

Name: _____

Class: _____

Option: _____

Teacher: Mr. Jones

ACCOUNTS
WORKBOOK
GRADE 11
PRINCE WILLIAMS HIGH SCHOOL
TERM 1

INSTRUCTIONS TO CANDIDATES

REVIEW NOTES AND ANSWER QUESTIONS PROVIDED

ALL YOUR ANSWERS MUST BE WRITTEN IN INK.

Most firms conduct a large proportion of their business on a credit basis, whether it is a wholesale or retail business. Therefore, at the end of any one month, the firm will have a certain amount of money that is outstanding from debtors.

However, over the years, a firm may find that there are some debtors who will not pay up amounts that are owed. A number of reasons could contribute to this. The debtor could have gone bankrupt and is simply not in a position to pay. It could also be that, his business could have burnt down, or the debtor has gone abroad without honouring his debts. Whatever the reason, the firm has to take into account any amount that it will not collect. The objective is to make the adjustment in the final account, so that the firm's profits won't be overstated.

Bad debt, then, is that proportion of an outstanding debt, that the firm feels it will not collect. Once the debt has been declared bad, then it needs to be removed from the books.

The double entry for removing a debt is as follows:

(i) Dr Bad Debt a/c

(ii) Cr Debtors a/c

The second step would be to close off the Bad Debt account, the entries are:

(iii) Cr Bad Debt a/c

(iv) Dr Profit and loss a/c

Bad Debt is regarded as an expense and is therefore listed among the expenses in the profit and loss account.

PROVISION FOR BAD DEBT

In accounting a provision is really making an allowance for something before it actually occurs. A firm creates a provision for bad debt because it knows from experience over the years some of its debtors may eventually become bad debts. One could ask, "But why does the firm continue to credit if they know this"? The firm does not know for sure, who will not pay, but it is just one of the risks of business that it is still willing to take.

The entries for recording provision for bad debt are: In the first year:

(i) Dr Profit & Loss a/c

(ii) Cr Provision for Bad Debt a/c

Sometimes there may be either an increase or a decrease in the provision. To record an increase

(iii) Dr Profit & Loss a/c

(iv) Cr Provision for Bad Debt a/c

with the amount of the increase. An increase in the total provision, further decreases profits, hence the reason we debit the profit and loss account. Please note that bad debt represents a cost to the firm, since it is revenue that the firm has lost.

If there is a decrease in the provision for bad debt the entries are:

(v) Cr Profit & Loss a/c

Dr Provision for Bad Debt a/c with the amount of the decrease. Here the profit and Loss account is credited because we are collecting more money than anticipated.

THE BALANCE SHEET

The total provision for Bad Debt is subtracted from debtors in the balance sheet.

we continue our discussion on Bad Debts. Let's look at an example:

EXAMPLE 1

Chadwicks Ltd is a Trading firm in Kingston. One of its customers Wayne Brady has fallen on hard times and gone bankrupt. He has an outstanding balance of \$860 at Dec. 31,

2003. The firm has decided to write off the debt.

SOLUTION:

First we remove the debt, then close off the bad debt account as follows.

W. BRADY A/C

| | | | |
|----------------|-----------|------------------|-----------|
| 2003 | \$ | 2003 | \$ |
| Dec 31 bal b/d | 860 | Dec 31 Bad Debts | 860 |

BAD DEBT A/C

| | | | |
|-----------------|-----------|----------------------|-----------|
| 2003 | \$ | 2003 | \$ |
| Dec 31 W. Brady | 860 | Dec 31 Profit & Loss | 860 |

PROFIT & LOSS (EXTRACT)

| | |
|------------------------|-----|
| Rent | 200 |
| Wages | 150 |
| Bad Debts | 860 |
| ance at Dec. 31, 2004. | |

EXAMPLE 2

The following year, the firm decided to make a provision for bad debt at year end. The balance of debtors remaining was \$12,500. It was decided to make a provision for bad debt of 5% of the debtor bal-

SOLUTION:

5% of \$12,500 = 625

The following two years the information was as follows

Take note that in the year 2005, there was a reduction in the provision for bad debt, from

PROVISION FOR BAD DEBT A/C

| | | | |
|----------------|-----------|----------------------|-----------|
| 2004 | \$ | 2004 | \$ |
| Dec 31 bal c/d | 625 | Dec 31 Profit & Loss | 625 |
| | | 2005 | |
| | | Jan 1 bal b/d | 625 |

\$625 to \$480. In the year 2006 the provision increased from \$480 to \$840.

Here are the entries.

| Year | Total Debtors | % provision |
|--------------------|----------------------|--------------------|
| 2005 | \$12,000 | 4 |
| 2006 | \$14,000 | 6 |
| 4% of 12,000 = 480 | | |
| 6% of 14,000 = 480 | | |

Notice that in the second year (2005) only the amount of the decrease that is, the \$145

was debited in the provision for bad debt account.

A reduction in the provision means increased profits, the reason we credit the Profit & Loss account.

