><br>Dr Discount allowed (E+)<br>Cr Trade receivable Name (A-)<br><br>Dr Trade payable Name (L-)<br>Cr Discount received (I+) |
| 5 | *Example* | Buy 10 get 10% discount<br>Buy 20 get 20% discount | If payment is made within 10 days, 5% discount will be given. |

*Note:*
*List price = Original price (before discount)*
*Net price = After discount*
*Invoiced amount = Amount owing as stated in the invoice*

Refer to Chapter 10 for trade receivable account
Refer to Chapter 12 for trade payable account

**DISCOUNTS**


Discounts
Trade discount is **not** recorded
Eg. 5% trade discount is **not** recorded. Only the 95% is recorded.
Cash discount
**Discount allowed (Expense)**
Discount given to credit customers for prompt payment
**Discount received (Income)**
Discount received from credit supplier for prompt payment

# CHAPTER 5 TRIAL BALANCE & FINANCIAL STATEMENTS

## TRIAL BALANCE

**Definition**
A trial balance is a listing of ledger account balances at a specific date.

**Purpose**
- Facilitate the preparation of the financial statements
- Ensure arithmetic accuracy in recording

**A**ssets
**E**xpenses
**D**rawings

**L**iabilities
**I**ncome
**C**apital

**JYSS Ltd**
**Trial Balance as at 31 October 2025**

| | Dr<br>$ | Cr<br>$ |
|---|---|---|
| Trade receivables | xx | |
| Allowance for impairment of trade receivables *(contra-asset)* | | xx |
| Cash at bank | xx | |
| Inventory | xx | |
| Trade payables | | xx |
| Long term borrowing | | xx |
| Capital | | xx |
| Sales revenue | | xx |
| Sales returns *(contra-income)* | xx | |
| Drawings | xx | |
| Cost of sales | xx | |
| Rent expense | xx | |
| Equipment | xx | |
| Accumulated depreciation *(contra-asset)* | | xx |
| Interest income | | xx |
| | Xxx | Xxx |

Ensure that
total debit = total credit

## STATEMENT OF FINANCIAL PERFORMANCE

**Definition**
A financial statement that shows the income earned and expenses incurred for a period of time to determine the profit or loss of a business.

**Income** are earnings from the activities of a business. It consists of:
(i) Revenue could be sales revenue or service fee revenue. Sales revenue earned from selling goods. Service fee revenue is earned from providing services.
(ii) Other income is earnings which are not from normal sale of goods and services e.g. interest income.
(iii) Other gains arise when the business sells its non-current assets.

**Expenses** are costs incurred to earn income in the same accounting period, which consist of cost of sales and other expenses.

**Application of Accounting Theory**

1. **Going concern theory**
A business is assumed to have indefinite economic life unless there is credible evidence that it may close down. Financial statements are prepared to assess the performance and position of the business for continuity.

2. **Accounting period theory**
The life of a business is divided into regular time intervals to allow for meaningful reporting. The statement of financial performance is prepared periodically (usually yearly) to assess the profitability of the business.

| Trading portion | Profit and loss portion |
|---|---|
| Shows gross profit or loss | Shows (overall) profit or loss for the year |
| Reflects how well the business is able to sell its goods to generate profit | Reflects the overall profitability of a business |
| Gross Profit<br>= Sales revenue – Sales returns<br>– Cost of sales | Profit for the year<br>= Gross profit + Other income<br>– Other expenses |

**TRADING BUSINESS**

**JYSS Trading**
**Statement of Financial Performance for the year ended 31 October 2025**

| | | $ | $ |
|---|---|---|---|
| Trading portion | **Sales revenue** | X | |
| | Less: **Sales returns** | X | |
| | Net sales revenue | | X |
| | Less: **Cost of sales** | | X |
| | Gross profit / Gross loss | | XX / (XX) |
| | | | |
| Profit & Loss portion | <u>Other income</u> | | |
| | Discount received | X | |
| | Rent income | X | XX |
| | | | |
| | <u>Less: Other expenses</u> | | |
| | Impairment loss on trade receivables | X | |
| | OR Reversal of impairment loss on trade receivables | (X) | |
| | Depreciation of fixtures and fittings | X | |
| | Depreciation of motor vehicles | X | |
| | Insurance expense | X | |
| | Commission expense | X | |
| | Bank charges | X | |
| | Discount allowed | X | |
| | ⋮ | ⋮ | XX |
| | Profit for the year / Loss for the year | | XX / (XX) |

*Items in the trading portion are <u>fixed</u>!*

*If there's <u>no sales returns</u>, <u>skip net sales revenue</u> too.*

Note: Single solid line means "sum up the above figures".
"Less" means subtract.
Bracket means "negative".
Double line means "the end"

For income and expenses in the P&L portion, include only the items reflected in the question. The income and expenses provided above are only examples.

## SERVICE BUSINESS

**JYSS Service**
**Statement of Financial Performance for the year ended 31 October 2025**

| | $ | $ |
|---|---|---|
| Service fee revenue | | XX |
| | | |
| <u>Other income</u> | | |
| Discount received | X | |
| Rent income | X | XX |
| | | |
| <u>Less: Other expenses</u> | | |
| Impairment loss on trade receivables | X | |
| OR Reversal of impairment loss on trade receivables | (X) | |
| Depreciation of fixtures and fittings | X | |
| Depreciation of motor vehicles | X | |
| Insurance expense | X | |
| Commission expense | X | |
| Bank charges | X | |
| Discount allowed | X | |
| ⋮ | | XX |
| Profit for the year / Loss for the year | | XX / (XX) |

Profit & Loss portion

Note: Single solid line means "sum up the above figures".
"Less" means subtract.
Bracket means "negative".
Double line means "the end"

There is <u>NO</u> trading portion as the service business does not trade i.e. buy and sell goods. It is replaced by service fee revenue (the main income earned from providing services), and is set apart from other income.

For income and expenses in the P&L portion, include only the items reflected in the question. The income and expenses provided above are only examples.

## STATEMENT OF FINANCIAL POSITION

**Definition**
A list of the assets, liabilities and equity of a business at a specified date.

**Non-current Assets** are resources that have benefits that **last** beyond one financial year, and are not easily converted to cash.

**Current Assets** are resources that have benefits that are **used** within one financial year, and are easily converted to cash.

**Owner's Equity** is the claim by the owner on the net assets of a business.

**Non-current Liabilities** are long-term debts due to be repaid after one financial year.

**Current Liabilities** are short-term debts due to be repaid within one financial year.

### Application of Accounting Theory

1. **Accounting period theory**
   The life of a business is divided into regular time intervals to allow for meaningful reporting.
   The statement of financial position is prepared periodically to provide information on how the resources are obtained and used in a business and the claim by the owner/s on the net assets of the business on a certain date.

## BANK OVERDRAFT VS CASH AT BANK

**Business Cash at Bank Account**

← Overspends and **owes** the bank an overdraft.
**Bank Overdraft** (Current Liability)
**Cr** CAB balance

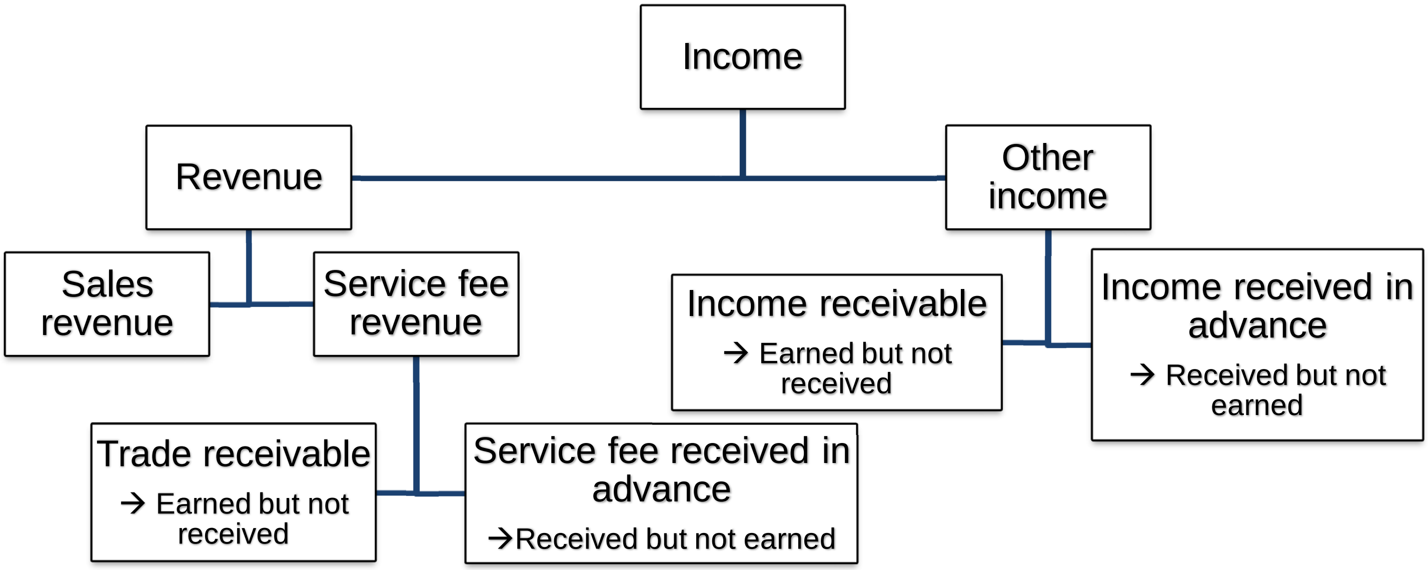
→ Positive balance in the bank
**Cash at Bank** (Current Asset)
**Dr** CAB balance

**SOLE PROPRIETORSHIP**

**JYSS Trading**
**Statement of Financial Position as at 31 October 2025**

| | | $ | $ |
|---|---|---|---|
| **ASSETS** | | | |
| Non-current assets | Cost | Accumulated depreciation | Net book value |
| Motor vehicle | X | X | X |
| Equipment | X | X | X |
| Fixtures and fittings | X | X | X |
| | | | XX |
| Current assets | | | |
| Trade receivables | X | | |
| Less: Allowance for impairment of trade receivables | X | X | |
| Inventory | | X | |
| Other receivables | | X | |
| Cash in hand | | X | |
| Cash at bank | | X | |
| Prepaid ________ expense | | X | |
| ________ income receivable | | X | XX |
| **Total assets** | | | XXX |
| | | | |
| **EQUITY AND LIABILITIES** | | | |
| Owner's Equity | | | |
| Capital *(Beginning capital + Additional capital + Profit for the year / – Loss for the year – Drawings)* | | | XX |
| | | | |
| Non-current liabilities | | | |
| Long-term borrowings *(Loan / Mortgage)* | | | XX |
| | | | |
| Current liabilities | | | |
| Current-portion of long-term borrowings | | X | |
| Bank overdraft | | X | |
| Trade payables | | X | |
| ________ expense payable | | X | |
| ________ income received in advance | | X | XX |
| **Total equity and liabilities** | | | XXX |

# CHAPTER 6 INCOME




- Received = cash / cheque is received
- Earned = goods / services have been provided

| **Income Receivable** | **Income Received in Advance** |
|---|---|
| ▪ Owing/Outstanding/Due/Accrued<br>▪ **Earned but not yet received**<br>▪ Received < Earned<br>▪ Receivable = Earned – Received<br>▪ Recorded as **Current Assets** | ▪ Unearned/owed services or goods<br>▪ **Received but not yet earned**<br>▪ Received > Earned<br>▪ Received in Advance = Received – Earned<br>▪ Recorded as **Current Liabilities** |

## Application of Accounting Theory

1. **Revenue recognition theory**
   Income is recognised when goods have been delivered or services have been provided.

2. **Accrual basis of accounting**
   Income is recognised when goods are delivered or services are provided regardless whether payment is received.

## SALES REVENUE

Sales revenue is the income earned from the sale of goods, and is credit in nature.

### Journal Entry

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Jun 12 | Trade receivable Jeff (A+) | 3 000 | |
| | **Sales revenue** (I+) | | 3 000 |
| | Cost of sales (E+) | 1 200 | |
| | Inventory (A-) | | 1 200 |
| | *Sold goods on credit to Jeff for $3000. The cost of goods sold was $1200.* | | |
| | | | |
| Jun 26 | Cash in hand (A+) | 4 000 | |
| | **Sales revenue** (I+) | | 4 000 |
| | Cost of sales (E+) | 2 700 | |
| | Inventory (A-) | | 2 700 |
| | *Sold goods to Tom for $4000 and received cash. The cost of goods sold was $2700.* | | |
| | | | |
| Jun 30 | **Sales revenue** (I-) | 8 000* | |
| *(year-end)* | Income summary (I+) | | 8 000 |
| ***(Closing entry)*** | *Total sales revenue **earned** for the year transferred to income summary account.* | | |

**Sales revenue account**

| 2021 | | Dr -<br>$ | Cr +<br>$ | Bal<br>$ |
|---|---|---|---|---|
| Jun 1 | Balance b/d | | | 1 000 Cr |
| 12 | Trade receivable Jeff | | 3 000 | 4 000 Cr |
| 26 | Cash in hand | | 4 000 | 8 000 Cr |
| 30 | Income summary | 8 000* | | 0 |

### Interpretation

- 1 Jun: Sales revenue of $1000 was brought down from May 2021 to Jun 2021.
- 12 Jun: The business sold goods **for** $3000 on credit to Jeff.
- 26 Jun: The business sold goods and received $4000 in cash.
- 30 Jun: $8000 of sales revenue was earned during the year and transferred to the income summary account.

## SALES RETURNS

Sales returns are the return of goods from customers, and is debit in nature.

### Journal Entry

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Jun 19 | **Sales returns** (I-) | 500 | |
| | Trade receivable Jeff (A-) | | 500 |
| | Inventory (A+) | 100 | |
| | Cost of sales (E-) | | 100 |
| | *Customer Jeff returned goods that was previously sold to him on credit for $500. The cost of goods sold was $100.* | | |
| | | | |
| Jun 28 | **Sales returns** (I-) | 900 | |
| | Cash in hand (A-) | | 900 |
| | Inventory (A+) | 300 | |
| | Cost of sales (E-) | | 300 |
| | *Customer Tom returned goods and $900 cash refund was made to him. The cost of goods sold was $300.* | | |
| | | | |
| Jun 30 | Income summary (-I+) | 3 400* | |
| *(year-end)* | **Sales returns** (-I-) | | 3 400 |
| ***(Closing entry)*** | *Total sales returns for the year transferred to income summary account.* | | |

**Sales returns account**

| 2021 | | Dr +<br>$ | Cr -<br>$ | Bal<br>$ |
|---|---|---|---|---|
| Jun 1 | Balance b/d | | | 2 000 Dr |
| 19 | Trade receivable Jeff | 500 | | |
| 28 | Cash in hand | 900 | | 3 400 Dr |
| 30 | Income summary | | 3 400* | 0 |

### Interpretation

- 1 Jun: Sales returns $2 000 was brought down from May 2021 to Jun 2021.
- 19 Jun: Customer Jeff returned goods previously sold to him on credit **for** $500.
- 28 Jun: Customer returned goods and $900 cash refund was made to him.
- 30 Jun: Sales returns totalled $3400 for the year was transferred to the income summary account.

## INCOME RECEIVABLE

It is income earned this year but payment have not been received. It is recorded as a **current asset** in the statement of financial position.

### Journal Entry

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Jan 1 | Income (I-) | 2 000 | |
| | Income receivable (A-) | | 2 000 |
| | *Income earned but not yet received last year was reversed.* | | |
| | | | |
| Dec 31 | Cash at bank / cash in hand (A+) | 5 000 | |
| (use date if given) | Income (I+) | | 5 000 |
| | *The business **received** cheque / cash for income.* | | |
| | | | |
| Dec 31 | Income (I-) | 3 400 | |
| *(year-end)* | Income summary (I+) | | 3 400 |
| ***(Closing entry)*** | *Income **earned** during the year was transferred to income summary account.* | | |
| | | | |
| Dec 31 | Income receivable (A+) | 400 | |
| *(year-end)* | Income (I+) | | 400 |
| | *Income earned this year but have not been received was adjusted.* | | |

Income account (I)

| 2021 | Particulars | Dr $<br>- | Cr $<br>+ | Bal $ |
|---|---|---|---|---|
| Jan 1 | Income receivable (**0**) | 2 000 | | 2 000 Dr |
| Dec 31 | Cash in hand / Cash at bank (**1**) | | 5 000 | |
| Dec 31 | Income summary (**2**) | 3 400 | | |
| Dec 31 | Income receivable (**3**) | | 400 | 0 |

**Interpretation**

**(0)** 1 Jan 2021: Income of $2000 earned but not received last year was reversed.

**(1)** 31 Dec 2021: The business received cash/cheque of $5000 for income.

**(2)** 31 Dec 2021: Income of $3400 was earned during the year and transferred to the income summary account.

**(3)** 31 Dec 2021: Income of $400 earned this year but have not been received was adjusted.

## INCOME RECEIVED IN ADVANCE

It is income received this year but not earned. It is recorded as a **current liability** in the statement of financial position.

### Journal Entry

Journal

| Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| 2020 | | | |
| Apr 1 | Income received in advance (L-) | 600 | |
| | Income (I+) | | 600 |
| | *Income received but not yet earned last year was reversed.* | | |
| 2021 | | | |
| Mar 31 | Cash at bank / cash in hand (A+) | 1 000 | |
| (use date if given) | Income (I+) | | 1 000 |
| | *The business* ***received*** *cheque / cash for* income. | | |
| | | | |
| Mar 31 | Income (I-) | 900 | |
| *(year-end)* | Income summary (I+) | | 900 |
| ***(Closing entry)*** | *Income* ***earned*** *during the year was transferred to income summary.account.* | | |
| | | | |
| Mar 31 | Income (I-) | 700 | |
| *(year-end)* | Income received in advance (L+) | | 700 |
| | *Income received this year but have not been earned was adjusted.* | | |

Income account (I)

| 2020 | Particulars | Dr $ - | Cr $ + | Bal $ |
|---|---|---|---|---|
| Apr 1 | Income received in advance (**0**) | | 600 | 600 Cr |
| 2021<br>Mar 31 | Cash in hand/ Cash at bank (**1**) | | 1 000 | |
| Mar 31 | Income summary (**2**) | 900 | | |
| Mar 31 | Income received in advance (**3**) | 700 | | 0 |

### Interpretation

**(0)** 1 Apr 2020: Income of $600 received but not yet earned last year was reversed.
**(1)** 31 Mar 2021: The business received cash/cheque of $1000 for income.
**(2)** 31 Mar 2021: Income of $900 was earned during the year and transferred to the income summary account.
**(3)** 31 Mar 2021: Income of $700 received this year but have not been earned was adjusted.

**Summary**

| | | | |
|---|---|---|---|
| **0** | **Reversal** at the start of the financial year | Reversal of last year's income received in advance | Dr Income received in advance **(L-)**<br>Cr *Income* (I+) |
| | | Reversal of last year's income receivable | Dr *Income* (I-)<br>Cr Income receivable **(A-)** |
| **1** | Record income **received** | | Dr **Cash in hand / Cash at bank** (A+)<br>Cr *Income* (I+) |
| **2** | Record income **earned** (**closing entry** / transfer to income summary a/c at end of financial year) | | Dr *Income* (I-)<br>Cr **Income Summary** (I+) |
| **3** | **Adjustment** at the end of the financial year | Adjust for income received in advance | Dr *Income* (I-)<br>Cr Income received in advance **(L+)** |
| | | Adjust for income receivable | Dr Income receivable **(A+)**<br>Cr *Income* (I+) |

☟ Income account (I)

| 2021 | Particulars | Dr $<br>- | Cr $<br>+ | Bal $ |
|---|---|---|---|---|
| Jan 1 | Income receivable /<br>Income received in advance (**0**) | **R**eceivable | Received in **A**dvance | |
| Dec 31 | Cash in hand / Cash at bank (**1**) | | √ | |
| Dec 31 | Income summary (**2**) | √ | | |
| Dec 31 | Income received in advance /<br>Income receivable (**3**) | Received in **A**dvance | **R**eceivable | 0 |

JYSS Ltd

Statement of Financial Performance for year ended 31 December 2021 (extract)

| | | $ |
|---|---|---|
| Other Income | | |
| ___________ income **(2)** | Amount transferred to the **income summary** account → | XX |

JYSS Ltd

Statement of Financial Position as at 31 December 2021 (extract)

| | $ |
|---|---|
| **Current assets** | |
| ___________ income **receivable (3)** | XX |
| | |
| **Current liabilities** | |
| ___________ income **received in advance (3)** | XX |

## Calculation of Income Earned

| | | | | ***Not*** *earned this year* | | ***Earned*** *this year* |
|---|---|---|---|---|---|---|
| Income **earned*** this year | = | Cash / cheque **received** | – | Last year's **receivable**<br>OR<br>This year's **received in advance** | + | Last year's **received in advance**<br>OR<br>This year's **receivable** |

*Income earned is the closing entry transferred to **income summary account**
Also reflected in the **statement of financial performance**

Earned = – Receivable (start) + Received + Receivable (end)

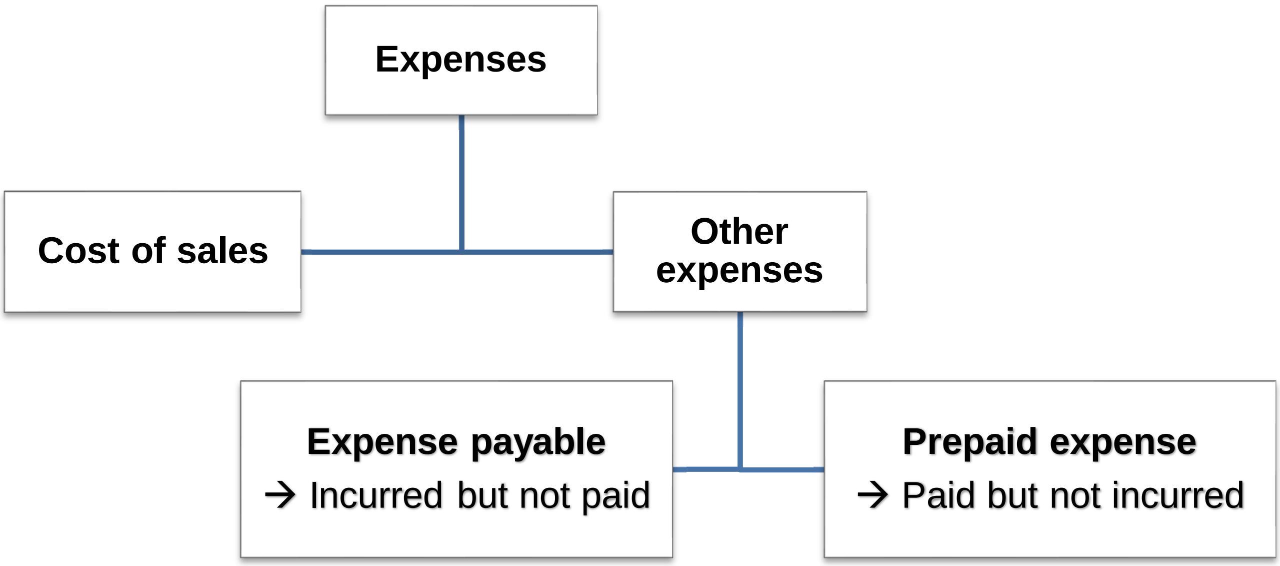
Earned = + Received in advance (start) + Received – Received in advance (end)

## Effects of Year-End Adjustment

| Income receivable | Effect on | | |
|---|---|---|---|
| | **Income** | **Profit** | **Current Asset** |
| **If not** adjusted | Understated | Understated | Understated |
| **After** adjustment | Increased | Increased | Increased |

| Income received in advance | Effect on | | |
|---|---|---|---|
| | **Income** | **Profit** | **Current Liability** |
| **If not** adjusted | Overstated | Overstated | Understated |
| **After** adjustment | Decreased | Decreased | Increased |

# CHAPTER 7 EXPENSES




| Expense Payable | Prepaid Expense |
|---|---|
| ▪ Owing/Outstanding/Due/Payable/Accrued<br>▪ **Incurred but not yet paid**<br>▪ Paid < Incurred (used)<br>▪ Payable = Incurred – Paid<br>▪ Recorded as **Current Liabilities** | ▪ Paid in advance<br>▪ **Paid but not yet incurred**<br>▪ Paid > Incurred (used)<br>▪ Prepaid = Paid – Incurred<br>▪ Recorded as **Current Assets** |

## Application of Accounting Theory

1. **Matching theory**
   The cost of sales must be matched against the sales revenue earned from selling the inventory in the same accounting year to determine the gross profit.

   Other costs incurred to generate revenue and other income must be matched against revenue and other income earned in the same accounting year to determine the profit for the year.

2. **Accrual basis of accounting**
   Expenses are recognised when incurred regardless whether payment is made.

## COST OF SALES

It is the cost of goods sold, recorded when goods are sold and reversed when sold goods are returned. It is an expense, and is debit in nature.

### Journal Entry

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Dec 15 | Trade receivable Akif (A+) | 1 000 | |
| | Sales revenue (I+) | | 1 000 |
| | **Cost of sales** (E+) | 600 | |
| | Inventory (A-) | | 600 |
| | *Sold goods to Akif on credit for $1 000. The cost of goods sold was $600.* | | |
| | | | |
| Dec 24 | Cash at bank (A+) *(if received cash→ Cash in hand)* | 750 | |
| | Sales revenue (I+) | | 750 |
| | **Cost of sales** (E+) | 330 | |
| | Inventory (A-) | | 330 |
| | *Sold goods and received $750 cheque. The cost of goods sold was $330.* | | |
| | | | |
| Dec 28 | Sales returns (I-) | 50 | |
| | Trade receivable Akif (A-) | | 50 |
| | Inventory (A+) | 10 | |
| | **Cost of sales** (E-) | | 10 |
| | *Akif returned goods worth $50. The cost of goods sold was $10.* | | |
| | | | |
| Dec 31 | Income summary (E+) | 920 | |
| *(year-end)* | **Cost of sales** (E-) | | 920 |
| ***(Closing entry)*** | *Total sales returns for the year was transferred to income summary account.* | | |

**Cost of sales account**

| 2021 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Dec 1 | Balance b/d | | | 4 000 Dr |
| 15 | Inventory | 600 | | |
| 24 | Inventory | 330 | | |
| 28 | Inventory | | 10 | 4 920 Dr |
| 31 | Income summary | | 4 920 | 0 |

Cost of sales **increases** when goods are **sold**

**Interpretation**

- 1 Dec 2021: Cost of sales of $4000 was brought down from Nov to Dec.
- 15 Dec 2021: The business sold goods **costing** $600.
- 24 Dec 2021: The business sold goods **costing** $330.
- 28 Dec 2021: Customers returned goods **costing** $10.
- 31 Dec 2021: A total of $4920 cost of sales was **incurred** during the year and transferred to the income summary account.

## PREPAID EXPENSE

It is an expense paid in advance this year but services have not been incurred or used. It is recognised as a **current asset** in the statement of financial position.

### Journal Entry

Journal

| Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| 2020 | | | |
| July 1 | Expense (E+) | 500 | |
| | Prepaid expense (A-) | | 500 |
| | *Reversal entry for the prepaid expense recorded last year.* | | |
| 2021 | | | |
| Jun 30 | Expense (E+) | 2 000 | |
| (use date if given) | Cash at bank / cash in hand (A-) | | 2 000 |
| | *The business **paid** cheque / cash for* expense. | | |
| | | | |
| Jun 30 | Income summary (E+) | 1 100 | |
| *(year-end)* | Expense (E-) | | 1 100 |
| ***(Closing entry)*** | *Expense **incurred** for the year transferred to income summary account.* | | |
| | | | |
| Jun 30 | Prepaid expense (A+) | 1 400 | |
| *(year-end)* | Expense (E-) | | 1 400 |
| | *Expense paid in advance this year but not incurred.* | | |

Expense account

| 2020 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Jul 1 | Prepaid expense (**0**) | 500 | | 500 Dr |
| 2021 Jun 30 | Cash in hand/ Cash at bank (**1**) | 2 000 | | |
| Jun 30 | Income summary (**2**) | | 1 100 | |
| Jun 30 | Prepaid expense (**3**) | | 1 400 | 0 |

### Interpretation

**(0)** 1 Jul 2020: Expense of $500 paid but not incurred last year was reversed.
**(1)** 30 Jun 2021: The business paid cash/cheque of $2000 for expense.
**(2)** 30 Jun 2021: Expense of $1100 was incurred during the year and transferred to the income summary account.
**(3)** 30 Jun 2021: Expense of $1400 paid this year but have not been incurred was adjusted.

**EXPENSE PAYABLE**

It is expense incurred this year but not yet paid. The owing of the expense is recognised as a **current liability** in the statement of financial position.

**Journal Entry**

Journal

| Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| 2020 | | | |
| Oct 1 | Expense payable (L-) | 800 | |
| | Expense (E-) | | 800 |
| | *Reversal entry for the expense payable recorded last year.* | | |
| 2021 | | | |
| Sep 30 | Expense (E+) | 1 000 | |
| (use date if given) | Cash at bank / cash in hand (A-) | | 1 000 |
| | *The business **paid** cheque / cash for* expense. | | |
| | | | |
| Sep 30 | Income summary (E+) | 400 | |
| *(year-end)* | Expense (E-) | | 400 |
| ***(Closing entry)*** | *Expense **incurred** for the year transferred to income summary.* | | |
| | | | |
| Sep 30 | Expense (E+) | 200 | |
| *(year-end)* | Expense payable (L+) | | 200 |
| | *Expense incurred but not paid this year.* | | |

Expense account

| 2020 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Oct 1 | Expense payable (**0**) | | 800 | 800 Cr |
| 2021 Sep 30 | Cash in hand/ Cash at bank (**1**) | 1 000 | | |
| Sep 30 | Income summary (**2**) | | 400 | |
| Sep 30 | Expense payable (**3**) | 200 | | 0 |

**Interpretation**

**(0)** 1 Oct 2020: Expense of $800 incurred but not paid last year was reversed.
**(1)** 30 Sep 2021: The business paid cash/cheque of $1000 for expense.
**(2)** 30 Sep 2021: Expense of $400 was incurred during the year and transferred to the income summary account.
**(3)** 30 Sep 2021: Expense of $200 was incurred this year but have not been paid was adjusted.

**Summary**

| | | | |
|---|---|---|---|
| **0** | **Reversal** at the start of the financial year | Reversal of last year's expenses payable | Dr Expense payable (L-)<br>*Cr Expense (E-)* |
| | | Reversal of last year's prepaid expenses | *Dr Expense (E+)*<br>Cr Prepaid expense (A-) |
| **1** | Record expenses **paid** | | *Dr Expense (E+)*<br>Cr Cash in hand / Cash at bank (A-) |
| **2** | Record expenses **incurred (closing entry** / transfer to income summary at end of financial year) | | Dr Income Summary (E+)<br>*Cr Expense (E-)* |
| **3** | **Adjustment** at the end of the financial year | Adjust for expenses payable | *Dr Expense (E+)*<br>Cr Expense payable (L+) |
| | | Adjust for prepaid expenses | Dr Prepaid expense (A+)<br>*Cr Expense (E-)* |

Expense account (E)

| 2021 | Particulars | Dr $<br>+ | Cr $<br>- | Bal $ |
|---|---|---|---|---|
| Jan 1 | Prepaid expense / Expense payable **(0)** | Prepaid | Payable | |
| Dec 31 | Cash in hand/ Cash at bank **(1)** | √ | | |
| Dec 31 | Income summary **(2)** | | √ | |
| Dec 31 | Expense payable / Prepaid expense **(3)** | Payable | Prepaid | 0 |

JYSS Ltd
Statement of Financial Performance for year ended 31 December 2021 (extract)

| | $ |
|---|---|
| Less: Other expenses | |
| _____ expense **(2)** | XX |

Same as the amount transferred to the **income summary** account

JYSS Ltd
Statement of Financial Position as at 31 December 2021 (extract)

| | $ |
|---|---|
| **Current assets** | |
| **Prepaid** _____ expense **(3)** | XX |
| | |
| **Current liabilities** | |
| ______ expense **payable (3)** | XX |

## Calculation of Expense Incurred

| Expense **incurred*** this year | = | Cash / cheque **paid** | – | ***Not** incurred this year*<br>Last year's expense **payable**<br>OR<br>This year's **prepaid** expense | + | ***Incurred** this year*<br>Last year's **prepaid** expense<br>OR<br>This year's expense **payable** |
|---|---|---|---|---|---|---|

*Expense incurred is the closing entry transferred to **income summary account**
Also reflected in the **statement of financial performance**

Incurred = – Payable (start) + Paid + Payable (end)

Incurred = + Prepaid (start) + Paid – Prepaid (end)

## Effects of Year-End Adjustment

| Prepaid expense | Effect on | | |
|---|---|---|---|
| | **Expense** | **Profit** | **Current Asset** |
| **If not** adjusted | Overstated | Understated | Understated |
| **After** adjustment | Decreased | Increased | Increased |

| Expense payable | Effect on | | |
|---|---|---|---|
| | **Expense** | **Profit** | **Current Liability** |
| **If not** adjusted | Understated | Overstated | Understated |
| **After** adjustment | Increased | Decreased | Increased |

## INCOME SUMMARY ACCOUNT

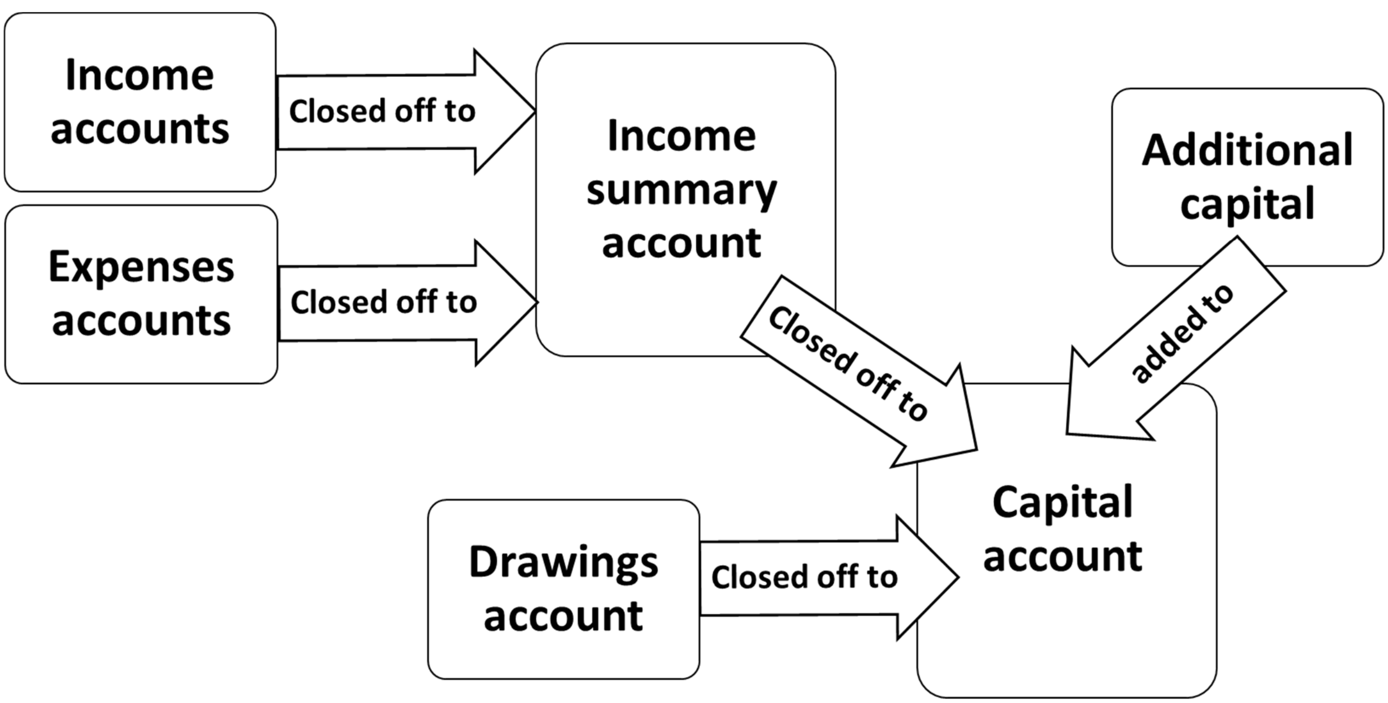
Income Summary Account

| 2025 | Particulars | Dr $ | Cr $ | Bal $ |
|---|---|---|---|---|
| Dec 31 | Sales revenue | | 93 400 | 93 400 Cr |
| | Sales returns | 3 400 | | 90 000 Cr |
| | Commission income | | 10 000 | 100 000 Cr |
| | Rent income | | 5 000 | 105 000 Cr |
| | Discount received | | 2 000 | 107 000 Cr |
| | Cost of sales | 30 000 | | 77 000 Cr |
| | Utilities expense | 1 000 | | 76 000 Cr |
| | Repairs and maintenance | 7 000 | | 69 000 Cr |
| | Insurance expense | 8 000 | | 61 000 Cr |
| | Advertising expense | 3 000 | | 58 000 Cr |
| | Capital | 58 000 | | 0 |

**Not** *required to prepare nor interpret this account.*

## CLOSING OF INCOME SUMMARY ACCOUNT

**<u>SOLE PROPRIETORSHIP</u>**



# CHAPTER 8 CASH

## DISHONOURED CHEQUE

Cheques can be dishonoured/ rejected/ labelled “refer to drawer” due to the following reasons:

- Cheque has **expired**. *(dated more than 6 months ago)*
- Cheque is **post-dated**. *(dated using a future date)*
- Inconsistent information on cheque e.g. signature on the cheque does not tally with the authorised signature recorded with the bank.
- Information on cheque is not complete e.g. no date.
- Payers’ bank account does not have enough money.

**Journal Entry**

Journal

| 2021 | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| Jun 5 | Cash at bank (A+) | 800 | |
| | Discount allowed (E+) | 10 | |
| | Trade receivable Leonard (A-) | | 810 |
| | *The business received $800 cheque from TR Leonard and gave Leonard a $10 cash discount* | | |

On 12 June, the bank informed the business that the $800 cheque received from Leonard on 5 June was ***dishonoured***, the business **reverses** the entries made on 5 June, as if the transaction on 5 June never did happen:

Journal

| 2021 | | Dr $ | Cr $ |
|---|---|---|---|
| Jun 12 | Trade receivable Leonard (A+) | 810 | |
| | Discount allowed (E-) | | 10 |
| | Cash at bank (A-) | | 800 |
| | *The bank informed the business that the $800 cheque received from Leonard on 5 June was dishonoured.* | | |

Note:
If cash discount was not given on 5 Jun, the reversal entry on 12 Jun due to the dishonoured cheque would also not adjust ‘discount allowed’.

## INTERNAL CONTROL

### Purpose

Internal controls are policies and procedures established to:

1. Safeguard assets of business
2. Ensure business transactions are recorded accurately
3. Comply with laws and regulations

### Internal Control over CASH

Cash in hand and cash at bank are highly susceptible to theft and fraud.

| **Types** | **Explanation** |
|---|---|
| 1) **S**egregation of duties | Separate cash handling and cash recording duties among different employees so that no one single person has control over the entire cash process. |
| 2) **C**ustody of cash | Secure cash and cheques in a locked storage and limit access of cash only to authorised employees. |
| 3) **A**uthorisation | Obtain proper approvals for all payments from authorised personnel**.** |
| 4) **B**ank reconciliation | Compare and identify items that caused the differences between the ending balances in the cash at bank account and bank statement. |

## CASH IN HAND & CASH AT BANK ACCOUNT

**Cash in hand account**

| 2021 | | Dr + $ | Cr - $ | Bal $ |
|---|---|---|---|---|
| Jan 1 | Bal b/d | | | 1000 Dr |
| 1 | Rent expense | | 402 | 598 Dr |
| 3 | Sales revenue | 250 | | 848 Dr |
| 5 | Advertising | | 100 | 748 Dr |
| 6 | Inventory | | 325 | 423 Dr |
| 12 | Cash at bank | | 200 | 223 Dr |
| 29 | Cash at bank | 800 | | 1023 Dr |
| Feb 1 | Bal b/d | | | 1023 Dr |

### Interpretation

- 1 Jan 2021: the business has $1000 **cash** balance from previous month.
- 1 Jan 2021: the business paid $402 **cash** for rent expense.
- 3 Jan 2021: the business received $250 **cash** for the sale of goods.
- 5 Jan 2021: the business paid $100 **cash** for advertising.
- 12 Jan 2021: the business deposited $200 office **cash** into the business bank.
- 29 Jan 2021: the business withdrew $800 **cash** from business bank account for office use.
- 1 Feb 2021: the business has $1023 **cash** balance brought down from Jan to Feb.

**Cash at bank account**

| 2021 | | Dr + $ | Cr - $ | Bal $ |
|---|---|---|---|---|
| Jan 1 | Bal b/d | | | 300 Dr |
| 12 | Cash in hand | 200 | | 500 Dr |
| 15 | Thomas | 400 | | 900 Dr |
| 22 | Joey | | 600 | 300 Dr |
| 28 | Drawings | | 900 | 600 Cr |
| 29 | Cash in hand | | 800 | 1400 Cr |
| Feb 1 | Bal b/d | | | 1400 Cr |

### Interpretation

- 1 Jan 2021: the business has $300 in the business **bank** account from previous month.
- 12 Jan 2021: the business deposited $200 office cash into the business **bank**.
- 15 Jan 2021: the business received $400 **cheque** from credit customer Thomas ~~after $50 discount.~~
- 22 Jan 2021: the business paid credit supplier Joey $600 **cheque** ~~after receiving $25 discount.~~
- 28 Jan 2021: the owner took $900 **cash at bank** for personal use.
- 29 Jan 2021: the business withdrew $800 cash from business **bank** account for office use.
- 1 Feb 2021: the business owed the bank $1400 **overdraft** and the balance was brought down from Jan to Feb.

## BANK RECONCILIATION

Business deposits money into the bank account


**Cash at bank account**

| | Dr($) | Cr($) | Bal($) |
|---|---|---|---|
| Sales revenue | 600 | | |

**Bank Statement**

### Recorded by the Business as Asset

**Debit is +**

### Recorded by the Bank as Liability

**Credit is +**

The bank has responsibility to safeguard the money and **owes** it to the business.

Both records ought to be identical but are different due to timing differences and errors. Hence, the accountant needs to reconcile the differences.

## BANK RECONCILIATION

Steps:

1. Put in +/- in cash at bank a/c and -/+ in bank statement.
2. Check opening balance and cancel the items that caused any differences.
   Adjust for errors in cash at bank and bank statement, if any.
3. Tick the common items and circle the differences.
4. Use the circled items in the bank statement to update the cash at bank a/c.
5. Use the circled items in the cash at bank a/c to prepare the bank reconciliation statement.

Cash at Bank account

| 2022 | | Dr ($) + | Cr ($) - | Balance ($) |
|---|---|---|---|---|
| Sep 30 | Balance b/d | | | **A** Dr or **A** Cr |
| | Nicholas | X | | |
| | Dividends | X | | |
| | Bank charges | | X | |
| | Interest expense | | X | |
| | Insurance | | X | |
| | | | | |
| Oct 1 | Balance b/d | | | **C** Dr or **C** Cr |

**DO NOT** write "dishonoured cheque" in the particulars! Write the ***name of TR*** who gave the cheque.

### JYSS Ltd
### Bank Reconciliation Statement as at 30 September 2022

| | | $ |
|---|---|---|
| Credit/(Debit) balance as per bank statement | Obtain this from last bal in bank statement | **B** or **(B)** |
| Add: Deposits in transit | | |
| Cash | These are the circled items in CAB Dr+ side | X |
| Jeremy | | X |
| Less: Cheques not yet presented | | |
| Kelly | These are the circled items in CAB Cr- side | X |
| Yao Hui | | X |
| Debit/(Credit) balance as per adjusted cash at bank a/c | | **C** or **(C)** |

**Should be the same**

- ❖ Credit balance in the cash at bank a/c means bank overdraft.
- ❖ Debit balance in the bank statement means bank overdraft.

Recall: Money deposited in the bank is the business' asset (debit in the cash at bank account prepared by the business) is a **LIABILITY** (credit in the bank statement prepared by the bank) to the bank.

**BANK RECONCILIATION**

**Purpose**

- It is prepared by the business to explain the differences, between the cash at bank account balance and the bank statement balance due to timing differences.
- To identify any errors in the cash at bank or the bank statement.
- To deter fraud

**** Items recorded in the cash at bank a/c but not in bank statement:**

**(i) Deposits in transit**

Business has deposited the cheque with the bank but the bank has not recorded the transaction.

**(ii) Cheques not yet presented**

Business has issued a cheque to its supplier but the supplier has not presented the cheque to the bank for payment yet.

**** Items not recorded in cash at bank a/c but recorded in bank statement:**

**(i) Direct deposits**

Money received by the bank on behalf of the company. E.g. credit transfer, bank interest income.

**(ii) Direct payments**

Instructions to the bank to make payments at a given date. E.g. standing order
Fees deducted directly by bank. E.g. bank charges (for bank services rendered), interest on bank loan.

**(iii) Dishonoured cheque**

Cheque refused to be processed by the bank.

*** Definitions not tested*

**Items that cause cash at bank balance <u>greater than</u> bank statement balance**

i. Deposits in transit *(amount already added to CAB but not BS)*
ii. Direct payments *(amount already deducted from BS but not CAB)*
iii. Dishonoured cheques *(amount already deducted from BS but not CAB)*

**Items that cause cash at bank balance <u>less than</u> bank statement balance**

i. Cheques not yet presented *(amount already deducted from CAB but not BS)*
ii. Direct deposits *(amount already added to BS but not CAB)*

**Effects of Adjusting the Differences on Cash at Bank and Profit for the year**

| Reconciling Item | Double Entry | Effects on | |
|---|---|---|---|
| | | Cash at Bank | Profit for the year |
| Direct payments | Dr Expenses<br>Cr Cash at bank | Decrease | Decrease |
| Dishonoured cheque | Dr Trade receivable<br>Cr Cash at bank | Decrease | No effect |
| Direct deposits (for income) | Dr Cash at bank<br>Cr Income | Increase | Increase |
| Direct deposits (from trade receivable) | Dr Cash at bank<br>Cr Trade receivable | Increase | No effect |

# CHAPTER 9 INVENTORY

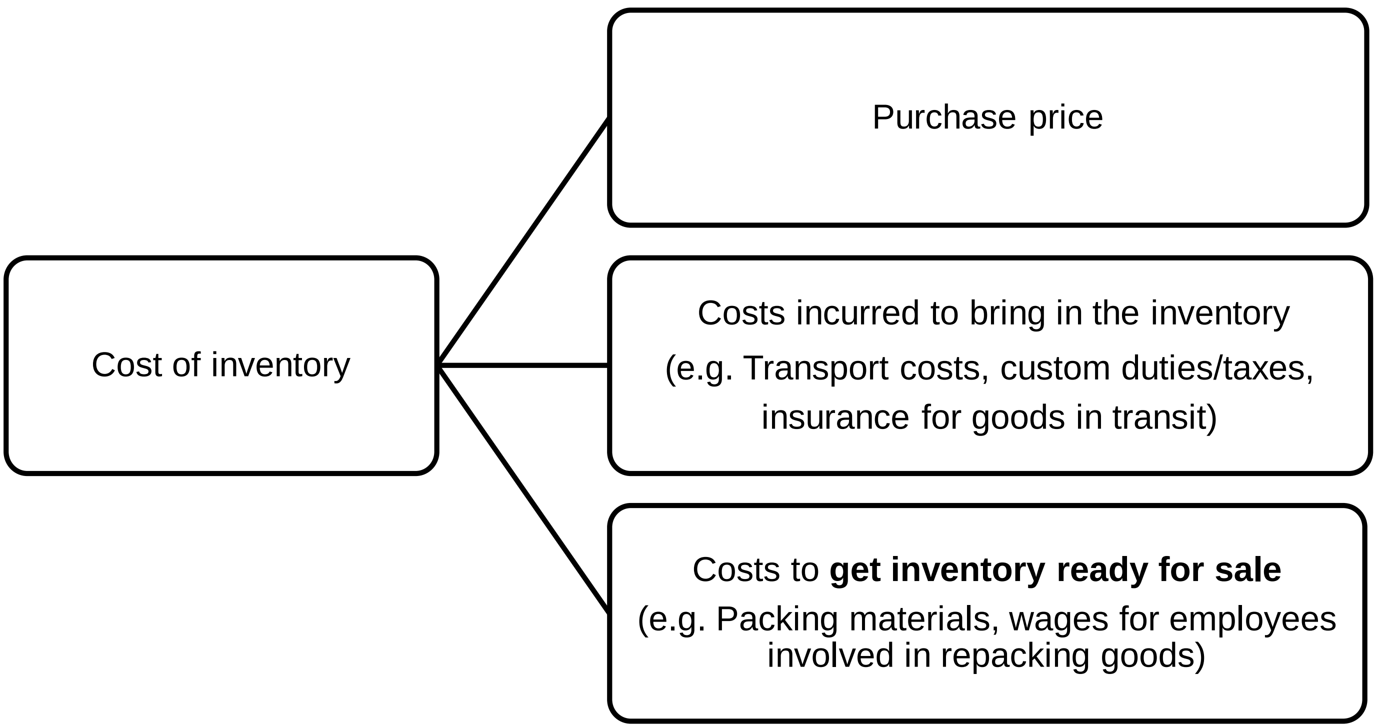
**Why businesses keep inventories**

- A business buys sufficient goods to keep on hand to prevent a stock-out situation, which often results in loss of sales.
- However, if the business buys too much goods, it will incur higher storage costs and increase the risk of the goods becoming obsolete.

**How businesses manage inventories**

- Keeping proper records to track inventory
- Keeping inventories both in the shops and warehouse to avoid stock-out situation
- Buying insurance to insure the inventory

**COST OF PURCHASES**

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**FIRST-IN-FIRST-OUT (FIFO)**

- FIFO method is used to calculate the cost of sales assuming that the goods purchased earliest are sold first. As such, the ending inventory is made up of goods purchased last.
- FIFO is only applicable to determining the cost of sales and returns from customers.
- FIFO does not apply to purchases returns.

**Journal Entry**

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Feb 2 | **Inventory** (A+) | 500 | |
| | Cash in hand/ Cash at bank (A-) | | 500 |
| | *Purchased goods worth $500 and paid cash/ cheque.* | | |
| | | | |
| Feb 3 | **Inventory** (A+) | 4 000 | |
| | Trade payable – Alvin (L+) | | 4 000 |
| | *Purchased goods worth $4000 on credit from supplier Alvin.* | | |
| | | | |
| Feb 9 | Trade payable – Alvin (L-) | 1 000 | |
| | **Inventory** (A-) | | 1 000 |
| | *Returned goods worth $1000 to credit supplier Alvin.* | | |
| | | | |
| Feb 10 | Trade receivable/ Cash in hand/ Cash at bank (A+) | 7 000 | |
| | Sales revenue (I+) | | 7 000 |
| | Cost of sales (E+) | 3 000 | |
| | **Inventory** (A-) | | 3 000 |
| | *Sold goods for $7000 on credit / received cash / cheque.*<br>*The cost of goods sold was $3000.* | | |
| | | | |
| Feb 15 | Trade receivable/ Cash in hand/ Cash at bank (A+) | 900 | |
| | Sales revenue (I+) | | 900 |
| | Cost of sales (E+) | 500 | |
| | **Inventory** (A-) | | 500 |
| | *Sold goods for $900 on credit / received cash / cheque.*<br>*The cost of goods sold was $500.* | | |
| | | | |
| Feb 21 | Sales returns (I-) | 120 | |
| | Trade receivable/ Cash in hand/ Cash at bank (A-) | | 120 |
| | **Inventory** (A+) | 70 | |
| | Cost of sales (E-) | | 70 |
| | *Customer returned goods previously sold at $120.*<br>*The cost of sales was $70.* | | |
| | | | |
| Feb 22 | Drawings (D+) | 2 000 | |
| | **Inventory** (A-) | | 2 000 |
| | *The owner took goods costing $2 000 for his own use.* | | |

Inventory account (asset)

| 2021 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Feb 1 | Balance b/d | | | 3 000 Dr |
| 2 | Cash in hand/ Cash at bank | 500 | | |
| 3 | Trade payable – Alvin | 4 000 | | |
| 9 | Trade payable – Alvin | | 1 000 | |
| 10 | **Cost of sales** | | 3 000 | FIFO |
| 15 | **Cost of sales** | | 500 | |
| 21 | **Cost of sales** | 70 | | |
| 22 | Drawings | | 2 000 | 1 070 Dr |
| | | | | |
| Mar 1 | Bal b/d | | | 1 070 Dr |
| | | | | |

**Interpretation**

- 1 Feb 2021: the business had goods costing $3000 brought over from the previous month.
- 2 Feb 2021: the business purchased goods and paid $500 by cash/ cheque.
- 3 Feb 2021: the business purchased goods worth $4000 on credit from Alvin.
- 9 Feb 2021: the business returned goods costing $1000 previously bought on credit from Alvin / to credit supplier Alvin
- 10 Feb 2021: the business sold goods **costing** $3000.
- 15 Feb 2021: the business sold goods **costing** $500.
- 21 Feb 2021: Customers returned goods **costing** $70.
- 22 Feb 2021: Owner withdrew goods worth $2000 for his personal use.
- 1 Mar 2021: the business had goods costing $1070 brought down from Feb to Mar.

**Extracts of Financial Statements**

JYSS Ltd
Statement of Financial Position as at 28 February 2021 (extract)

| | $ | |
|---|---|---|
| <u>**Current assets**</u> | | |
| Inventory | 1 070 | |

Cost of sales account (expense)

| 2021 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Feb10 | **Inventory** *(sold goods)* | 3 000 | | 3 000 Dr |
| 15 | **Inventory** *(sold goods)* | 500 | | |
| 21 | **Inventory** *(goods returned by customers)* | | 70 | 3 430 Dr |
| 28 | Income summary | | 3 430 | 0 |

**Interpretation**

- 10 Feb 2021: the business sold goods **costing** $3000.
- 15 Feb 2021: the business sold goods **costing** $500.
- 21 Feb 2021: Customers returned goods **costing** $70.
- 28 Feb 2021: $3430 cost of sales was **incurred** during the year and transferred to the income summary account.

**Extracts of Financial Statements**

JYSS Ltd

Statement of Financial Performance for the month ended 28 February 2021 (extract)

| | $ | $ |
|---|---|---|
| Sales revenue (7 000 + 900) | 7 900 | |
| Less: Sales returns | 120 | |
| Net sales revenue | | 7 780 |
| Less: Cost of sales | | 3 430 |
| Gross profit | | 4 350 |

## IMPAIRMENT LOSS ON INVENTORY

**Inventory Valuation Method / Rule**
Inventory is valued at the lower of cost and net realisable value.

**Net Realisable Value**
The net realisable value (NRV) is the potential amount receivable from selling goods. Businesses aim to sell its goods at a NRV higher than its cost.

*NRV = Estimated selling price – additional cost to sell the inventory (e.g. repair costs, repackaging costs, refurbishment costs, marketing costs)*

**Impairment Loss on Inventory**
Usually, inventory is recorded at cost. However, when the NRV is lower than its cost, the value of inventory is to be written down (reduced) to its NRV.

Impairment loss on inventory is the difference between the higher cost of inventory and the lower NRV. It is recorded as an expense, and is debit in nature.
*Impairment loss on inventory = Cost – NRV*

**Causes of Impairment Loss on Inventory**
- Goods damaged by fire or flood
- Goods stolen
- Goods outdated

**Application of Accounting Theory**

1. **Prudence theory**
   Inventory is valued at the lower of cost and net realisable value so that profits and assets are not overstated.

   When the NRV falls below the cost of inventory, the business should record the potential loss as impairment loss on inventory so as not to overstate its assets and profits.

## IMPAIRMENT LOSS ON INVENTORY

### Journal Entry

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Nov 10 | Impairment loss on inventory (E+) | 2 000 | |
| | **Inventory** (A-) | | 2 000 |
| | *Due to goods damaged in a flood, the cost of inventory $3 500 was written down to its net realisable value $1 500.* | | |
| | | | |
| Nov 30 | Insurance claim receivable (A+) | 800 | |
| | Impairment loss on inventory (E-) | | 800 |
| | *Insurance company confirmed that the business is able to claim $800 of compensation which will be paid out after the financial year.* | | |

Inventory account (asset)

| 2021 | Particulars | Dr $<br>+ | Cr $<br>- | Bal $ |
|---|---|---|---|---|
| Nov 1 | Balance b/d | | | 3 500 Dr |
| 10 | Impairment loss on inventory | | 2 000 | 1 500 Dr |
| Dec 1 | Balance b/d | | | 1 500 Dr |

### Interpretation

- 1 Nov 2021: the business had $3 500 worth of inventory carried down from previous month.
- 10 Nov 2021: the cost of the inventory was written down **by** $2 000, **from** $3500 to $1500.

✋ Impairment loss on inventory account (expense)

| 2021 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Nov 10 | Inventory | 2 000 | | 2 000 Dr |
| 30 | Insurance claim receivable | | 800 | 1 200 Dr |
| 30 | Income summary | | 1 200 | 0 |

**Interpretation**

- ❖ 10 Nov 2021: The cost of the inventory was written down by $2 000 to its net realisable value.
- ❖ 30 Nov 2021: The insurance claim would compensate $800 of the impairment loss on inventory.
- ❖ 30 Nov 2021: $1 200 of impairment loss on inventory was incurred during the year and transferred to the income summary account.

**Extracts of Financial Statements**

JYSS Ltd

Statement of Financial Performance for year ended 30 November 2021 (extract)

| | $ |
|---|---|
| Less: Other expenses | |
| Impairment loss on inventory | 1 200 |

JYSS Ltd

Statement of Financial Position as at 30 November 2021 (extract)

| | $ |
|---|---|
| Current assets | |
| Inventory | 1 500 |
| Insurance claim receivable | 800 |

# CHAPTER 10 TRADE RECEIVABLES (TR)

Refers to the amounts owed by customers who buy goods or enjoy services from the business on credit. It is a current asset, and is debit in nature.

**Journal Entry**

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Jan 2 | **Trade receivable Hazim** (A+) | 950 | |
| | Sales revenue (I+) | | 950 |
| | Cost of sales (E+) | 200 | |
| | Inventory (A-) | | 200 |
| | *Sold goods on credit to Hazim for $950. The cost of goods sold was $200.* | | |
| | | | |
| Jan 9 | Sales returns (I-) | 76 | |
| | **Trade receivable Hazim** (A-) | | 76 |
| | Inventory (A+) | 30 | |
| | Cost of sales (E-) | | 30 |
| | *Credit customer Hazim returned goods previously sold at $76. The cost of goods sold was $30.* | | |
| | | | |
| Jan 11 | **Trade receivable Hazim** (A+) | 100 | |
| | Sales revenue (I+) | | 100 |
| | Cost of sales (E+) | 40 | |
| | Inventory (A-) | | 40 |
| | *Sold goods on credit to Hazim for $950. The cost of goods sold was $200.* | | |
| | | | |
| Jan 15 | Cash in hand / cash at bank (A+) | 882 | |
| | Discount allowed (E+) | 18 | |
| | **Trade receivable Hazim** (A-) | | 900 |
| | *Cash/cheque payment from credit customer Hazim to settle $900 owing, after 2% cash discount was given.* | | |
| | | | |
| Jan 18 | **Trade receivable Hazim** (A+) | 900 | |
| | Cash in hand / cash at bank (A-) | | 882 |
| | Discount allowed (E-) | | 18 |
| | *The bank informed that the cheque received on 15 Jan was dishonoured.* | | |

## Trade Receivable Ledger account

For TR acc, particulars should not be inventory when the biz is selling goods

Hazim **owes** business **more**

Hazim **owes** business **less**

(Asset)
Trade receivable Hazim account

| 2021 | Particulars | Dr $ + | Cr $ - | Bal $ | Source document |
|---|---|---|---|---|---|
| Jan 1 | Balance b/d | | | 900 Dr | |
| 2 | **Sales revenue** (95%x1000) | 950 | | | Invoice |
| 9 | **Sales returns** (95%x80) | | 76 | | Credit note |
| 11 | **Sales revenue** | 100 | | | Debit note |
| 15 | Cash in hand / cash at bank (98%x900) | | 882 | | Receipt |
| 15 | Discount allowed (2%x900) | | 18 | | Receipt |
| 18 | Cash at bank | 882 | | | Bank statement |
| 18 | Discount **allowed** | 18 | | 1 874 Dr | |
| Feb 1 | Balance b/d | | | 1 874 Dr | |

Cash sales is **NOT** recorded in TR account because the double entry is:
Dr Cash at bank / Cash in hand (A+), Cr Sales revenue (I+)

| Date | **Interpretation** | Remarks |
|---|---|---|
| Jan 1 | $900 owed by credit customer Hazim was brought over from the previous month. | |
| Jan 2 | The business sold goods on credit to Hazim for $950. | *E.g. List price $1000 less 5% trade discount, 95% owed by Hazim is recorded*<br>*5% trade discount is not recorded.* |
| Jan 9 | Credit customer Hazim returned goods previously sold at $76. | *E.g.* ***List price $80*** *returned*<br>*Sales returns = 95% x $80 = $76*<br>*5% trade discount given earlier also apply to the returns of the same batch of goods.*<br>*E.g.* ***Net price $76.*** *Net price is after discount.* |
| Jan 11 | The credit sales to Hazim made on 2 Jan was undercharged. | *Double entry for invoice and debit note is the same.* |
| Jan 15 | The business received cash/cheque of $882 from credit customer Hazim to settle $900 owing, after $18 cash discount was given. | *'Settle' means the business no longer owes supplier $900 → 98% paid ($882) and the 2% cash discount ($18).*<br>*2% cash discount must be recorded.* |
| Jan 18 | The cheque of $882 received on 15 Jan was dishonoured and the cash discount of $18 was withdrawn. | *The entries recorded on 15 Jan are reversed.* |
| Feb 1 | $1 874 owed by credit customer Hazim was brought down from Jan to Feb. | |

Refer to Chapter 2 for source documents and Chapter 4 for discounts.

## ALLOWANCE FOR IMPAIRMENT OF TRADE RECEIVABLES

**Trade Receivables (TR)**
Refers to the amounts owed by customers who buy goods or enjoy services from the business on credit. It is a current asset, and is debit in nature.

**Allowance for Impairment of Trade Receivables**
Refers to the amount of debt owed by trade receivables that is estimated likely to be uncollectible. It is a contra-asset, and is credit in nature.

*Allowance = Estimated % x Ending TR balance*

**Impairment Loss on Trade Receivables**
It is the difference between the allowance at the beginning and end of the year. It is the change (increase or decrease) in allowance. It is an expense account, and is debit in nature.

**Trade Receivable Valuation Method**
Trade receivables is valued at net trade receivables, which is total trade receivables less allowance for impairment of trade receivables, in the statement of financial position.

**Application of Accounting Theory**

1. **Prudence theory**
   The allowance for impairment of trade receivables is reported in the statement of financial position as a deduction against the trade receivables book value so that assets are not overstated.

2. **Matching theory**
   As the increase in allowance for impairment of trade receivables is a likely expense, it should be recorded in the same accounting year as the sales revenue earned to obtain a true and fair profit for the year.

## IMPAIRMENT LOSS ON TRADE RECEIVABLES

| Given info | 31 Dec 2019 ($) | | 31 Dec 2020 ($) | | 31 Dec 2021 ($) |
|---|---|---|---|---|---|
| TR | 4000 | Impairment Loss - 40 | 3200 | Impairment Loss + 130 | 5800 |
| Allowance at 5% of TR | 200 | ↔ | 160 | ↔ | 290 |
| Net TR | 3800 | | 3040 | | 5510 |

**Impairment loss on TR = Ending AFIOTR – Beginning AFIOTR + Write off**

### Journal Entry

Journal

| Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| 2019 | | | |
| Dec 31 | Impairment loss on trade receivables (E+) | 200 | |
| | Allowance for impairment of trade recievables (A-) | | 200 |
| | *The estimated uncollectible debt **increased** from $0 to $200.* | | |
| | (200-0) | | |
| 2020 | | | |
| Dec 31 | Allowance for impairment of trade recievables (A+) | 40 | |
| | Impairment loss on trade receivables (E-) | | 40 |
| | *The estimated uncollectible debt **decreased** by $40.* | | |
| | (160-200) | | |
| 2021 | | | |
| Dec 31 | Impairment loss on trade receivables (E+) | 130 | |
| | Allowance for impairment of trade recievables (A-) | | 130 |
| | *The estimated uncollectible debt **increased** by $130.* | | |
| | (290-160) | | |

✋ AFIOTR account (contra-asset)

| 2019 | Particulars | Dr $<br>- | Cr $<br>+ | Bal $ |
|---|---|---|---|---|
| Dec 31 | Impairment loss on trade receivables | | 200 | 200 Cr |
| 2020 | | | | |
| Jan 1 | Bal b/d | | | 200 Cr |
| Dec 31 | Impairment loss on trade receivables | 40 | | 160 Cr |
| 2021 | | | | |
| Jan 1 | Bal b/d | | | 160 Cr |
| Dec 31 | Impairment loss on trade receivables | | 130 | 290 Cr |
| 2022 | | | | |
| Jan 1 | Bal b/d | | | 290 Cr |

**Interpretation**

- ❖ 2019 Dec 31: The business reviewed its trade receivables and increased its estimated uncollectible debts by and to $200.
- ❖ 2020 Jan 1: The estimated uncollectible debts owed by credit customers totalled $200.
- ❖ 2020 Dec 31: The business reviewed its trade receivables and decreased its estimated uncollectible debts by $40, from $200 to $160.
- ❖ 2021 Jan 1: The estimated uncollectible debts of trade receivables amounted to $160.
- ❖ 2021 Dec 31: The business reviewed its trade receivables and increased its estimated uncollectible debts by $130, from $160 to $290.
- ❖ 2022 Jan 1: The esstimated uncollectible debts owed by customers was $290.

☝ Impairment loss on trade receivables account (expense)

| 2019 | Particulars | Dr $<br>+ | Cr $<br>- | Bal $ |
|---|---|---|---|---|
| Dec 31 | AFIOTR | 200 | | 200 Dr |
| Dec 31 | Income summary | | 200 | 0 |
| 2020 | | | | |
| Dec 31 | AFIOTR | | 40 | 40 Cr |
| Dec 31 | Income summary | 40 | | 0 |
| 2021 | | | | |
| Dec 31 | AFIOTR | 130 | | 130 Dr |
| Dec 31 | Income summary | | 130 | 0 |

**Interpretation**

- 2019 Dec 31: The business reviewed its trade receivables and increased the estimated uncollectible debts by $200.
  The $200 impairment loss on trade receivables was transferred to income summary account as an expense.

- 2020 Dec 31: The business reviewed its trade receivables and decreased the estimated uncollectible debts by $40.
  The $40 impairment loss on trade receivables was transferred to income summary account as a reversal of expense.

- 2021 Dec 31: The business reviewed its trade receivables and increased the estimated uncollectible debts by $130.
  The $130 impairment loss on trade receivables was transferred to income summary account as an expense.

## Extracts of Financial Statements

JYSS Ltd
Statement of Financial **Performance** for year ended 31 December **2019** (extract)

| | $ |
|---|---|
| Less: Other expenses | |
| **Impairment loss** on trade receivables | 200 |

JYSS Ltd
Statement of Financial **Performance** for year ended 31 December **2020** (extract)

| | $ |
|---|---|
| Less: Other expenses | |
| **Reversal of impairment loss** on trade receivables | (40) |

*Decrease in AFIOTR*

JYSS Ltd
Statement of Financial **Performance** for year ended 31 December **2021** (extract)

| | $ |
|---|---|
| Less: Other expenses | |
| **Impairment loss** on trade receivables | 130 |

## Extracts of Financial Statements

JYSS Ltd
Statement of Financial **Position** as at 31 December **2019** (extract)

| | $ | $ |
|---|---|---|
| **Current assets** | | |
| Trade receivables | 4 000 | |
| Less: **Allowance** for impairment of trade receivables | 200 | 3 800 |

JYSS Ltd
Statement of Financial **Position** as at 31 December **2020** (extract)

| | $ | $ |
|---|---|---|
| **Current assets** | | |
| Trade receivables | 3 200 | |
| Less: **Allowance** for impairment of trade receivables | 160 | 3 040 |

JYSS Ltd
Statement of Financial **Position** as at 31 December **2021** (extract)

| | $ | $ |
|---|---|---|
| **Current assets** | | |
| Trade receivables | 5 800 | |
| Less: **Allowance** for impairment of trade receivables | 290 | 5 510 |

Likely to be uncollectible

**NET TR** = Amount that the business is confident of collecting

**WRITING OFF DEBT**

When it is certain/confirmed that the debts are uncollectible, the business should write-off the debt owed by the specific customer.

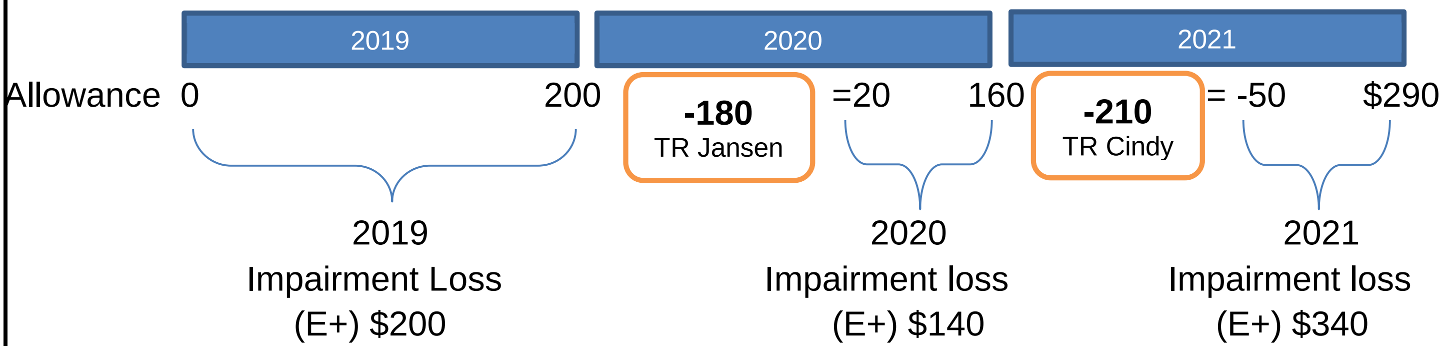
**Journal Entry**

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2020 | | | |
| Mar 20 | Allowance for impairment of trade recievables | 180 | |
| | Trade receivable Jansen (A-) | | 180 |
| | *Trade receivable Jansen declared bankrupt and the $180 debt* | | |
| | *he owed was written off.* | | |
| | | | |
| 2021 | | | |
| Sep 15 | Cash in hand (A+) [30% x 300] | 90 | |
| | Allowance for impairment of trade recievables [70% x 300] | 210 | |
| | Trade receivable Cindy (A-) | | 300 |
| | *Credit customer Cindy paid 30% of her $300 debt by cash $210* | | |
| | *and the remaining $90 owing was written off as irrecoverable.* | | |
| | | | |

## Writing Off of Irrecoverable Debt

| | 31 Dec 2019 ($) | 31 Dec 2020 ($) | 31 Dec 2021 ($) |
|---|---|---|---|
| TR | 4000 | 3200 | 5800 |
| Allowance at 5% of TR | 200 | 160 | 290 |
| Net TR | 3800 | 3040 | 5510 |




**Impairment loss on TR = Ending AFIOTR – Beginning AFIOTR + Write off**

AFIOTR account (contra-asset)

| 2019 | Particulars | Dr $<br>- | Cr $<br>+ | Bal $ |
|---|---|---|---|---|
| Dec 31 | Impairment loss on trade receivables | | 200 | 200 Cr |
| 2020 | | | | |
| Jan 1 | Bal b/d | | | 200 Cr |
| **Mar 20** | **Trade receivable Jansen** | **180** | | 20 Cr |
| Dec 31 | Impairment loss on trade receivables<br>(160 – 200 + 180) | | **140** | 160 Cr |
| 2021 | | | | |
| Jan 1 | Bal b/d | | | 160 Cr |
| **Sep 15** | **Trade receivable Cindy** | **210** | | 50 Dr |
| Dec 31 | Impairment loss on trade receivables<br>(290 – 160 + 210) | | **340** | 290 Cr |
| 2022 | | | | |
| Jan 1 | Bal b/d | | | 290 Cr |

**Interpretation**

- ❖ 2020 Mar 20: The business wrote off $180 worth of debts owed by Jansen.
- ❖ 2020 Dec 31: The estimated uncollectible debts increased by $140 to $160 after a review of its trade receivables.
- ❖ 2021 Sep 15: Trade receivable Cindy's debt of $210 was written off.
- ❖ 2021 Dec 31: The estimated uncollectible debts increased by $340 to $290 after a review of its trade receivables.

# CHAPTER 11 NON-CURRENT ASSETS (NCA)

## CAPITAL & REVENUE EXPENDITURE

| | Capital Expenditure | Revenue Expenditure |
|---|---|---|
| Definition | • Includes **costs of purchasing** the NCA,<br>• costs to **bring** the NCA **to its intended use**, and<br>∗ costs to **enhance** the NCA | ∗ Includes costs to **operate** the NCA, and<br>∗ to **repair and maintain** the NCA in **working condition** |
| Impact on financial statements | ∗ All related capital expenditures are added and presented as a **non-current asset** in the statement of financial **position**<br>∗ as the **benefits** of capital expenditures usually **last for more than 1 year** | ∗ Revenue expenditures are presented as individual **expenses** in the statement of financial **performance**<br>∗ as the **benefits** of revenue expenditures are usually **used within 1 year** |
| Examples | Purchase cost of the NCA,<br>Extension to premises,<br>Installation fees of air conditioner,<br>Freight / delivery / shipping charges,<br>Import duties, legal fees etc. | Petrol for vehicle,<br>Machine oil for equipment,<br>Utility bills for air conditioner,<br>Repairs of machinery,<br>Servicing of engine parts etc. |

### Journal Entry

Journal

| Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| 2022 | | | |
| Dec 5 | NCA (A+) | 10 500 | |
| | Trade payable (L+) / Cash at bank (A-) / Cash in hand (A-) | | 10 500 |
| | *Recording capital expenditures for the purchase of NCA on credit / paid by cheque / by cash.* | | |
| | | | |
| Dec 5 | Expense (E+) | 750 | |
| | Expense payable (L+) / Cash at bank (A-) / Cash in hand (A-) | | 750 |
| | *Recording revenue expenditures as expensed incurred but not yet paid / paid by cheque / by cash.* | | |

**Effects of wrong classification of Capital Expenditure (NCA) and Revenue Expenditure (Expense)**

| Error | Effect on Other Expenses | Effect on Profit | Effect on Non-current Assets |
|---|---|---|---|
| Capital expenditure (NCA) wrongly classified as revenue expenditure (Expense) | Overstated | Understated | Understated |
| Revenue expenditure (Expense) wrongly classified as capital expenditure (NCA) | Understated | Overstated | Overstated |

**Application of Accounting Theory**

1. **Materiality theory**

   If the amount spent on a NCA is insignificant to decision making, it does not need to be reported as an NCA even though the benefits last for more than one accounting year.

   It could be classified as revenue expenditure and reported as an expense in the statement of financial performance.

Motor vehicles account (at **cost**)

| 2020 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Jan 1 | Bal b/d | | | 6 000 Dr |
| Apr 16 | Cash at bank | 1 500 | | |
| May 20 | Trade payable Thom | 4 000 | | 11 500 Dr |
| | | | | |
| 2021 | | | | |
| Jan 1 | Bal b/d | | | 11 500 Dr |

**Interpretation**

- 2020 Jan 1: The business had existing motor vehicles <u>costing</u> $6 000 balance brought down from previous month.
- 2020 Apr 16: The business bought motor vehicles <u>costing</u> $1 500 by cheque.
- 2020 May 20: The business bought motor vehicles <u>costing</u> $4 000 from Thom on credit.
- 2021 Jan 1: The business had motor vehicles <u>costing</u> $11 500 brought down to 1 Jan 2021. .

## DEPRECIATION

### Depreciation

Depreciation is the allocation of cost of NCA over its estimated useful life.
It is an expense, and is debit in nature.

### Accumulated Depreciation

Accumulated depreciation refers to the total depreciation to-date.
It is a contra-asset account, and is credit in nature.

### Non-current Assets Valuation Method

Non-current assets are presented at net book value, which is cost less accumulated depreciation in the statement of financial position.
*Net book value = Cost – Accumulated depreciation*

### Causes of Depreciation

- Wear and tear (e.g. motor vehicle)
- Obsolescence / Out-dated (e.g. computers)
- Usage (e.g. coal from coal mines)
- Legal limits (e.g. 60 year leasehold shop)

Depreciation is not provided for **land** because land is a limited resource and it is not subjected to wear and tear.

Depreciation is not provided for **inventory** because inventory is bought for resale purpose and not meant for long term use.

## DEPRECIATION METHODS

| | Straight Line Method | Reducing-balance Method |
|---|---|---|
| Also known as | % on **Cost** | % on **Net Book Value**<br>(NBV = Cost – Acc Dep) |
| Formula | *Depreciation expense*<br><br>*= % Rate x (Cost – **Scrap value***)*<br><br>*OR*<br><br>$= \dfrac{Cost - Scrap\ value*}{Useful\ life(in\ years)}$<br><br>* Scrap / Residual value refers to the remaining amount that the business is able to receive at the end of its useful life | *Depreciation expense*<br><br>*= % Rate x NBV*<br>*= % Rate x (Cost – **Acc Dep**)* |
| Effect on Expenses | **Equal** amount of **depreciation** is recorded every financial period, hence its name "straight line" | **Higher depreciation** expense is recorded in the **earlier years** and **reduces** as time goes by, hence its name "reducing-balance". |
| Effect on Profit | Profit decreases by the **same** amount every year | Profit decreases by a **higher** amount in **earlier** years |
| Effect on Net Book Value | NBV decreases by an **equal** amount ever year | NBV decreases by a **higher** amount in **earlier** years |
| Suitability | Suited for NCA that is expected to **earn income evenly** over its useful life | Suited for NCA that is expected to **earn more income** in its **earlier** years **than** in its **later** years. |

**Application of Accounting Theory**

Why should a business depreciate its NCA?

1. **Matching theory**
   Depreciation expense, which is a portion of the cost of the NCA, should be matched against the income earned from using the NCA in the same year to obtain a true and fair profit for the year.

2. **Prudence theory**
   Non-current assets should be valued at their net book value, which is cost less accumulated depreciation, so that profits and assets are not overstated.

Why should the same accounting methods be used?

1. **Consistency theory**
   The depreciation method and rate of depreciation used by the business must be consistent from period to period so that its financial performance can be meaningfully compared across financial periods.

## ACCOUNTING FOR DEPRECIATION

| | |
|---|---|
| Method | Straight line |
| Cost of equipment | $1 000 |
| % Rate | 10% |
| Depreciation Expense | $100 every year |

**Journal Entry**

Journal

| Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| 2020 | | | |
| Jun 30 | Depreciation (E+) | 100 | |
| (year-end) | Accumulated depreciation (A-) | | 100 |
| | *Depreciation charged for the year was $100.* | | |
| | | | |
| Jun 30 | Income summary | 100 | |
| (year-end) | Depreciation (E-) | | 100 |
| Closing entry | *Depreciation expense for the year was transferred to the income summary account.* | | |
| | | | |

Depreciation of equipment account (expense)

| 2020 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Jun 30 | Accumulated depreciation | 100 | | 100 Dr |
| 30 | Income summary | | 100 | 0 |
| 2021 | | | | |
| Jun 30 | Accumulated depreciation | 100 | | 100 Dr |
| 30 | Income summary | | 100 | 0 |

**Interpretation**

30 Jun 2020 and 30 Jun 2021:
Depreciation charged on equipment for the year was $100 and the depreciation expense incurred was transferred to the income summary account.

☟ Accumulated depreciation of equipment account (contra-asset)

| 2020 | Particulars | Dr $ - | Cr $ + | Bal $ |
|---|---|---|---|---|
| Jun 30 | Depreciation | | 100 | 100 Cr |
| | | | | |
| Jul 1 | Bal b/d | | | 100 Cr |
| 2021 | | | | |
| Jun 30 | Depreciation | | 100 | 200 Cr |
| | | | | |
| Jul 1 | Bal b/d | | | 200 Cr |

**Interpretation**

- 30 Jun 2020: Accumulated depreciation of equipment increased by and to $100.
- 1 Jul 2020: The accumulated depreciation was $100.
- 30 June 2021: Accumulated depreciation of equipment increased by $100 to $200.
- 1 Jul 2021: The accumulated depreciation was $200.

**Extracts of Financial Statements**

JYSS Ltd

Statement of Financial Performance for year ended 30 June 2021 (extract)

| | $ |
|---|---|
| **Less: Other expenses** | |
| **Depreciation** of equipment | 100 |

JYSS Ltd

Statement of Financial Position as at 30 June 2021 (extract)

| | $ | $ | $ |
|---|---|---|---|
| **Non-current assets** | **Cost** | **Accumulated depreciation** | **Net book value** |
| Equipment | 1 000 | 200 | 800 |

# CHAPTER 12 TRADE PAYABLES

Refers to the amounts owing to suppliers whom the business bought on credit from. It is a current liability, and is credit in nature.

**Journal entry**

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Jan 6 | Inventory (A+) | 4 500 | |
| | **Trade payable Eugene** (L+) | | 4 500 |
| | *The business <u>bought</u> goods on credit from supplier Eugene.* | | |
| | | | |
| Jan 12 | **Trade payable Eugene** (L-) | 270 | |
| | Inventory (A-) | | 270 |
| | *The business <u>returned</u> goods to credit supplier Eugene.* | | |
| | | | |
| Jan 29 | **Trade payable Eugene** (L-) | 6 000 | |
| | Cash in hand / cash at bank | | 5 880 |
| | Discount received | | 120 |
| | *The business <u>paid</u> credit supplier Eugene cash/cheque to settle $6000 owing after $120 cash discount received.* | | |
| | | | |
| Jan 31 | Inventory (A+) | 100 | |
| | **Trade payable Eugene** (L+) | | 100 |
| | *Credit purchases made on 6 Jan was <u>undercharged</u>.* | | |

## **Trade Payable Ledger account** (with discounts & source documents)

For TP acc, particulars cannot be: Sales revenue, sales returns or cost of sales
Because the biz is not selling but buying goods

Business **owes** supplier Eugene **less**

Business **owes** supplier Eugene **more**

(Liability)
Trade payable Eugene account

| 2021 | Particulars | Dr $ – | Cr $ + | Bal $ | Source document |
|---|---|---|---|---|---|
| Jan 1 | Balance b/d | | | 7 500 Cr | |
| 6 | **Inventory** (90%x5000) | | 4 500 | | Invoice |
| 12 | **Inventory** (90%x300) | 270 | | | Credit note |
| 29 | Cash in hand / cash at bank (98%x6000) | 5 880 | | | Payment voucher |
| 29 | Discount **received** (2%x6000) | 120 | | | - |
| 31 | **Inventory** | | 100 | 5 830 Cr | Debit note |
| Feb 1 | Balance b/d | | | 5 830 Cr | |

Cash purchases is **NOT** recorded in TP account because the double entry is:
Dr Inventory (A+), Cr Cash at bank / Cash in hand (A-)

| Date | **Interpretation** | Remarks |
|---|---|---|
| Jan 1 | $7 500 was owed to credit supplier Eugene was brought over from the previous month. | |
| Jan 6 | The business bought goods worth $4 500 on credit from supplier Eugene. | *E.g. List price $5000 less 10% trade discount, only the 90% owed to Eugene is recorded. 10% trade discount is not recorded.* |
| Jan 12 | The business returned goods worth $270 to credit supplier Eugene. | *E.g. List price $300 returned 10% trade discount given earlie also apply to the returns of the same batch of goods. E.g. Net price $270, Net price is after discount.* |
| Jan 29 | The business paid credit supplier Eugene cash/cheque $5880 (98%) to settle $6000 owing after cash discount of $120 (2%) was received. | *'Settle' means the business no longer owes supplier $6000 → The 98% paid ($5880) and the 2% cash discount ($120). Cash discount must be recorded.* |
| Jan 31 | The credit purchases from Eugene made on 6 Jan was undercharged. | *Double entry for invoice and debit note is the same.* |
| Feb 1 | $5 830 owed to credit supplier Eugene was brought down from Jan to Feb. | |

Refer to Chapter 2 for source documents and Chapter 4 for discounts.

# CHAPTER 13 LONG-TERM BORROWINGS

## BANK LOAN VS BANK OVERDRAFT

| | Bank loan | Bank overdraft |
|---|---|---|
| Amount of borrowing | Amount borrowed is fixed. | Amount borrowed is not fixed but it must not exceed the limit agreed with the bank. |
| Transference of cash | Cash is transferred to the business. | No cash is transferred to the business. Business withdrew more than what is deposited in its bank account. |
| Repayment | Usually regular fixed cash repayments to reduce the amount borrowed.<br><br>Sometimes the business is allowed to pay off entire amount only at the end of loan period. | No cash repayment. Any deposit into the bank account reduces the amount borrowed. |
| Double entry recording | Loan from bank account is credited | Reflected as a credit balance of the cash at bank account |
| Classification in statement of financial position | Shown as long term borrowing under non-current liabilities. | Shown as bank overdraft under current liabilities. |

## ACCOUNTING FOR LOAN

The business took a 5 year loan of $10 000 from the bank on 1 Jan 2020.
The partial principal sum repayment is to be made on 31 December every year.

**Journal entry**

Journal

| Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| 2020 | | | |
| Jan 1 | Cash at bank (A+) | 10 000 | |
| | **Loan from bank** (L+) | | 10 000 |
| | *The business obtained loan from bank.* | | |
| | | | |
| Dec 31 | **Loan from bank** (L-) | 2 000 | |
| | Cash at bank (A-) | | 2 000 |
| | *The business repaid bank loan.* | | |

Bank loan account

| 2020 | Particulars | Dr $ – | Cr $ + | Bal $ |
|---|---|---|---|---|
| Jan 1 | Cash at bank | | 10 000 | 10 000 Cr |
| Dec 31 | Cash at bank | 2 000 | | 8 000 Cr |
| 2021 | | | | |
| Jan 1 | Bal b/d | | | 8 000 Cr |

**Interpretation**

- 1 Jan 2020: The business borrowed bank loan of $10 000.
- 31 Dec 2020: The business repaid $2 000 of the bank loan by bank transfer.
- 1 Jan 2021: The amount of loan owing to the bank $8 000 was brought down to 1 Jan 2021.

**Extracts of Financial Statements**

JYSS Ltd

Statement of Financial Position as at 31 December 2020 (extract)

| | $ |
|---|---|
| Non-current liabilities | |
| Long-term borrowings (3/5 x 10 000) | 6 000 |
| | |
| Current liabilities | |
| **Current portion** of long-term borrowings (1/5 x 10 000) | 2 000 |

Note:

On 31 Dec 2020, a total of $8 000 loan was outstanding. However, $2 000 is due for repayment next year, hence it is the current portion of LTB, a CL. The remaining $6 000 loan owed will be due for repayment years later, hence NCL.

## ACCOUNTING FOR INTEREST EXPENSE *(O LEVEL ONLY)*

| |
|---|
| Interest expense incurred = Interest **rate** (%) x **Principal** sum borrowed<br><br>** To be pro-rated by the **number of months** when necessary* |

### Application of Accounting Theory

1. **Matching theory**
   Interest expense incurred must be matched against the income earned from using the loan to operate business in the same accounting year to determine the profit for the year.

2. **Accrual basis of accounting**
   Interest expense must be recognised in the financial period once incurred, regardless of whether or not it has been paid.

### Journal entry (*Similar to expenses journal entries in Chapter 7)

| | | |
|---|---|---|
| **1** | Adjust for interest expenses payable (**Reversal**) | Dr Interest expense payable (L-)<br>Cr Interest expense (E-) |
| **2** | Record interest expense **paid** | Dr Interest expense (E+)<br>Cr Cash at bank (A-) |
| **3** | Record interest expenses **incurred** (transfer to income summary at end of financial year) | Dr Income Summary (E+)<br>Cr Interest expense (E-) |
| **4** | **Adjust** for interest expenses payable (current year) | Dr Interest expense (E+)<br>Cr Interest expense payable (L+) |

✋ Interest expense account

| 2020 | Particulars | Dr $ + | Cr $ – | Bal $ |
|---|---|---|---|---|
| Jan 1 | Interest expense payable | | 4 500 | 4 500 Cr |
| Mar 31 | Cash at bank | 6 000 | | 1 500 Dr |
| Dec 31 | Interest expense payable | 4 200 | | 5 700 Dr |
| 31 | Income summary | | 5 700 | 0 |

**Interpretation**

- 1 Jan 2020: The business reversed the adjustment made for $4 500 interest expense owed in the previous financial year.
- 31 Mar 2020: The business paid $6 000 interest expense by cheque.
- 31 Dec 2020: The business owed $4 200 of interest expense as at year end.
- 31 Dec 2020: The business incurred $5 700 of interest expense for the year and transferred to the income summary account.

**Extracts of Financial Statements**

JYSS Ltd

Statement of Financial Performance for year ended 31 December 2020 (extract)

| | $ |
|---|---|
| Less: Other expenses | |
| **Interest expense** | 5 700 |

JYSS Ltd

Statement of Financial Position as at 31 December 2020 (extract)

| | $ |
|---|---|
| **Current liabilities** | |
| Interest expense **payable** | 4 200 |

# CHAPTER 14 EQUITIES

## FEATURES OF SOLE PROPRIETORSHIP

| Features | Sole Proprietorship (SP) |
|---|---|
| Ownership | **One owner** who contributes capital to set up the SP. |
| Access to funds | Less likely for lenders to lend money to the SP due to the **lack of personal assets that can serve as collaterals.**<br><br>Funds is usually limited to the owner's personal funds. |
| Extent of liability | Owner is **personally liable** to pay all debts and losses incurred by the business. |
| Level of control | Owner has **full control** over it but he may hire professionals to help him. |
| Lifespan of business | Exists as long as the owner is alive and desires to continue operation. |
| Transferability of ownership | Owner can transfer or sell the business by notifying the corporate regulatory authority. |
| Formalities and procedures | Minimal administrative duties to adhere to. |

**OWNER'S EQUITY**

**Application of Accounting Theory**

**Accounting entity theory**

- The activities of the business are separate from the actions of the owner. All transactions are recorded from the point of view of the business.

- Resources contributed by the owner for business use are recorded as capital.

- Withdrawal of business assets for personal use are recorded as drawings.

**DRAWINGS**

Drawings is the amount of resources withdrawn by the business owner for his personal use. It is a contra-equity account, and is debit in nature.

At the **end of the financial year**, the **total** drawings are transferred to the capital account to reduce it.

**Journal entry**

Journal

| Date | Particulars | Dr $ | Cr $ |
|---|---|---|---|
| 2021 | | | |
| Feb 3 | Drawings | 3 000 | |
| | Cash at bank (A-) | | 3 000 |
| | *The owner took $3000 from the business bank for* | | |
| | *personal use.* | | |
| | | | |
| Jun 20 | Drawings | 250 | |
| | Inventory (A-) | | 250 |
| | *The owner took $250 worth of goods for his own use.* | | |
| | | | |
| Oct 24 | Drawings | 700 | |
| | Cash in hand (A-) | | 700 |
| | *The owner took $700 from the office cash for his* | | |
| | *private use.* | | |
| | | | |
| Dec 31 | Capital | 3 950 | |
| (year-end) | Drawings | | 3 950 |
| Closing entry | ***Total** drawings for the year are transferred to the* | | |
| | *capital account.* | | |

Drawings account

| 2021 | Particulars | Dr $ + | Cr $ - | Bal $ |
|---|---|---|---|---|
| Feb 3 | Cash at bank | 3 000 | | 3 000 Dr |
| Jun 20 | Inventory | 250 | | |
| Oct 24 | Cash in hand | 700 | | 3 950 Dr |
| Dec 31 | Capital | | 3 950 | 0 |

**Interpretation**

- 3 Feb: The owner took cash from business bank account $3 000 for his own use.
- 20 Jun: The owner took inventory costing $250 from business for personal use.
- 24 Oct: The owner took business/office cash $700 for his own use.
- 31 Dec: The total drawings of $3 950 for the year was transferred to the capital account.

**CAPITAL**

Capital is the amount of resources/ net assets contributed by the business owner. It is an equity account, and is credit in nature.

*Capital or net assets = Total Assets – Total Liabilities*

**Journal entry**

Journal

| Date | Particulars | Dr<br>$ | Cr<br>$ |
|---|---|---|---|
| 2021 | | | |
| Mar 15 | Equipment (A+) | 5 000 | |
| | Capital (+) | | 5 000 |
| | *Owner contributed a personal equipment worth $3000.* | | |
| | | | |
| Dec 31 | Capital (-) | 3 950 | |
| (year-end) | Drawings (-) | | 3 950 |
| | *Total drawings for the year are transferred to the* | | |
| | *capital account.* | | |
| | | | |
| Dec 31 | Income summary | 1 050 | |
| (year-end) | Capital (+) | | 1 050 |
| | *The business made a profit of $1 050 for the year ended 31 Dec 2021 which is transferred from income summary account to the capital account* | | |

Capital Account

| 2021 | Particulars | Dr $<br>- | Cr $<br>+ | Bal $ |
|---|---|---|---|---|
| Jan 1 | Balance b/d | | | 10 000 Cr |
| Mar 15 | Equipment | | 5 000 | |
| Dec 31 | Drawings | 3 950 | | |
| Dec 31 | Income Summary | [Loss] | 1 050<br>[Profit] | 12 100 Cr |
| 2022 | | | | |
| Jan 1 | Balance b/d | | | 12 100 Cr |

**Interpretation**

- ❖ 1 Jan 2021: The capital brought down from previous year was $10 000.
- ❖ 15 Mar 2021: Owner brought his own equipment costing $5 000 into the business.
- ❖ 31 Dec 2021: Total of $3 950 drawings for the year was transferred to the capital account.
- ❖ 31 Dec 2021: $1 050 profit for the year was transferred from income summary account to the capital account.
- ❖ 1 Jan 2022: The capital brought down to the following year was $12 100.

**Extracts of Financial Statements**

JYSS Ltd

Statement of Financial Position as at 31 December 2020 (extract)

| | $ |
|---|---|
| <u>Owner's equity</u> | |
| Capital (10 000 + 5 000 + 1 050 – 3 950) | 12 100 |

<u>Note:</u>

Capital = Beginning capital + additional capital + Profit for the year – Drawings

**Effect on Owner's Equity**

| Business activities | Effect on Owner's Equity |
|---|---|
| Owner contributes assets to the business i.e. additional capital. | Increase |
| Owner withdraws business assets for personal use i.e. drawings. | Decrease |
| Profit for the year | Increase |
| Loss for the year | Decrease |

# CHAPTER 15 CORRECTIONS OF ERRORS

**Limitation of Trial Balance**

There are errors in the accounts if the trial balance is not balanced.
However, there are some errors which will not affect the agreement of the trial balance totals. Such errors are not revealed by the trial balance.

**Errors Not Revealed by Trial Balance**

1) The transaction is not recorded at all.

2) The wrong amount is recorded on both the debit and credit entries.

3) The transaction is recorded in the wrong account of a different accounting element.

4) The transaction is recorded in the wrong account of the same accounting element.

5) The debit and credit entries are reversed.

## Error in Amount

***When the recorded amount is <u>understated</u>:***
A $2000✓ cheque received from a trade receivable has been recorded as $200✗.

| | |
|---|---|
| ✗ Wrong entry<br>*(as described in question)* | Dr Cash at bank 200<br>Cr Trade receivable 200 |
| **Correction of Error**<br>*[This is the Answer!]* | **Dr Cash at bank 1800**<br>**Cr Trade receivable 1800** |
| ✓ Correct entry<br>*(by right should have been like that)* | Dr Cash at bank 2000<br>Cr Trade receivable 2000 |

*Amount for **Dr** Cash at bank was **too low**, to **increase** it by $1800 → **Dr** Cash at bank $1800*
*Amount for **Cr** Trade receivable was **too low**, to **increase** it by $1800 → **Cr** Trade receivable $1800*

∴ *<u>**Top up**</u> the Dr & Cr entries by the difference when the wrong amount is **too low**.*

---

***When the recorded amount is <u>overstated</u>:***
Credit purchase of goods worth $340✓ has been recorded as $430✗.

| | |
|---|---|
| ✗ Wrong entry<br>*(as described in question)* | Dr Inventory 430<br>Cr Trade payable 430 |
| **Correction of Error**<br>*[This is the Answer!]* | **Dr Trade payable 90**<br>**Cr Inventory 90** |
| ✓ Correct entry<br>*(by right should have been like that)* | Dr Inventory 340<br>Cr Trade payable 340 |

*Amount for **Dr** Inventory was **too high**, to **reduce** it by $90 → **Cr** Inventory $90*
*Amount for **Cr** Trade payable was **too high**, to **reduce** it by $90 → **Dr** Trade payable $90*

∴ *<u>**Reverse**</u> the Dr & Cr entries by the difference when the wrong amount is **too high**.*

**Wrong Account of a <u>Different</u> Accounting Element**

Purchase of equipment ✓ worth $400 has been recorded as repairs✗ of equipment.

| | |
|---|---|
| ✗ Wrong entry<br>*(as described in question)* | Dr Repairs expense 400 ✗<br>*Cr CAB / CIH / TP 400 ✓ |
| **Correction of Error**<br>*[This is the Answer!]* | **Dr Equipment 400**<br>**Cr Repairs expense 400** |
| ✓ Correct entry<br>*(by right should have been like that)* | Dr Equipment 400<br>*Cr CAB / CIH / TP 400 ✓ |

** The credit entry is not described in the question as there is no error and does not require correction.*
***<u>Remove</u>*** *the wrong* ***Dr*** *Repairs by correcting it with* ***Cr*** *Repairs.*
*Then,* ***<u>create</u>*** *the correct entry* ***Dr*** *Equipment.*

---

**Wrong Account of the <u>Same</u> Accounting Element**

Credit sale of goods worth $500 to Lucy ✓ has been posted to Luca's✗ account.

| | |
|---|---|
| ✗ Wrong entry<br>*(as described in question)* | Dr TR Luca 500 ✗<br>*Cr Sales revenue 500 ✓ |
| **Correction of Error**<br>*[This is the Answer!]* | **Dr TR Lucy 500**<br>**Cr TR Luca 500** |
| ✓ Correct entry<br>*(by right should have been like that)* | Dr TR Lucy 500<br>*Cr Sales revenue 500 ✓ |

** The credit entry is not wrong and does not require correction.*
***<u>Remove</u>*** *the wrong* ***Dr*** *TR Luca by correcting it with* ***Cr*** *TR Luca.*
*Then,* ***<u>create</u>*** *the correct entry* ***Dr*** *TR Lucy.*

**Reversal of entries**

Cheques of $600 received from Betty ✓ has been debited to Betty's ✗ account and credited to cash at bank.

| | | |
|---|---|---|
| ✗ Wrong entry<br>*(as described in question)* | Dr TR Betty 600<br>Cr Cash at bank 600 | |
| **Correction of Error**<br>*[This is the Answer!]* | | **Dr Cash at bank 1200**<br>**Cr TR Betty 1200** |
| ✓ Correct entry<br>*(by right should have been like that)* | Dr Cash at bank 600<br>Cr TR Betty 600 | |

***Dr*** *TR Betty $600 was wrong. To* ***remove*** *it →* ***Cr*** *TR Betty $600*
*To create the correct entry →* ***Cr*** *TR Betty $600 again.*

***Cr*** *Cash at bank $600 was wrong. To* ***remove*** *it →* ***Dr*** *Cash at bank $600*
*To create the correct entry →* ***Dr*** *Cash at bank $600 again.*

∴ *To correct the error of complete reversal, do the correct entry with the amount* ***doubled***.

## EFFECTS ON PROFIT

| Correction Item | Effect of **Error** on | | Effect of **Correction** on | |
|---|---|---|---|---|
| | Gross Profit | Profit for the year | Gross Profit | Profit for the year |
| **<u>Debit</u>**:<br>• Sales revenue<br>• Sales returns<br>• Cost of sales | Overstated | | **<u>Decrease</u>** | |
| **Credit**:<br>• Sales revenue<br>• Sales returns<br>• Cost of sales | Understated | | **Increase** | |
| **<u>Debit:</u>**<br>• Other income<br>• Other expense | No effect | Overstated | No effect | **<u>Decrease</u>** |
| **Credit:**<br>• Other income<br>• Other expense | No effect | Understated | No effect | **Increase** |

*Profit is **Cr** in nature.*
*∴ When any income / expenses is **credited** to correct an error, the profit **increases**, and vice versa.*

# CHAPTER 17 SCENARIO-BASED

## ACCOUNTING AND NON-ACCOUNTING INFORMATION

**Accounting information** refers to information usually generated by the accounting information system and is largely information that can be extracted from journals, ledger accounts and financial statements (including financial ratios).

**Non-accounting information** refers to information not found in journals, ledger accounts and financial statements.

**Why owners and managers of a business are interested in non-accounting information**

Making decisions with only accounting information may cause stakeholders to leave out important business-related factors that are not shown on financial statements but may affect decisions.

## SOURCES OF ACCOUNTING AND NON-ACCOUNTING INFORMATION

| Decision | | Accounting information | Non-accounting information |
|---|---|---|---|
| 1 | Which **inventory** to buy to sell as goods | 1) Cost of goods<br>2) Storage cost | 1) Nature of product<br>2) Storage requirements<br>3) Consumer preference<br>4) Reputation / review of product |
| 2 | Which **supplier** to buy goods or NCA from | 1) Cost of inventory / NCA<br>2) Trade discount and<br>3) Delivery charges<br>4) Cost of services (installation and maintenance)<br>5) Credit terms and cash discount | 1) Online or brick-and-mortar supplier<br>2) Local or overseas seller<br>3) After-sales service<br>4) Return policy<br>5) Reputation of supplier<br>6) Warranty |
| 3 | Whether to **extend credit** to customer | 1) Trade receivables balance<br>2) Credit terms and cash discount<br>3) Number of days trade receivables are overdue<br>4) Existing customer's history of repayment | 1) Economic outlook of the country<br>2) Specific industry outlook<br>3) Reputation of customer<br>4) New customer's history of repayment |

**Scenario Based Question (SBQ)**

**Structure:** *7 marks (3 reasons)*

| Para | | Marks | |
|---|---|---|---|
| 1 | Decision | 1m | State your **decision** clearly by answering the question. |
| 2 | Reason 1 | 2m | **Evidence:**<br>Quote evidence to support.<br>Make comparison wherever applicable.<br>✓ *Comparison: cheaper, faster, more efficient…*<br>✓ *Eg. A costs $40 which is cheaper than B which costs $60.*<br><br>**Benefit:**<br>Explain one possible benefit. |
| 3 | Reason 2 | 2m | *Avoid repeating the same benefit.* |

- Organise your answer into **3** paragraphs.
- Write in full sentences, not in point form.
- Be succinct. One good sentence scores 1 mark.
- Make a decision. Choose either option A or option B. Do **not** write for both.
- If you choose A, compare and explain why A is good / better. Do **not** explain why you did not choose B or why B is not good / worse.
- No need conclusion as the mark for decision has already been given.

**DECISION: WHICH INVENTORY TO BUY TO SELL AS GOODS?**

*Note: You are the accountant, advising which product the business should buy for its inventory* ***to sell*** *to its customers.*

**Accounting information**

| | Source of information | Explanation of benefit |
|---|---|---|
| 1 | **Cost of goods**<br><br>*Includes:*<br>*- delivery charges*<br>*- import tax*<br>*- any other cost of inventory*<br><br>*Consider net cost after trade discount.* | 1) **Higher gross profit:**<br>Lower inventory cost reduces cost of sales and increases gross profit, assuming the selling price remains unchanged.<br><br>2) **Competitive pricing:**<br>Lower inventory costs let the business offer more competitive prices, helping attract more customers and boost sales. |
| 2 | **Storage cost** | 1) **Higher profit:**<br>Lower storage cost reduces expenses leading to higher profit for the year. |

*DECISION: WHICH INVENTORY TO BUY TO SELL AS GOODS?*

**Non-accounting information**

| | Source of information | Explanation of benefit |
|---|---|---|
| 1 | **Nature of product** | 1) **Durability:**<br>Durable goods indicate good quality and help improve the business's reputation.<br><br>2) **Shelf life:**<br>Goods with longer shelf life allows more time for the business to sell them before they expire. This lowers the risk of writing off expired goods.<br><br>3) **Eco-friendliness:**<br>Eco-friendly goods appeal to customers and improve the business's image as a responsible company that cares about the environment and sustainability. |
| 2 | **Storage requirements** | 1) **Space-saving:**<br>Goods that take up less space allow the business to stock more, reducing the risk of stock-outs and lost sales.<br><br>2) **Specific storage needs:**<br>Goods less affected by storage conditions are less likely to spoil, lowering the risk of impairment loss on inventory to write off spoilt goods. |
| 3 | **Consumer preference** | 1) **Popular designs:**<br>Offering products with a wider range of colours and designs attracts a broader customer base and increases sales. |
| 4 | **Reputation / Reviews of product** | 1) **Brand reputation:**<br>Goods from reputable brands help build customer trust and loyalty, leading to more consistent sales.<br><br>2) **Good reviews:**<br>Goods with positive reviews offers a higher level of quality assurance , reducing returns and improving brand image. |

## DECISION: WHICH SUPPLIER TO BUY GOODS / NCA FROM?

### Accounting information

| | Source of information | Explanation of benefit |
|---|---|---|
| 1 | **Cost**<br><br>*Includes:*<br>*- delivery charges*<br>*- import tax*<br>*- any other cost of purchases*<br><br>*Consider net cost after trade discount.* | 1) **Higher gross profit:**<br>Lower inventory cost reduces cost of sales and increases gross profit, assuming the selling price remains unchanged.<br><br>2) **Competitive pricing:**<br>Lower inventory costs let the business offer more competitive prices, helping attract more customers and boost sales.<br><br>3) **Improved cash flow:**<br>A lower cost of inventory / non-current asset (NCA) would lead to cash savings and improved cash flow for other operating needs of the business. |
| 2 | **Credit period**<br><br>*No. of days supplier allows the business to owe* | 1) **Better cash flow**<br>A longer credit period means the business has more time to pay, helping it manage its cash flow better. |
| 3 | **Cash discount**<br><br>*Consider the cash needed after deduction of cash discount.*<br><br>*→ cash discount is received upon repayment within the credit period.* | 1) **Cash savings**<br>If the business pays early within a specific period, it can enjoy cash discounts. This leads to cash savings and reduces cash outflow. |

*DECISION: WHICH SUPPLIER TO BUY GOODS / NCA FROM?*

**Non-accounting information**

| | Source of information | Explanation of benefit |
|---|---|---|
| 1 | **Online or brick-and-mortar supplier** | 1) **Brick-and-mortar supplier:** Suppliers with physical shops enable businesses to physically chedck the goods before buying. This helps make sure the goods meet quality expectations.<br><br>2) **Online supplier:** The business can easily browse and compare goods anytime online. It can also read reviews before deciding what to buy.<br>3) |
| 2 | **Local or overseas supplier** | **Advantages of local seller:**<br>1) Local suppliers can deliver goods more quickly, helping the business avoid stock-out and losing sales.<br><br>2) If goods are damaged, local suppliers make it easier and cheaper to return or repair them because they are nearby. |
| 3 | **After-sales service**<br><br>*Includes free installation, prompt response to enquiries, repair services etc.* | **Reliable after-sale services:**<br>1) Suppliers who offer after-sales services such as installation and maintenance enable the business to focus on its main operations.<br><br>2) Suppliers that provide reliable after-sales service help build a strong relationship with the business. This means the business can get faster help and better support when problems happen, which reduces downtime and keeps operations running smoothly. |

*DECISION: WHICH SUPPLIER TO BUY GOODS / NCA FROM?*

**Non-accounting information**

| | Source of information | Explanation of benefit |
|---|---|---|
| 4 | **Return policy** | 1) **Quality assurance:**<br>A longer or more flexible return policy gives the business confidence that the goods meet quality standards. If the goods don’t meet expectations, they can be returned easily, reducing the risk of losses. |
| 5 | **Reputation of supplier** | 1) **Postive reviews:**<br>Positive customer reviews show that the supplier is known for providing good quality goods and services. This gives the business confidence when choosing the supplier.<br><br>2) **Established brand:**<br>Suppliers who have been in the industry for many years are seen as more established and trustworthy. This helps the business feel assured that the goods will be of consistent good quality. |
| 6 | **Warranty** *(For NCA)* | 1) **Cost saving:**<br>A longer warranty gives the business confidence that the product is durable. It also helps avoid extra costs for repairs or replacements over time.<br><br>2) **Minimise downtime due to breakdown:**<br>A longer warranty protects the business from delays caused by equipment breakdowns. This helps the business continue running smoothly. |

## DECISION: CREDIT WORTHINESS OF CUSTOMER

*Which customer to grant credit to?*
*Whether to extend credit period to customer?*

### Accounting information

| | Source of information | Explanation of benefit |
|---|---|---|
| 1 | **Trade receivables balance** | 1) **Higher TR balance:**<br>A customer with a higher trade receivables balance could be bringing in more sales. Granting credit extension can help improve customer relation and grow the business.<br><br>2) **Lower TR balance:**<br>A customer with a lower trade receivables balance is less likely to default on payment. This means lower credit risk, which can help the business get bank loan approval more easily. |
| 2 | **Credit terms /**<br><br>**Number of days TR are overdue**<br><br>**Existing customer's history of repayment** | **1) Credit Terms & Payment History**<br>A customer who pays on time is more reliable. Giving credit to the customer helps the business collect payment quickly and manage its cash flow better. |

*DECISION: CREDIT WORTHINESS OF CUSTOMER*

**Non-accounting information**

| | Source of information | Explanation of benefit |
|---|---|---|
| 1 | **Economic outlook of the country** | When the country is in recession, people spend less, so businesses have less cash and may struggle to repay debts..<br><br>When the country is in economic boom, businesses earn more sales revenue and are better able to repay debts. |
| 2 | **Specific industry outlook** | A business in a new or growing industry has uncertain market demand but offers new business opportunities.<br><br>A business in a mature industry is stable but faces fierce competition. |
| 3 | **Reputation of customer** | A customer with better reputation is likely to generate more sales and profit, so they can repay debts more easily. |
| 4 | **New customer's history of repayment** | The new customer with better track record of making prompt payments to its existing suppliers would provide greater assurance of its ability to repay debts on time. |

# NOTES ON FINANCIAL STATEMENTS WITH BALANCE DAY ADJUSTMENTS

<table>
<tr><th colspan="2">Type of Adjustments</th><th>Effects on<br>Statement (Performance)</th><th>Effects on<br>Statement (Position)</th></tr>
<tr><td>1)</td><td><u>Additional capital</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Capital 50 000<br>Cash at bank 8 300<br>Motor vehicle 40 000<br><br>Profit for the year is $1 000.<br><br>(i) Owner contributed additional capital of $1 200, which was banked into business bank account.<br><br>(ii) Owner brought in a motor vehicle valued at $15 000 for business use.</td><td>No effect</td><td><u>Non-current assets</u><br>Motor vehicle<br>(40 000+15 000) 55 000<br><br><u>Current assets</u><br>Cash at bank<br>(8 300+1 200) 9 500<br><br><u>Owner's equity</u><br>Capital 67 200<br>(50 000+1 200+15 000+1 000)</td></tr>
<tr><td>2)</td><td><u>Drawings</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Drawings 7 000<br>Cash at bank (overdrawn) 1 500<br>Inventory 6 000<br>Capital 20 000<br><br>Profit for the year is $3 000.<br><br>(i) Owner withdrew $800 from business bank for personal use.<br><br>(ii) Owner withdrew $1 200 goods for personal use.</td><td>No effect</td><td><u>Current assets</u><br>Inventory<br>(6 000 – 1 200) 4 800<br><br><u>Owner's equity</u><br>Capital 14 000<br>[20 000 + 3 000 –<br>(7 000 + 800 +1 200)]<br><br><u>Current liability</u><br>Bank overdraft<br>(1500 + 800) 2 300</td></tr>
</table>

<table>
<tr><th colspan="2">Type of Adjustments</th><th>Effects on<br>Statement (Performance)</th><th>Effects on<br>Statement (Position)</th></tr>
<tr><td>3)</td><td><u>Prepaid expenses</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Stationery (Paid) 400<br>Advertising (Paid) 3 000<br>Rent (Paid) 4 200<br><br>(i) Stationery worth $100 was prepaid.<br><br>(ii) Advertising incurred per month is $200 / The annual advertising expense is $2 400.<br><br>(iii) Included in the rent was an amount of $600 paid for 6 months contract ending 28 Feb 2021.</td><td>Expenses recorded in Performance is the amount incurred.<br><br><u>Less: Other expenses</u><br>Stationery<br>(400 – 100) 300<br><br>Advertising<br>(3 000 – 600*) 2 400<br><br>Rent<br>(4 200 – 200**) 4 000<br><br>Incurred = Paid – Prepaid</td><td><u>Current assets</u><br>Prepaid stationery 100<br>Prepaid advertising 600<br>Prepaid rent 200<br><br>*3 months of advertising is prepaid<br>= $3 000 – ($200 X12) = $600<br><br>**2 months (Jan & Feb 2021) of rental is prepaid<br>= $600 X 2/6<br>= $200</td></tr>
<tr><td>4)</td><td><u>Expenses payable</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Advertising (Paid) 3 100<br>Rent expense (Paid) 18 000<br>Insurance (Paid) 5 000<br><br>(i) Outstanding advertising of $80. / $80 of advertising was owing.<br><br>(ii) The annual rent was $19 200. / The monthly rent was $1 600.<br><br>(iii) Insurance was paid for 10 months to 31 Oct 2020. Insurance for Nov and Dec was owing.</td><td>Expenses recorded in Performance is the amount incurred.<br><br><u>Less: Other expenses</u><br>Advertising<br>(3100 + 80) 3 180<br><br>Rent expense<br>(1 600 x 12) 19 200<br><br>Insurance<br>(5 000 / 10 x 12) 6 000<br><br>Incurred = Paid + Payable</td><td><u>Current liabilities</u><br>Advertising payable 80<br>Rent payable<br>(19 200 – 18 000) 1 200<br>Insurance payable 1 000<br>(5 000 /10 X 2)</td></tr>
</table>

<table>
<tr><th colspan="2">Type of Adjustments</th><th>Effects on<br>Statement (Performance)</th><th>Effects on<br>Statement (Position)</th></tr>
<tr><td>5)</td><td><u>Income received in advance</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Rent income (Received) 750<br>Service fee revenue (Received) 700<br>Commission income (Received) 6 000<br><br>(i) Rent received included an advance payment of $250 for the month of January 2021. / Rent income received in advance was $250.<br><br>(ii) Service fee revenue is earned at $50 per month. / The service fee revenue earned for the year was $600.<br><br>(iii) Commission income includes payment of $1 200 for the half year to 31 March 2021.</td><td>Income recorded in Performance is the amount earned.<br><br>Service fee revenue 600<br><br><u>Other income</u><br>Rent income<br>(750 – 250) 500<br><br>Commission income<br>(6 000 – 600*) 5 400<br><br>Earned = Received - RIA</td><td><u>Current liabilities</u><br>Rent income received in advance 250<br><br>Service fee received in advance 100<br><br>Commission income received in advance 600<br><br>*3 months (Jan to Mar 2021) of commission was received in advance<br>= $1 200 X 3/6<br>= $600</td></tr>
<tr><td>6)</td><td><u>Income receivable</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Interest income (Received) 850<br>Commission income (Received) 900<br>Rent received (Received) 1 000<br><br>(i) Interest income $120 was yet to be received.<br><br>(ii) The annual commission income was $1 200. / The monthly commission earned was $100.<br><br>(iii) Rent income is earned at $200 per month. / The rent income earned for the year was $2 400.</td><td>Income recorded in Performance is the amount earned.<br><br><u>Other income</u><br>Interest income<br>(850+120) 970<br><br>Commission income<br>(100 x 12) 1 200<br><br>Rent income<br>(200 X 12) 2 400<br><br>Earned =<br>Received + Receivable</td><td><u>Current assets</u><br>Interest income receivable 120<br><br>Commission income receivable<br>(1 200 – 900) 300<br><br>Rent income receivable<br>(2 400 – 1 000) 1 400</td></tr>
</table>

<table>
<tr><th colspan="2">Type of Adjustments</th><th>Effects on<br>Statement (Performance)</th><th>Effects on<br>Statement (Position)</th></tr>
<tr><td>7)</td><td><u>Current & Non-current portion of Long Term Borrowing</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Bank loan 4 000<br><br>(i) One quarter of the bank loan is to be repaid by 30 June 2021.</td><td>No effect</td><td><u>Non-current liabilities</u><br>Long-term borrowing 3 000<br>(4 000 x 3/4)<br><br><u>Current liabilities</u><br>Current portion of<br>long-term borrowing 1 000<br>(4 000 X 1/4)</td></tr>
<tr><td>8)</td><td><u>Interest on loan (O Level only)</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>5% Long-term loan 20 000<br><br>(i) Interest on long term loan has not been paid.<br><br>(ii) The loan was obtained on 1 Oct 2020.</td><td><u>Less: Other expenses</u><br>Interest on loan 250<br><br>Interest from 1 Oct to 31 Dec 2020 = (5% X 20 000 X 3/12) = $250</td><td><u>Non-current liabilities</u><br>Long term borrowing 20 000<br><br><u>Current liabilities</u><br>Interest payable 250</td></tr>
<tr><td>9)</td><td><u>Interest on loan (O Level only)</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>10% Mortgage loan 8 000<br>Interest on mortgage loan (Paid) 150<br><br>(i) Interest on mortgage loan is not fully paid up. The loan was obtained on 1 July 2020.</td><td><u>Less: Other expenses</u><br>Interest on mortgage loan 400<br><br>Interest from 1 Jul to 31 Dec 2020 = (10% x 8 000 x 6/12) = $400</td><td><u>Non-current liabilities</u><br>Long-term borrowing 8 000<br><br><u>Current liabilities</u><br>Interest payable 250<br>(400 – 150)</td></tr>
<tr><td>10)</td><td><u>Current & Non-current portion of Loan & Interest on loan (O Level only)</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Loan 5 000<br>Interest on loan (paid) 300<br><br>(i) Interest on loan is 8% per annum.<br><br>(ii) One-tenth of the loan is repayable on 31 August 2021.</td><td><u>Less: Other expenses</u><br>Interest on loan 400<br>(8% X 5 000)</td><td><u>Non-current liabilities</u><br>Long-term borrowing<br>(5 000 – 500) 4 500<br><br><u>Current liabilities</u><br>Interest payable 100<br>(400 – 300)<br><br>Current portion of<br>long-term borrowing 500<br>(5 000 x 1/10)</td></tr>
</table>

| | Type of Adjustments | Effects on Statement (Performance) | Effects on Statement (Position) |
|---|---|---|---|
| 11) | **<u>Interest income (O Level only)</u>**<br><br>Trial balance as at 31 Dec 2020:<br>$<br>5% Bank deposit 20 000<br><br>(i) The bank deposits commenced on 30 June 2020. | <u>Other income</u><br>Interest income 500<br><br>Interest income from 30 June 2020 to 31 Dec 2020<br>= (5% X 20 000 X 6/12)<br>= $500 | <u>Current assets</u><br>5% Bank deposit 20 000<br><br>Interest income receivable 500 |
| 12) | **<u>Interest income (O Level only)</u>**<br><br>Trial balance as at 31 Dec 2020:<br>$<br>6% Bank deposits 8 000<br>Interest income 300<br><br>(i) The bank deposits commenced on 31 March 2020. | <u>Other income</u><br>Interest income 360<br><br>Interest income from 31 Mar to 31 Dec 2020<br>= (6% X 8 000 X 9/12)<br>= $360 | <u>Current assets</u><br>6% Bank deposits 8 000<br>Interest income receivable 60<br>(360 – 300) |
| 13) | **<u>Increase in Allowance for impairment of TR (AFIOTR)</u>**<br><br>Trial balance as at 31 Dec 2020:<br>$<br>Trade receivables 6 000<br>AFIOTR **(last yr's estimate)** 200<br><br>(i) It is estimated that 5% of its trade receivables are likely to be uncollectible. | <u>Less: Other expenses</u><br>Impairment loss on TR 100<br>(300 – 200)<br><br>Impairment loss on TR is the change (**increase**) in AFIOTR | <u>Current assets</u><br>Trade receivables 6 000<br>Less: AFIOTR<br>(5% X 6 000) <u>300</u><br>**5700** |
| 14) | **<u>Decrease in Allowance for impairment of TR (AFIOTR)</u>**<br><br>Trial balance as at 31 Dec 2020:<br>$<br>Trade receivables 13 000<br>AFIOTR **(last yr's estimate)** 900<br><br>(i) The business maintains its allowance for impairment of trade receivables at 2% of its trade receivables. | <u>Less: Other expenses</u><br>**Reversal** of impairment loss on TR (640)<br>(900 – 260)<br><br>Reversal of impairment loss is the change (**decrease**) in AFIOTR | <u>Current assets</u><br>Trade receivables 13 000<br>Less: AFIOTR<br>(2% X 13 000) <u>260</u><br>**12 740** |

| Type of Adjustments | | Effects on Statement (Performance) | Effects on Statement (Position) |
|---|---|---|---|
| 15) | **<u>Write-off of TR (Bankrupt)</u>**<br>**<u>No ending allowance</u>**<br><br>Trial balance as at 31 Dec 2020:<br>$<br>Trade receivables 4 800<br>AFIOTR **(last yr's estimate)** 600<br><br>(i) Jen was declared bankrupt and the business decided to write-off the amount $700 owing from her. | <u>Less: Other expenses</u><br>Impairment loss on TR 100<br><br>To write-off:<br>TR – 600; AFIOTR – 600<br><br>After write-off, updated AFIOTR<br>= 600 – 700 = – 100<br>It should **increase by $100** to become $0. | <u>Current assets</u><br>Trade receivables<br>(4 800 – 600) 4 200<br><br>*AFIOTR is 0 as the estimated uncollectible amount is not given in additional info. You may skip it.* |
| 16) | **<u>Partial write-off of TR (Bankrupt)</u>**<br>**<u>No ending allowance</u>**<br><br>Trial balance as at 31 Dec 2020:<br>$<br>Trade receivables 9 000<br>AFIOTR **(last yr's estimate)** 900<br>Cash at bank 700<br><br>(i) A customer who owed $400 paid only 10% of debts owed. The remaining amount was to be written off. | <u>Less: expenses</u><br>**Reversal** of<br>impairment loss on TR (540)<br><br>To write-off: TR – 400<br>AFIOTR – 360; CAB + 40<br><br>After write-off, updated AFIOTR<br>= 900 – 360 = 540<br>It should **decrease by $540** to become $0. | <u>Current assets</u><br>Trade receivables<br>(9 000 – 400) 8 600<br><br>Cash at bank 740<br>(700 + 40)<br><br>*AFIOTR is 0 as the estimated uncollectible amount is not given in additional info. You may skip it.* |
| 17) | **<u>Write-off of TR (Bankrupt)</u>**<br>**<u>& Increase in Allowance for impairment of TR (AFIOTR)</u>**<br><br>Trial balance as at 31 Dec 2020:<br>$<br>Trade receivables 9 000<br>AFIOTR **(last yr's estimate)** 200<br><br>(i) A customer who owed $1 000 was declared bankrupt and its debt was written off.<br><br>(ii) It is estimated that 6% of its trade receivables are likely to be uncollectible. | *Write-off of TR must be deducted from TR and allowance before calculating impairment loss i.e. do adjustment (i) before (ii)*<br><br><u>Less: Other expenses</u><br>Impairment loss on TR 1 280<br><br>To write-off:<br>TR – 1000; AFIOTR – 1000<br><br>After write-off, updated AFIOTR<br>= 200 – 1 000 = – 800<br>It should **increase by $1280** to become $480. | <u>Current assets</u><br>Trade receivables<br>(9 000 – 1 000) 8 000<br>Less: AFIOTR<br>(6% X 8 000) <u>480</u><br>**7 520** |

<table>
<tr><th colspan="2">Type of Adjustments</th><th>Effects on<br>Statement (Performance)</th><th>Effects on<br>Statement (Position)</th></tr>
<tr><td>18)</td><td><u>Write-off inventory</u><br><br>Trial balance as at 31 Dec 2020:<br>Inventory 20 000<br><br>(i) The net realisable value of inventory is $15 000. / $5 000 worth of inventory was damaged. This has not been adjusted at year end.</td><td>Inventory is recorded at cost of net realisable value, whichever is lower.<br>Impairment loss = Cost – NRV<br><br><u>Less: Other expenses</u><br>Impairment loss on inventory 5 000<br>[20 000 – 15 000]</td><td><u>Current assets</u><br>Inventory 15 000</td></tr>
<tr><td>19)</td><td><u>Write-off inventory<br>& a total claim has been agreed with the insurance company.</u><br><br>Trial balance as at 31 Dec 2020:<br>Inventory 20 000<br><br>(i) During the year, $5 000 worth of inventory was stolen. The insurance company agreed to compensate fully but this amount has not been received as at year end.</td><td>No effect</td><td><u>Current assets</u><br>Inventory 15 000<br>(20 000 – 5 000)<br><br>Insurance claim receivable 5 000</td></tr>
<tr><td>20)</td><td><u>Write-off inventory<br>& a partial claim has been agreed with the insurance company.</u><br><br>Trial balance as at 31 Dec 2020:<br>Inventory 20 000<br><br>(i) During the year, $5 000 worth of inventory was stolen. The insurance company agreed to compensate only $1 000. This amount was not paid to the business as at year end.</td><td><u>Less: Other expenses</u><br>Impairment loss on inventory 4 000<br>(5 000 – 1 000)</td><td><u>Current assets</u><br>Inventory 15 000<br>(20 000 – 5 000)<br><br>Insurance claim receivable 1 000</td></tr>
<tr><td>21)</td><td><u>Depreciation of NCA</u><br><br>Trial balance as at 31 Dec 2020:<br>$<br>Equipment 1 800<br>Accumulated depreciation 360<br>Motor vehicle 25 900<br>Accumulated depreciation 5180</td><td><u>Less: Other expenses</u><br>Depreciation of equipment (10%x 1 800) 180<br><br>Depreciation of motor vehicle 4 144<br>[20%x (25 900 – 5 180)]</td><td><u>Non-current assets</u><br><br><table><tr><th></th><th><u>Cost</u></th><th><u>Acc Dep</u></th><th><u>NBV</u></th></tr><tr><td>Eqmt</td><td>1800</td><td>540*</td><td>1260</td></tr><tr><td>MV</td><td>25900</td><td>9324**</td><td>16576</td></tr><tr><td>Property</td><td>120000</td><td>4000***</td><td>116000</td></tr></table></td></tr>
</table>

| Type of Adjustments | | Effects on Statement (Performance) | Effects on Statement (Position) |
|---|---|---|---|
| | Property 120 000<br>Accumulated depreciation 3 000<br><br>(i) Depreciation is charged at 10% using the straight-line method on the equipment. / Depreciation is charged on equipment at 10% **on cost.**<br><br>(ii) Depreciation is charged at 20% using the reducing balance method on the motor vehicle. Depreciation is charged at 20% **on net book value** of the motor vehicle.<br><br>(iii) Property have a useful life of 100 years with a residual value of $20 000. | Depreciation of property 1 000<br>[(120 000 – 20 000) /100] | *Acc Dep = 360 + 180<br><br>**Acc Dep = 5 180 + 4 144<br><br>*** Acc Dep = 3 000 +1 000 |