When the provision increased in the year 2006 the Profit and Loss account was debited.

This indicates an increased cost for the firm. The profit and loss and Balance Sheet extracts would appear as follows.

PROVISION FOR BAD DEBT

| | | | | |
|----------------|------------|---------------|------------|-------------|
| 2004 | | 2004 | | |
| Dec 31 BAL C/D | 625 | Dec 31 P&L | 625 | |
| 2005 | | 2005 | | |
| Dec 31 P&L | 145 | Jan 1 bal b/d | 625 | Note |
| Dec 31 bal c/d | 480 | | | that, it is |
| | 625 | | 625 | the |
| 2006 | | 2006 | | amounts |
| Dec 31 bal c/d | 840 | Jan 1 bal b/d | 480 | that the |
| | 840 | Dec 31 P&L | 840 | provision |
| | | | | in- |
| | | | | creased |
| | | | | to |
| | | | | (\$840) |

and decreased to (\$480) that went to the Balance Sheet.

PROFIT & LOSS (EXTRACT)

| | | | |
|------------------------|-----|-----------------------|-----|
| 2004 | | 2005 | |
| provision for bad debt | 625 | decrease in provision | 145 |
| | | | 5 |
| 2006 | | | |
| increase in provision | 360 | | |

BALANCE SHEET (EXTRACT)**Current Assets**

| | | | |
|-----------------|--------|--------|----|
| 2004 | | \$ | \$ |
| Debtors | 12,500 | | |
| Less provision | 625 | 11,875 | |
| 2005 | | | |
| Debtors | 12,000 | | |
| less; provision | 480 | 11,520 | |
| 2006 | | | |
| Debtors | 14,000 | | |
| Less provision | 840 | 13,160 | |

The following refers to the Letter T Trading Company:

| YEAR | DEBTORS | PROVISION FOR DOUBTFUL DEBTS |
|------|----------|------------------------------|
| 2003 | \$10 000 | 2 ½ % |
| 2004 | 12 500 | 3 % |
| 2005 | 12 000 | 3 % |

You are required to :

- A. i) Show the entries for recording the Provision for Doubtful Debts for each year in a Journal. [9]
- ii) Show the Provision for Doubtful Debts for each year [2]
- iii) Show the Profit and Loss Accounts Extract for each year. [3]
- iv) Show the Balance Sheet extract for each year [3]

- B. i) Why is a Provision for Doubtful Debts account needed ?

[2]

- ii) The creation of a provision for Doubtful debts is an example of which Accounting Concept (Principle or Convention) ?

[1]

PREPAYMENTS AND ACCRUALS

AS YOU have seen from the preparation of the profit and loss account, all businesses incur expenses as a normal part of their day-to-day operations. Such expenses may take the form of utility bills, wages and salaries, advertising and rent.

Sometimes, at the end of the accounting period, there may be expenses that still remain unpaid, even though they are due. The amount that is owing is referred to as an accrual. On the other hand, the firm may pay an expense before it becomes due. This is regarded as a prepayment.

In an effort to give an accurate figure for net profit, we must make adjustments for prepayments and accruals in the final accounts.

PREPAYMENT: EXAMPLE 1

The annual insurance premium on the motor van of Unimotors Ltd. is \$12,000. The premiums are paid Quarterly and payments were made as follows:

| | |
|---------|---------|
| March 1 | \$6,000 |
| June 30 | \$2,500 |
| Dec. 31 | \$6,000 |

This is what the insurance account would look like.

| | | <u>Insurance a/c</u> | | |
|--------------|---------|----------------------|----------|--|
| Mar 1 Bank | \$6,000 | Dec 31 P&L | \$12,000 | |
| June 30 Bank | \$2,500 | | | |
| Dec 31 Bank | \$6,000 | Dec 31 Prepaid c/d | \$ 2,500 | |
| | 14,500 | | 14,500 | |

EXAMPLE 1: ACCRUALS

During the year the company purchased stationery on credit costing \$1,000 payments were subsequently made as follows:

A total of \$750 has been paid at year end. The stationery account would appear as follows.

Take note that the balance of \$250 represents an accrual, the amount still owing at year end.

THE PROFIT & LOSS A/C

| | |
|-------------|-----|
| | \$ |
| February 10 | 250 |
| July 1 | 350 |
| December 20 | 150 |

Prepayment is subtracted from the actual amount of the expense paid. Accruals on the other hand are added to the actual amount that was paid.

EXAMPLE 2: Prepayment

| | | <u>Stationery a/c</u> | | |
|------------------|-------|-----------------------|-------|--|
| Feb 10 Bank | \$250 | Dec 31 P&L | 1,000 | |
| Jul 1 Bank | \$350 | | | |
| Dec 20 Bank | 150 | | | |
| Dec 31 Owing c/d | 250 | | | |
| | 1,000 | | 1,000 | |
| | | Jan 1 Owing b/d | 250 | |

THE BALANCE SHEET

Prepayments are listed as the last item under *current assets*. This money still belongs to the firm, since it is not yet due.

Accruals are listed as the last item under *current liabilities* since this amount is still owing.

Profit & Loss a/c (extract)

| | \$ | \$ |
|-----------------|--------|--------|
| Insurance | 12,500 | |
| Less Prepayment | 2,500 | 10,000 |
| Stationery | 750 | |
| Add Accrual | 250 | 1,000 |

| Telephone | |
|---|-------------|
| 2005 | \$ |
| Apr 2 Bank | 345 |
| Jul 3 Bank | 420 |
| Oct 5 Bank | 375 |
| <i>Note:</i> The telephone bill of \$520 for the three months ended 31 December 2005 was not paid until 2006. | |
| Rent | |
| 2005 | \$ |
| Jan 2 Bank | 2,000 |
| Mar 31 Bank | 2,000 |
| Jul 7 Bank | 2,000 |
| Oct 2 Bank | 2,000 |
| Dec 30 Bank | 2,000 |
| <i>Note:</i> The payment for rent of \$2,000 on 30 December 2005 covers the period 1 January 2006 to 31 March 2006. | |
| Commission Income | |
| | 2005 |
| | \$ |
| | Apr 30 Bank |
| | 1,280 |
| | Sept 2 Bank |
| | 1,400 |
| <i>Note:</i> The commission income of \$1,360 earned for the four months from 1 September to 31 December 2005 will be received in 2006. | |

P. Curtis bought a motor vehicle for \$10 000 on 1 January 2006. It had a residual value of \$500 and is to be used for 5 years. The motor vehicle was sold on 2 January 2008 for \$6 000.

YOU ARE REQUIRED TO:

I. Draw up the following Ledger accounts:

i. Motor Vehicle account

[1½]

ii. Provision for Depreciation account

[2½]

iii. Motor Vehicle Disposal account

[3]

II. Show the Profit & Loss account extract.

[2]

III. Prepare the Balance Sheet extract for 31 December 2008.

[2]

IV. What is the purpose of *DEPRECIATION*?

[1]

- (a) On 1 January 1994 W. Clark purchased by cheque two motor vans for \$7,000 each.

At the end of each year 31 December 1994, 1995, and 1996 the vans were depreciated by 20% of cost.

1 January 1997 one van was sold for \$3,000 cash whilst the other was taken in part exchange at a valuation of \$2,500 for a new van bought on credit for \$11,000 from Cartwright Garage Ltd.

Write up accounts to record the purchase of the old and new vans, depreciation, disposal and the entries for the creditor's account. [8]

- (b) Set out extracts from the appropriate section of the balance sheets on 31 December 1994, 1995 and 1996 showing how the motor vans should appear. [5]

Total marks [13]

V. Say how *EACH* of the following methods of depreciation is calculated. [3]

Straight Line

Diminishing Balance

Revaluation

Total marks [15]

There are three methods of depreciation, calculate the following.

- (a) If a fixed asset costing \$6,500 was depreciated on the revaluation method of \$650 per annum, what would it be worth at the end of one year?

_____ [1]

- (b) A fixed asset costing \$7,500 was purchased with an estimated life of 10 years and a scrap value at the end of that time of \$500. Using the straight line or fixed instalment method, what would be the amount of depreciation at the end of the first year.

_____ [2]

- (c) Using the diminishing balance method, if a fixed asset costing \$2,000 was depreciated at 10% per annum after two years, what would it be worth?

_____ [3]

The following trial balance has been extracted from the ledger of Sir Jones, a sole trader.

Trial Balance as at 31 May 2006

| | DR | CR |
|---------------------------|-----------|-----------|
| | \$ | \$ |
| Sales | | 138, 078 |
| Purchases | 82, 350 | |
| Carriage | 5, 144 | |
| Drawings | 7, 800 | |
| Rent, Rates and Insurance | 6, 622 | |
| Postage and Stationery | 3, 001 | |
| Advertising | 1, 330 | |
| Salaries and Wages | 26, 420 | |
| Bad debts | 877 | |
| Provision for bad debts | | 130 |
| Debtors | 12, 120 | |
| Creditors | | 6, 471 |
| Cash in Hand | 177 | |
| Cash at Bank | 1, 002 | |
| Stock as at 1 June 2005 | 11, 927 | |
| Equipment: | | |
| At cost | 58, 000 | |
| Accumulated depreciation | | 19, 000 |
| Capital | | 53, 091 |
| | 216, 770 | 216, 770 |

The following additional information as at 31 May, 2006 is available:

- a. Rent is accrued by \$210
- b. Rates have been prepaid by \$880
- c. \$2, 211 of carriage represents carriage inwards on purchases.
- d. Equipment is to be depreciated at 15% per annum using the straight line method (hint: find the net book value first.)
- e. The provision for bad debts is to increased by \$40
- f. Stock at the close of business has been value at \$13, 551

Required:

- A) Prepare Jones' Trading and profit and loss account for the period ended 31 May 2006 (20 marks)
- B) Prepare his balance sheet as May 31, 2006 (20 Marks)

Show all workings below: