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Financial Accounting Exercises

Exercises

Depreciation Case Study

Calculations:

Straight line

- = $\$15\,000 - \$3\,000 = \$12\,000 / 6 \text{ years} = \$2\,000 \times 9/12 = \$1\,500$

In this first calculation the asset has only been in the possession of the business for 9 months **and this has to be factored into the calculation.**

- = $\$15\,000 - \$3\,000 = \$12\,000 / 6 \text{ years} = \$2\,000$

Diminishing balance

- = $\$15\,000 \times .25 \times 9/12 = \$2\,813$
- = $\$15\,000 - \$2\,813 = \$12\,187 \times .25 = \$3\,047$

Note: It is unlikely that you will have irregular figures as per the diminishing balance calculations above.

You may be asked why the amount of depreciation for diminishing balance is greater in the second year than in the first. The answer is that in the first year the business only had the asset for 9 months of that time.

You will note that the straight line method takes into account residual value whilst the diminishing balance method ignores that amount for purposes of calculation.

Straight line

General journal

| | | | |
|-----------|---|-------|-------|
| 30.6.2002 | Depreciation of Pizza Oven | 1 500 | |
| | Accumulated depreciation of Pizza Oven | | 1 500 |
| | Pizza Oven depreciated at straight line for 6 years. | | |
| | Profit and Loss account | 1 500 | |
| | Depreciation of Pizza Oven | | 1 500 |
| | Depreciation posted to Profit and Loss account. | | |

It is important to include the name of the asset in the title - should a student simply use the term 'depreciation, there would be a one mark deduction.



Financial Accounting Exercises

General ledger

Depreciation of Pizza Oven

| | | | | | |
|-----------|--|-------|-----------|---------------------|-------|
| 30.6.2002 | Accumulated Depreciation of Pizza Oven | 1 500 | 30.6.2002 | Profit and Loss a/c | 1 500 |
|-----------|--|-------|-----------|---------------------|-------|

Accumulated depreciation of Pizza Oven

| | | | | | |
|--|--|--|-----------|----------------------------|-------|
| | | | 30.6.2002 | Depreciation of Pizza Oven | 1 500 |
|--|--|--|-----------|----------------------------|-------|

Profit and Loss account

| | | | | | |
|-----------|----------------------------|-------|--|--|--|
| 30.6.2002 | Depreciation of Pizza Oven | 1 500 | | | |
|-----------|----------------------------|-------|--|--|--|

Entries will be identical in both the general journal and general ledger for the second year of the straight line and for the two years of diminishing balance - only the dollar amounts will be different.

Look at other examples for how to deal with accumulated depreciation when an opening balance is provided.

Straight line

| Profit and Loss for year ended 30.6.2002 | | |
|--|-------|--------------|
| | \$ | \$ |
| Sales | | 8 000 |
| less Expenses | 4 000 | |
| + Depreciation of Pizza Oven | 1 500 | |
| Total Expenses | | 5 500 |
| Net profit | | 2 500 |

Straight line

| Profit and Loss for year ended 30.6.2003 | | |
|--|-------|--------------|
| | \$ | \$ |
| Sales | | 8 000 |
| less Expenses | 4 000 | |
| + Depreciation of Pizza Oven | 2 000 | |
| Total Expenses | | 6 000 |
| Net profit | | 2 000 |

Diminishing balance

| Profit and Loss for year ended 30.6.2002 | | |
|--|----|-------|
| | \$ | \$ |
| Sales | | 8 000 |



Financial Accounting Exercises

| | | |
|------------------------------|-------|--------------|
| less Expenses | 4 000 | |
| + Depreciation of Pizza Oven | 2 813 | |
| Total Expenses | | 6 813 |
| Net profit | | 1 187 |

Diminishing balance

| Profit and Loss for year ended 30.6.2003 | | |
|--|-------|------------|
| | \$ | \$ |
| Sales | | 8 000 |
| less Expenses | 4 000 | |
| + Depreciation of Pizza Oven | 3 047 | |
| Total Expenses | | 7 047 |
| Net profit | | 953 |

You will notice that the diminishing balance charges more to depreciation in the first two years. In 2002 it is \$1313 greater and in the year 2 003, \$1047 more. This reduces profit by those amounts in the first two years.

Balance sheet extracts - 30.6.2002

| | Straight line | Diminishing balance |
|-------------------------------|---------------|---------------------|
| Pizza Oven | 15 000 | 15 000 |
| less accumulated depreciation | 1 500 | 2 813 |
| Carrying cost | 13 500 | 12 187 |

Balance sheet extracts - 30.6.2003

| | Straight line | Diminishing balance |
|-------------------------------|---------------|---------------------|
| Pizza Oven | 15 000 | 15 000 |
| less accumulated depreciation | 3 500 | 5 860 |
| Carrying cost | 11 500 | 9 140 |

CC = carrying costs

The accumulated depreciation represents the amount of the cost of an asset allocated as an expense added up over a number of accounting periods.

CC represents that portion of the total cost of a non-current asset not yet allocated as a cost. It also includes the residual value.



Financial Accounting Exercises

Fun Run Enterprise – Exercise Details

A budgeting problem - Fun Run Enterprises

Fun Run enterprises commenced business in 2002. The following budgeted information for the year ending 30.6.2003 has been provided.

Sales

- total sales for the year is expected to be \$400 000
- 40% of sales are for cash
- staff are expected to be paid \$60 000 in salaries
- sales returns are anticipated at \$3000

Goods sold

- cost of goods sold is to be set at 60% of (gross) sales. All goods are bought on credit
- creditors are paid
- stock loss is expected to be \$2400
- stock on hand at 30.6.2003 is anticipated to be \$34 000

Anticipated payments

- advertising \$16 000
- cleaning \$6000
- drawings \$45 000
- loan repayment \$10 000

Other items

- discount expense \$500
- bad debts \$2000

Cash budget for the month ending 31 May

| | 1/7/2002 | 30/6/2003 |
|-------------------------------|-----------|-----------|
| Assets | \$ | \$ |
| Bank | 11 000 | ? |
| Stock | 32 000 | 34 000 |
| Prepaid advertising | 1 500 | 2 000 |
| Debtors | 52 000 | 55 000 |
| Machinery | 80 000 | 80 000 |
| less Accumulated depreciation | (4 000) | (12 000) |
| Liabilities | | |
| Creditors | 20 000 | 22 000 |
| Accrued salaries | 4 400 | 4 100 |
| Accrued interest | | 6 500 |
| Loan | 100 000 | 90 000 |
| Owner's equity | | |



Financial Accounting Exercises

| | | |
|---------|---|---|
| Capital | ? | ? |
|---------|---|---|

A task on variance analysis- Exercise Details

The following reports include the budgeted figures for Fun Run.

You are now provided with the actual figures and are asked to show the variance and state whether it is favourable or not.

The first step in the process of variance analysis is to state the amount of variance. For instance, if cleaning is budgeted for \$6000 and you actually pay \$7000 then the variance is \$1000.

The second step is to state whether this is favourable (F) or unfavourable (UF). This process is 'mechanical' in that it does not allow for subjective opinion. An increase in spending on advertising would be regarded as 'unfavourable' yet it may result in a substantial increase in sales. That would be regarded as favourable.

The example for cleaning is shown.

The third step is to 'explain' why the variation took place. When making this explanation you may have to consider an interrelationship with other items. Often these items are contained in the relevant ledger accounts.

Take the case of debtors. The closing balance in the debtors account will be affected by credit sales. An increase in credit sales has the potential to increase the closing balance. However, cash received from debtors, bad debts and discount reduce the debtors closing balance. An increase in discount should encourage debtors to pay more quickly.

Improvement in sales may be related to increases in selling expenses such as sales, salaries and advertising. It may also be due to an increase in non-current assets, in particular new premises, motor vehicles or equipment. In fact if certain expenses or non-current assets increase and sales do not respond you have to challenge why that expenditure was undertaken.

Learn to think in opposites. The explanation for debtors given above applies in the same way to creditors. Because we are using the perpetual stock approach you must link creditors to stock control. In a similar way cost of sales, which reduces the stock control balance is linked to sales. Sales may increase as a result of more units being sold, or as a result of increased prices. If more units are sold then we would expect an increase in cost of sales. This leads to changes in stock control and creditors (if the stock is bought on credit).



Financial Accounting Exercises

Variance reports – Exercise Detail

Advice

- To complete the variance reports the following steps are necessary.

Cash budget

1. Take the opening bank balance and add that to the total of cash receipts.
2. Total cash payments.
3. Deduct item 2 from item 1 to arrive at the closing bank balance.
4. Transfer the closing bank balance to the Balance sheet as the amount for 'Bank'.

Profit and Loss statement

1. Determine net profit by deducting the total of expenses from adjusted gross profit.
2. Transfer the net profit to the Owner's equity section of the balance sheet.

Balance sheet

1. Total current assets (after the inclusion of bank).
2. Determine the new figure for machinery.
3. Add depreciation from the Profit and Loss statement to accumulated depreciation (\$4 000 on 1 July 2002) to get the new figure for that item.
4. Total non-current assets.
5. Add current and non-current assets to get total assets.
6. Total current liabilities.
7. Insert net profit.
8. Insert drawings.
9. Determine total equities.

In preparing this problem the following accounts had to be reconstructed:

- debtors
- creditors
- stock control
- advertising
- salaries
- loan



Financial Accounting Exercises

Cash flow statements – Exercise Details

Stevens Computer Sales has supplied the following list of transactions for his business. The accounting period commenced 1 July 2002 and continues until 30 June 2003

- Steven commenced business with \$20 000 cash contribution to the business
- Steven bought a motor vehicle for \$15 000 cash on 31.12.2002
- the motor vehicle is to be depreciated at 10% per annum
- \$8000 is borrowed. It is to be repaid by instalment at \$2000 per annum
- cash sales are \$65 000
- credit sales are \$45 000 with \$40 000 being received by the end of the financial year from debtors
- wages paid are \$37 500, with \$2500 still owing
- Steven receives \$600 per year from a magazine commission. To date he has received \$400
- rent is \$200 per month and Steven has paid eleven months in this financial year
- Steven bought \$15 000 worth of computers and has sold \$13 600 worth
- advertising is \$2000 per quarter. In this financial year Steven has paid \$10 000
- other expenses total \$13 000 and they have been paid in cash

Prepare the following:

- a cash flow statement for the year ended 30.6.2003.
- a Profit and Loss statement for the same period.
- a balance sheet as at 30.6.2003.

In preparing the report for the cash flow statement

Likely errors include failure to:

- classify cash inflows and outflows into
 - operating
 - Investing
 - financing items
- reconstruct the accounts to determine revenue received and expenses paid rather than revenue earned and expenses incurred
- failure to include all items; for example, loan repayment may be overlooked
- correctly reconstruct accounts
- include opening bank balance into the cash flow statement
- exclude non-cash items
- correct classification of items



Financial Accounting Exercises

Horse people – Exercise Detail

Horse People present you with the following information.

| | Cash statement | Profit and Loss statement | Balance Sheet 1 Jan. | Balance Sheet 30 June |
|----------------------------|----------------|---------------------------|----------------------|-----------------------|
| Cash Sales - Whips | 20 000 | ? | | |
| - Saddles | ? | 10 000 | | |
| Credit sales - Whips | | 40 000 | | |
| - Saddles | | 20 000 | | |
| Cost of sales - Whips | 30 000 | ? | | |
| Cost of sales - Saddles | | 15 000 | | |
| Stock of saddles – 1 Jan. | | | 3 500 | |
| Stock of saddles – 30 June | | | | 3 000 |
| Rent revenue | 1 600 | | | |
| Advertising | 6 000 | | | |
| Wages | | 12 400 | | |
| Petrol | 2 000 | 2 000 | | |
| Depreciation of equipment | | ? | | |
| Office expenses | 1 500 | | | |
| Office salaries | | 6 500 | | |
| Discount expense | | 900 | | |
| Bad debts | | 400 | | |
| Accounting expenses | 800 | | | |
| Security expenses | | 200 | | |
| Profit and Loss | | | | ? |
| Bank | | | 5 000 | ? |
| Accrued rent revenue | | | | 800 |
| Debtors (cash received) | ? | | 22 000 | 21 500 |
| Prepaid advertising | | | 6 000 | 5 400 |
| Equipment | | | 30 000 | 40 000 |
| Accumulated. Depreciation | | | (10 000) | ? |
| Accrued wages expense | | | | (2 400) |
| Creditors | ? | | (14 000) | (13 500) |
| Loan (received 1 Jan.) | *1 000 | | (12 000) | ? |
| Capital | | | (30 500) | ? |
| Drawings of cash | 18 000 | | | |
| Surplus/deficit of cash | | | | |
| * repayment | | | | |

Whips are bought for cash, saddles are bought on credit.

Opening stock was valued at \$3500



Financial Accounting Exercises

Task Requirements

1. Determine cash sales in the cash statement.
2. Reconstruct debtors a/c to find cash received from debtors.
3. Reconstruct rent revenue a/c to find rent revenue (Profit and Loss a/c).
4. Reconstruct creditors a/c to find cash paid to creditors for saddles.
5. Reconstruct advertising a/c to determine advertising expense.
6. Reconstruct wages a/c to determine wages paid.
7. Calculate depreciation at 20 % per annum. Note that the additional equipment is bought on the last day of the accounting period.
8. Determine office expenses, office salaries, accounting expenses and security expenses in the appropriate column.
9. Determine accumulated depreciation of equipment in the balance sheet.
10. Determine loan in the balance sheet.

Additional information

In preparing the departmental Profit and Loss statement the following allocations of expenses occur.

- Advertising is distributed equally
- 90% of petrol is used to deliver saddles and 10% for whips
- The owner uses a personal vehicle and only petrol is charged to the business
- Wages is shared \$5000 to whips and the balance to saddles
- Equipment is used 40% for whips and 60% for saddles
- All other expenses are considered 'general'

Required

Prepare the following fully classified reports:

- Cash flow statement
- Departmental Profit and Loss statement
- Balance sheet



Financial Accounting Exercises

Departmental Profit and Loss statement A – Exercise Details

Welcome to Media World. This business sells DVD players (DVDs) and Television sets (TVs).

At the beginning of November Media World have the following assets and liabilities:

Assets

- stock \$6000
- prepaid rent \$1000
- workshop equipment \$36 000
- land and buildings \$180 000

Liabilities

- bank overdraft \$10 000
- accrued wages \$700
- loan \$40 000
- accumulated depreciation on workshop equipment is \$3000

You have to determine capital at 1 November.

Information

- Media World sells DVDs and TVs. Workshop equipment is only involved in repairing TVs, service costs are only for the DVDs
- Media World employs three sales staff, who spend two-thirds of their time selling DVDs and one-third selling TVs. Two other people work at repairing TVs and another person works in servicing. There are two staff members employed in the office
- the business has four cost centres: sales, workshop, office and finance
- each person employed by Media World is paid \$100 per day and works a five day week. The prepaid and accrued expenses must be reversed for each month
- the calendar for November is shown below. Dates shown in bold are the days on which staff are paid. Staff do not work on Monday and Tuesday as Media World operates in a tourist area and these are quiet days. They do work on weekends

| November | | | | | | |
|----------|----|----|----|----|-----------|----|
| M | T | W | TH | F | S | S |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 |
| 8 | 9 | 10 | 11 | 12 | 13 | 14 |
| 15 | 16 | 17 | 18 | 19 | 20 | 21 |
| 22 | 23 | 24 | 25 | 26 | 27 | 28 |
| 29 | 30 | | | | | |

- workshop equipment is depreciated at 12% per annum on cost
- interest is paid annually in December. It is \$1200 for the year on the Bank overdraft and \$3600 for the year for the loan



Financial Accounting Exercises

- rent is \$3000 per month and is allocated in equal proportions to sales, workshop and office
- advertising is allocated according to sales
- cash sales are 40% of total sales. Cash sales are \$20 000 for the DVD players and \$10 000 for TVs
- there is a mark up of 100% on all goods sold
- stock loss is \$500 (all DVDs)
- bad debts are \$1000
- at the end of November prepaid rent is \$600
- you will have to calculate accrued wages at 30 November
- Other expenses include:
 - advertising is \$3000
 - service costs are \$1000
 - cleaning \$2000



Financial Accounting Exercises

Cash versus profit – Case Study details

Stan Jones from Stan's CDs, DVDs Videos etc Pty Ltd is a friend seeking some accounting advice. He is unable to distinguish between cash and profit. Having recorded a significant profit for the period Stan is of the opinion that he is entitled to buy a new four-wheel drive vehicle. In fact he does buy the vehicle and has incurred the wrath of his bank manager. He asks you to explain why the bank manager is unhappy. You ask for the financial details of your friend. The reporting period runs from 1 January to 30 June.

At 1 January opening balances appeared as follows:

General journal

| | | | |
|--------|--------------------------------------|--------|--------|
| 1 Jan. | Bank | 6 500 | |
| | Debtors | 5 400 | |
| | Prepaid rent | 2 000 | |
| | Vehicles | 30 000 | |
| | Accumulated depreciation of vehicles | | 15 000 |
| | Creditors | | 6 000 |
| | Loan | | 10 000 |
| | Capital | | 12 900 |
| | Opening balances | | |

Between January and June the following events occur:

- the new vehicle is bought for \$45 000 cash
- the old vehicle is sold for \$13 500, with a loss of \$1500
- \$2000 is repaid on the loan. A further \$2000 will be repaid in November
- credit sales are \$80 000
- debtors pay \$76 000. They receive a further \$800 discount
- sales returns are \$1000
- cash sales are \$85 000
- all goods are bought on credit. Creditors are paid \$74 000. There is no discount
- cost of sales is \$70 000
- stock at 30 June is \$3500
- rent is \$200 per month and is prepaid
- the cash payments journal recorded the following expense payments:
 - wages \$18 000
 - advertising \$4000
 - other expenses \$6000



Financial Accounting Exercises

- cash drawings are \$20 000

Stan tells you that he has contributed:

- cash of \$10 000
- a fax machine valued at \$800 (no depreciation this period)
- depreciation on the new vehicle is 12% per annum on cost. The vehicle is to be depreciated for the full reporting period
- there is \$500 owing on wages

Required

Prepare the following reports:

1. Cash flow statement
2. Profit and Loss statement (expenses not required to be classified)
3. Balance sheet

Answer the following questions

The increase in the bank balance and net profit is different. Some items only affect cash, others only affect profit whilst some affect both at different amounts. State these items in the table below.

Case

Profit

Affect both at different amounts

Further question

What alternative actions did Stan have to buying the vehicle in this period?

1. postpone the purchase of the vehicle
2. acquire the vehicle by leasing

rather than buying



Financial Accounting Exercises

3. pay a deposit and buy on credit
4. buy a cheaper vehicle



Financial Accounting Exercises

Departmental profit and loss statement B- Exercise Details

Welcome to Matts World. This business sells and repairs bicycles.

Information

- Matts World sells and repairs bicycles. Workshop equipment is only involved in repairing bicycles, delivery costs are only for the sale of bicycles
- Matts World employs three sales staff, who spend two-thirds of their time selling bicycles and one-third repairing bicycles. Two other people work full time at repairing bicycles. There are two staff members employed in the office
- The business has four cost centres: sales, workshop, office and finance
- Each person employed by Matts World is paid \$100 per day and works a five day week. The prepaid and accrued expenses must be dealt with at the beginning of the month
- The calendar for November is shown below. Dates shown in bold are the days on which staff are paid. Staff do not work on Monday and Tuesday as Matts World operates in a tourist area and these are quiet days. They do work on weekends

| Sunday | Monday | Tuesday | Wednesday | Thursday | Friday | Saturday |
|--------|--------|---------|-----------|----------|--------|----------|
| 1 | 2 | 3 | 4 | 5 | 6 | 7 |
| 8 | 9 | 10 | 11 | 12 | 13 | 14 |
| 15 | 16 | 17 | 18 | 19 | 20 | 21 |
| 22 | 23 | 24 | 25 | 26 | 27 | 28 |
| 29 | 30 | | | □[| □ | |

- workshop equipment is depreciated at 12% per annum on cost
- interest is paid annually in December. It is \$600 for the year on the Bank overdraft, \$1600 for the year for the loan and \$4000 for the mortgage
- rent is \$2400 per month expense and is allocated in equal proportions to sales, workshop and office
- advertising is allocated 60% to sales of bicycles and 40% to repairs
- cash sales are 40% of total sales. Cash sales are \$40 000 for the bicycles
- fees are \$20 000 for bicycle repairs. All fees are for cash
- there is a mark up of 100% on all bicycles sold
- stock loss is \$1500
- bad debts are \$600
- at the end of November prepaid rent is \$200

Other expenses include:

- advertising \$6000
- delivery costs \$1800
- cleaning \$500



Financial Accounting Exercises

Required

A departmental Profit and Loss statement

- In this particular problem rent has been allocated in equal amounts to sales, repairs and office. This suggests an arbitrary allocation. Do you agree that all expenses should be allocated to departments?
- What advantages will Matt's World gain by classifying the Profit and Loss statement into departments?
- What advantages will Matt's World gain by classifying the balance sheet into departments?
- What are the benefits of reporting more frequently?
- The repairs department is not performing nearly as well as the sales department. What reasons may exist for retaining this department despite what appears to be a relatively poor performance?
- Suggest two reasons why it may be inappropriate to allocate cleaning to floor space
- Define the term 'contribution margin'
- List four items you would consider 'general expenses'
- It is discovered that \$200 of cleaning has been used by Matt for private use. How would you make this correction in the general journal



Financial Accounting Exercises

A stock control problem – Exercise Detail

Lou Lockwood has a shop selling electronic items, including CD Walkmans. His knowledge of accounting is limited and he only keeps a "list" of his transactions involving Walkmans.

All Walkmans are bought on credit and sold for cash.

He provides the following information:

| | |
|-------|--|
| 1 Oct | 4 Walkmans on hand (cost \$70 each) |
| 6 | 3 Walkmans bought on credit (cost \$72 each) |
| 10 | 2 Walkmans sold (cash) for \$100 each (1 @ \$70, 1 @ \$72) |
| 13 | 1 Walkman withdrawn for owner's personal use (\$72) |
| 18 | 1 Walkman returned by a disgruntled buyer (cost \$70) |
| 20 | 3 Walkmans sold for \$100 each (3 @ \$70) |
| 22 | 6 Walkmans bought on credit (cost \$72 each) |
| 24 | 1 Walkman used for advertising (1 @ \$72) |
| 31 | 2 Walkmans sold for \$100 each. (2 @ \$72) |

A physical stock take on 31 October revealed 4 Walkmans (1 @ \$70, 3 @ \$72) on hand.

Note: The bracketed amounts will be used for identified cost.



Financial Accounting Exercises

Perpetual stock - Exercise Details

Hayley Badge has recently converted from using the physical stock method to the perpetual stock approach. When asked why by her friends Hayley was at a loss to explain, other than that she no longer has to spend one Sunday each month counting stock in her licensed grocery. This will help 'free up' her social life.

The introduction of a new computer system has helped minimise the time spent recording daily transactions. Hayley has been unsure of a number of transactions and they have not 'gone through' the system. For instance, some of her stock has been used for wine tastings as part of her new marketing program. Hayley has also taken wine home for her personal use and she donated two bottles of her favourite wine to a local charity. Old habits die hard and at the end of the accounting period of one month Hayley carried out a physical stock take on her favourite wine. Allowing for the transactions above she is sure that there are three bottles less than expected in her stock card.

The particular wine has experienced a fall in selling price as new, fruitier wines have come onto the market. Hayley bought the 'Tabletop' brand for \$8 per bottle plus \$1 per bottle licence fee. It now sells for \$7.00 per bottle, including the licence fee of \$1.50.

Hayley has heard about the 'lower of cost and net realisable value on an item by item rule' from a friend and wonders if it applies in this situation.

She also has a number of questions that she seeks to ask you regarding other aspects of stock control.

Required

Hayley provides you with a partly completed stock card along with some diary entries. You are required to complete the stock card.

Stock card

Item: Tabletop

| Date | Particulars | IN | | OUT | | BALANCE | | |
|--------|-------------|-----|------|-----|------|---------|------|-------|
| | | Qty | Unit | Qty | Unit | Qty | Unit | Total |
| 1 Nov. | Balance | | | | | 10 | 9 | 90 |
| 12 | Inv. 099 | 25 | 9 | | | 35 | 9 | 315 |
| 16 | Inv. 211 | | | 7 | 9 | 28 | 9 | 252 |
| 23 | CN 96 | | | 2 | 9 | 26 | 9 | 234 |



Financial Accounting Exercises

Diary entries relating to 'Tabletop' wines.

- 6 bottles used for wine tastings
- 2 bottles donated to charity
- 4 bottles used for personal imbibing
- 3 bottles 'missing'

The diary entries are to be recorded on 30 November.

It may be assumed that the 'lower of cost and net realisable value (NRV) rule on an item by item basis' will apply. You are to record this event in the stock card.

Hayley would also like the details contained in the stock card to be recorded in the 'stock control account'.

Hayley asks a series of questions regarding stock management:

- explain the meaning of the terms 'cost' and 'net realisable value'.
- what is the effect of a stock write down on the Profit and Loss statement and the balance sheet using the example above?
- explain what accounting principle would be breached by failure to adopt the 'lower of cost and net realisable value rule'.
- in relation to this rule what is meant by the phrase 'on an item by item basis'?
- how is a stock write down recorded in the General journal?
- describe two ways the stock card may assist management decision making
- explain two advantages of Hayley carrying out a physical stock take on 30 November when using the perpetual system.
- Hayley has introduced computers to her business. Identify two advantages of a computer-based system of maintaining stock cards.
- state two advantages of using perpetual stock.
- state two advantages of using physical stock.
- Hayley is concerned about 'stock loss' in her business.
- give four reasons why stock loss may occur.
- give two reasons as to how a stock gain may occur.

Hayley is unsure whether to use FIFO or identified cost in valuing stock. Answer the following questions.

1. explain what each of these terms mean
2. provide two advantages of using FIFO
3. provide two advantages of using identified cost



Financial Accounting Exercises

In addition

Hayley provides you with a list of transactions for December and asks you to prepare separate stock cards using each method. It is important that you have the correct balance from the stock card for the month of November.

Transactions

| | |
|---------|--|
| 13 Dec. | 20 bottles of 'Tabletop' bought for \$8. Invoice 890 |
| 6 | 6 bottles sold (cost \$7) Invoice 091 |
| 9 | 10 bottles sold (cost \$8) Invoice 092 |
| 14 | 2 bottles returned in (cost \$8) Credit note 033 |
| 22 | Drawings 3 bottles (cost \$7) |
| 27 | Donations 2 bottles (cost \$8) |

General journal entries for above transactions and other possibilities:

General journal

| | | |
|--|-----|-----|
| Advertising | 54 | |
| Stock control | 54 | 54 |
| Wine tastings | | |
| Donations | 18 | |
| Stock control | 18 | 18 |
| 2 bottles donated to charity | | |
| Drawings | 36 | |
| Stock control | | 36 |
| Stock withdrawn for personal use | | |
| 27 | 27 | |
| Stock control | | 27 |
| Stock revealed missing by physical stock take | | |
| Stock write down | 22 | |
| Stock control | | 22 |
| Stock write down | | |
| Stock control | XXX | |
| Capital | | XXX |
| Owner contributes stock to the business | | |



Financial Accounting Exercises

Solutions

Fun Run Enterprises - Exercise Resolution

Accounts reconstruction

It is necessary to reconstruct the following accounts to find missing figures. These amounts will be shown in bold.

- debtors
- advertising
- salaries
- interest
- accounts payable
- stock control

Reconstruction of accounts

Debtors

| | | | | | |
|---------|--------------|----------------|---------|------------------|----------------|
| 1 Jul. | Balance | 52 000 | 30 Jun. | Bank | 231 500 |
| 30 Jun. | Credit sales | 240 000 | | Discount expense | 500 |
| | | | | Bad debts | 2 000 |
| | | | | Sales returns | 3 000 |
| | | | | Balance | 55 000 |
| | | 292 000 | | | 292 000 |

Creditors

| | | | | | |
|---------|---------|----------------|---------|---------------|----------------|
| 30 Jun. | Bank | 242 400 | 1 Jul. | Balance | 20 000 |
| | Balance | 22 000 | 30 Jun. | Stock control | 244 400 |
| | | 264 400 | | | 264 400 |

Stock control

| | | | | | |
|---------|-----------|------------|---------|---------------|------------|
| 1 Jul. | Balance | 32 000 | 30 Jun. | Cost of sales | 240 000 |
| 30 Jun. | Creditors | 244 400 | | Stock loss | 2 400 |
| | | | | Balance | 34 000 |
| | | 276 | | | 276 |



Financial Accounting Exercises

| | | | | | |
|--|--|------------|--|--|------------|
| | | 400 | | | 400 |
|--|--|------------|--|--|------------|

Cost of sales

| | | | | | |
|---------|---------------|------------|---------|--------------------------------|---------|
| 30 Jun. | Stock control | 240 000 | 30 Jun. | Profit and Loss summary a/c | 240 000 |
|---------|---------------|------------|---------|--------------------------------|---------|

Advertising

| | | | | | |
|---------|------------------------|---------------|---------|------------------------|---------------|
| 1 Jul. | Prepaid advertising | 1 500 | 30 Jun. | Prepaid advertising | 2 000 |
| 30 Jun. | Bank | 16 000 | | Profit and Loss a/c | 15 500 |
| | | 17 500 | | | 17 500 |

Salaries

| | | | | | |
|---------|------------------|---------------|---------|---------------------|---------------|
| 30 Jun. | Bank | 60 000 | 30 Jun. | Accrued salaries | 4 400 |
| | Accrued salaries | 4 100 | | Profit and Loss a/c | 59 700 |
| | | 64 100 | | | 64 100 |

Interest expense

| | | | | | |
|---------|------------------|-------|---------|------------------------------------|-------|
| 30 Jun. | Accrued interest | 6 500 | 30 Jun. | Profit and Loss summary expense | 6 500 |
|---------|------------------|-------|---------|------------------------------------|-------|

It is also necessary to determine Capital at 1.7.2002; that is, $OE(P) = A - L$

Balance sheet

| | 1.7.2002 | 30.6.2003 |
|-------------------------------|-----------------|------------------|
| Assets | \$ | \$ |
| Bank | 11 000 | ? |
| Stock | 32 000 | 34 000 |
| Prepaid advertising | 1 500 | 2 000 |
| Debtors | 52 000 | 55 000 |
| Machinery | 80 000 | 80 000 |
| less accumulated depreciation | (4 000) | (12 000) |
| | 172 500 | |
| Liabilities | | |
| Creditors | 20 000 | 22 000 |
| Accrued salaries | 4 400 | 4 100 |
| Accrued interest | | 6 500 |
| Loan | 100 000 | 90 000 |
| | | |
| Owner's equity | | |
| Capital | 48 100 | ? |



Financial Accounting Exercises

Fun Run Enterprises

Cash budget for the year ending 30.6.2003

| | \$ | \$ |
|---------------------------------------|---------|---------|
| Bank balance 1.7.2002 | | 11 000 |
| Plus anticipated cash receipts | | |
| Receipts from debtors | 231 500 | |
| Cash sales | 160 000 | |
| | | 391 500 |
| | | 402 500 |
| Less anticipated cash payments | | |
| Payments to creditors | 242 400 | |
| Salaries | 60 000 | |
| Advertising | 16 000 | |
| Cleaning | 6 000 | |
| Loan repayment | 10 000 | |
| Drawings | 45 000 | |
| | | 379 400 |
| Bank balance 30.6.2003 | | 23 100 |

Fun Run Enterprises

Budgeted Profit and Loss statement for the year ending 30.6.2003

| | \$ | \$ |
|------------------------------|----------------|----------------|
| Cash sales | 160 000 | |
| Credit sales | 240 000 | |
| | 400 000 | |
| less sales returns | 3 000 | |
| | 397 000 | |
| less cost of sales | 240 000 | |
| Gross profit | | 157 000 |
| less stock loss | | 2 400 |
| Adjusted gross profit | | 154 600 |
| less expenses | | |
| Salaries | 59 700 | |
| Advertising | 15 500 | |
| Cleaning | 6 000 | |
| Depreciation of machinery | 8 000 | |
| Interest | 6 500 | |
| Bad debts | 2 000 | |
| Discount expense | 500 | |
| | | 98 200 |
| Net profit | | 56 400 |



Financial Accounting Exercises

Fun Run Enterprises

Budgeted balance sheet as at 30.6.2003

| Current assets | \$ | \$ |
|--------------------------------|----------------|----------------|
| Bank | 23 100 | |
| Stock | 34 000 | |
| Debtors | 55 000 | |
| Prepaid advertising | 2 000 | |
| | | 114 100 |
| Non-current assets | | |
| Machinery | 80 000 | |
| less accumulated depreciation | 12 000 | |
| | | 68 000 |
| Total assets | | 182 100 |
| Current liabilities | | |
| Creditors | 22 000 | |
| Loan | 10 000 | |
| Accrued salaries | 4 100 | |
| Accrued interest | 6 500 | |
| | | 42 600 |
| Non-current liabilities | | |
| Loan | | 80 000 |
| Owner's equity | | |
| Capital | 48 100 | |
| + Net profit | 56 400 | |
| | 104 500 | |
| Drawings | 45 000 | |
| | | 59 500 |
| Total equities | | 182 100 |

You will be assessed on your ability to separate cash and profit. In the problem above an example of:

- a receipt but not revenue is cash received from debtors
- revenue but not a receipt is credit sales
- a payment but not an expense is drawings or loan repayment an expense but not a payment is depreciation, discount expense, bad debts and stock loss



Financial Accounting Exercises

Task on variance analysis – Exercise Solution

Fun Run Enterprises

Cash budget for the year ending 30.6.2003

| | Budget | Actual | Variance | F/UF |
|---------------------------------------|----------------|---------|----------|------|
| | \$ | \$ | | |
| Bank balance 1.7.2002 | 11 000 | 11 000 | | |
| Plus anticipated cash receipts | | | | |
| Receipts from debtors | 231 500 | 234 000 | | |
| Cash sales | 160 000 | 155 000 | | |
| Loan | | 40 000 | | |
| | 391 500 | | | |
| | 402 500 | | | |
| Less anticipated cash payments | | | | |
| Payments to creditors | 242 400 | 245 000 | | |
| Salaries | 60 000 | 62 000 | | |
| Advertising | 16 000 | 17 000 | | |
| Cleaning | 6 000 | 7 000 | 1 000 | UF |
| Loan repayment | 10 000 | 15 000 | | |
| Drawings | 45 000 | 50 000 | | |
| Machinery | | 40 000 | | |
| | 379 400 | | | |
| Bank balance 30.6.2003 | 23 100 | | | |



Financial Accounting Exercises

Fun Run Enterprises

Budgeted Profit and Loss statement for the year ending 30.6.2003

| | Budget | Actual | Variance | F/UF |
|------------------------------|----------------|----------------|----------|------|
| | \$ | \$ | | |
| Cash sales | 160 000 | 155 000 | | |
| Credit sales | 240 000 | 260 000 | | |
| | 400 000 | 415 000 | | |
| less sales returns | 3 000 | 3 200 | | |
| | 397 000 | 411 800 | | |
| less cost of sales | 240 000 | 249 000 | | |
| Gross profit | 157 000 | 162 800 | | |
| less stock loss | 2 400 | 3 000 | | |
| Adjusted gross profit | 154 600 | 159 800 | | |
| less expenses | | | | |
| Salaries | 59 700 | 61 000 | | |
| Advertising | 15 500 | 17 500 | | |
| Cleaning | 6 000 | 7 000 | | |
| Depreciation of machinery | 8 000 | 12 000 | | |
| Interest | 6 500 | 8 000 | | |
| Bad debts | 2 000 | 4 000 | | |
| Discount expense | 500 | 100 | | |
| Machinery | | | | |
| | 98 200 | 109 600 | | |
| Net profit | 56 400 | | | |



Financial Accounting Exercises

Fun Run Enterprises

Budgeted balance sheet as at 30.6.2003

| | Budget | Actual | Variance | F/UF |
|--------------------------------|----------------|----------------|----------|------|
| | \$ | \$ | | |
| Current assets | | | | |
| Bank | 23 100 | | | |
| Stock | 34 000 | 36 000 | | |
| Debtors | 55 000 | 73 900 | | |
| Prepaid advertising | 2 000 | 1 000 | | |
| | 114 100 | | | |
| Non-current assets | | | | |
| Machinery | 80 000 | | | |
| less accumulated depreciation | 12 000 | | | |
| | 68 000 | | | |
| Total assets | 182 100 | | | |
| Current liabilities | | | | |
| | | | | |
| Creditors | 22 000 | 31 000 | | |
| Loan | 10 000 | 15 000 | | |
| Accrued salaries | 4 100 | 3 400 | | |
| Accrued interest | 6 500 | 8 000 | | |
| | 42 600 | | | |
| Non-current liabilities | | | | |
| Loan | 80 000 | 100 000 | | |
| Owner's equity | | | | |
| Capital | 48 100 | 48 100 | | |
| + Net profit | 56 400 | | | |
| | 104 500 | | | |
| Drawings | 45 000 | 50 000 | | |
| | 59 500 | | | |
| Total equities | 182 100 | | | |



Financial Accounting Exercises

Variance reports – Exercise Solution

Fun Run Enterprise

Cash budget for the year ending 30.6.2003

| | Budget | Actual | Variance | F/UF |
|---------------------------------------|----------------|----------------|--------------|-----------|
| | \$ | \$ | | |
| Bank balance 1.7.2002 | 11 000 | 11 000 | | |
| Plus anticipated cash receipts | | | | |
| Receipts from debtors | 231 500 | 234 000 | 2 500 | F |
| Cash sales | 160 000 | 155 000 | 5 000 | UF |
| Loan | | 40 000 | 40 000 | F |
| | 391 500 | 429 000 | 37 500 | F |
| | 402 500 | 440 000 | 37 500 | F |
| Less anticipated cash payments | | | | |
| Payments to creditors | 242 400 | 245 000 | 2 600 | UF |
| Salaries | 60 000 | 62 000 | 2 000 | UF |
| Advertising | 16 000 | 17 000 | 1 000 | UF |
| Cleaning | 6 000 | 7 000 | 1 000 | UF |
| Loan repayment | 10 000 | 15 000 | 5 000 | UF |
| Drawings | 45 000 | 40 000 | 5 000 | F |
| Machinery | | 40 000 | 40 000 | UF |
| | 379 400 | 426 000 | 46 600 | UF |
| Bank balance 30.6.2003 | 23 100 | 14 000 | 9 100 | UF |



Financial Accounting Exercises

Fun Run Enterprises

Budgeted Profit and Loss statement for the year ending 30.6.2003

| | Budget | Actual | Variance | F/UF |
|------------------------------|----------------|----------------|-----------------|-------------|
| | \$ | \$ | | |
| Cash sales | 160 000 | 155 000 | 5 000 | UF |
| Credit sales | 240 000 | 260 000 | 20 000 | F |
| | 400 000 | 415 000 | 15 000 | F |
| less sales returns | 3 000 | 3 200 | 200 | UF |
| | 397 000 | 411 800 | 14 800 | |
| less cost of sales | 240 000 | 249 000 | 9 000 | UF |
| Gross profit | 157 000 | 162 800 | 5 800 | |
| less stock loss | 2 400 | 3 000 | 600 | UF |
| Adjusted gross profit | 154 600 | 159 800 | 5 200 | |
| less expenses | | | | |
| Salaries | 59 700 | 61 000 | 1 300 | UF |
| Advertising | 15 500 | 17 500 | 2 000 | UF |
| Cleaning | 6 000 | 7 000 | 1 000 | UF |
| Depreciation of machinery | 8 000 | 12 000 | 4 000 | UF |
| Interest | 6 500 | 8 000 | 1 500 | UF |
| Bad debts | 2 000 | 4 000 | 2 000 | UF |
| Discount expense | 500 | 100 | 400 | F |
| | 98 200 | 109 600 | 11 400 | |
| Net profit | 56 400 | 50 200 | (6 200) | |



Financial Accounting Exercises

Fun Run Enterprises

Budgeted balance sheet as at 30.6.2003

| | Budget | Actual | Variance | F/UF |
|--------------------------------|----------------|----------------|---------------|------|
| | \$ | \$ | | |
| Current assets | | | | |
| Bank | 23 100 | 14 000 | 9 100 | UF |
| Stock | 34 000 | 36 000 | 2 000 | F |
| Debtors | 55 000 | 70 700 | 15 700 | F |
| Prepaid advertising | 2 000 | 1 000 | 1 000 | UF |
| | 114 100 | 121 700 | 7 600 | F |
| Non-current assets | | | | |
| Machinery | 80 000 | 120 000 | 40 000 | F |
| less accumulated depreciation | 12 000 | 16 000 | 4 000 | UF |
| | 68 000 | 104 000 | 36 000 | F |
| Total assets | 182 100 | 225 700 | 43 600 | F |
| Current liabilities | | | | |
| Bank | | | | |
| Creditors | 22 000 | 31 000 | 9 000 | UF |
| Loan | 10 000 | 25 000 | 15 000 | UF |
| Accrued salaries | 4 100 | 3 400 | 700 | F |
| Accrued interest | 6 500 | 8 000 | 1 500 | UF |
| | 42 600 | 67 400 | 24 800 | UF |
| Non-current liabilities | | | | |
| Loan | 80 000 | 100 000 | 20 000 | UF |
| Owner's equity | | | | |
| Capital | 48 100 | 48 100 | | |
| + Net profit | 56 400 | 50 200 | 6 200 | UF |
| | 104 500 | 98 300 | | |
| Drawings | 45 000 | 40 000 | 5 000 | F |
| | 59 500 | 58 300 | 1 200 | UF |
| Total equities | 182 100 | 225 700 | 43 600 | UF |



Financial Accounting Exercises

Cash flow statements – Exercise Solution

Stevens Computer Repairs

| Cash flow statement for the year ending 30 June 2003 | |
|---|-----------|
| Operating | \$ |
| Cash inflow | |
| Cash sales | 65 000 |
| Cash from Debtors | 40 000 |
| Commission | 400 |
| Cash outflow | |
| Wages | (37 500) |
| Rent | (2 200) |
| Computers purchased | (15 000) |
| Advertising | (10 000) |
| Other expenses | (13 000) |
| Net cash inflow from operations | 27 700 |
| Investing | |
| Cash outflow | |
| Motor vehicle | (15 000) |
| Financing | |
| Cash inflow | |
| Loan | 8 000 |
| Cash outflow | |
| Loan repayment | (2 000) |
| Net cash inflow from financing | 6 000 |
| Total net cash inflow | 18 700 |
| Plus bank 1 .7.2000 | 20 000 |
| Bank 30 .6.2003 | 38 700 |



Financial Accounting Exercises

Profit and Loss Statement for the year ending 30.6.2003

| | \$ | \$ |
|--------------------------------|--------|---------------|
| Cash sales | 65 000 | |
| Credit sales | 45 000 | |
| Commission | 600 | |
| | | 110 600 |
| Less expenses | | |
| Wages | 40 000 | |
| Depreciation on motor vehicles | 750 | |
| Rent | 2 400 | |
| Advertising | 8 000 | |
| Other expenses | 13 000 | |
| Materials | 13 600 | |
| | | 77 750 |
| Net profit | | 32 850 |

Balance sheet as at 30 June 2003

| | \$ | \$ |
|--------------------------------|--------|---------------|
| Current assets | | |
| Bank | 38 700 | |
| Debtors | 5 000 | |
| Accrued commission | 200 | |
| Stock of materials | 1 400 | |
| Prepaid advertising | 2 000 | |
| | | 47 300 |
| Non-current assets | | |
| Motor vehicle | 15 000 | |
| Less accumulated depreciation | 750 | |
| | | 14 250 |
| Total assets | | 61 550 |
| Current liabilities | | |
| Accrued rent | 200 | |
| Accrued wages | 2 500 | |
| | | 2 700 |
| Non-current liabilities | | |
| Loan | | 6 000 |
| Owner's equity | | |
| Capital | 20 000 | |
| + Net profit | 32 850 | |
| | | 52 850 |
| Total equities | | 61 550 |



Financial Accounting Exercises

Horse people – Exercise Solution

Horse people - Solution

| | Cash statement | Profit and Loss statement | Balance Sheet 1 Jan. | Balance Sheet 30 June |
|----------------------------|----------------|---------------------------|----------------------|-----------------------|
| Cash Sales - Whips | 20 000 | 20 000 | | |
| - Saddles | 10 000 | 10 000 | | |
| Credit sales - Whips | | 40 000 | | |
| - Saddles | | 20 000 | | |
| Cost of sales - Whips | 30 000 | 30 000 | | |
| Cost of sales - Saddles | | 15 000 | | |
| Stock of saddles - 1 Jan. | | | 3 500 | |
| Stock of saddles - 30 June | | | | 3 000 |
| Rent revenue | 1 600 | 2 400 | | |
| Advertising | 6 000 | 6 600 | | |
| Wages | 10 000 | 12 400 | | |
| Petrol | 2 000 | 2 000 | | |
| Depreciation of equipment | | 3 000 | | |
| Office expenses | 1 500 | 1 500 | | |
| Office salaries | 6 500 | 6 500 | | |
| Discount expense | | 900 | | |
| Bad debts | | 400 | | |
| Accounting expenses | 800 | 800 | | |
| Security expenses | 200 | 200 | | |
| Profit and Loss | | | | |
| Bank | | | 5 000 | 200) |
| Accrued rent revenue | | | | 800 |
| Debtors (cash received) | 59 200 | | 22 000 | 21 500 |
| Prepaid advertising | | | 6 000 | 5 400 |
| Equipment | 10 000 | | 30 000 | 40 000 |
| Accumulated. Depreciation | | | (10 000) | (13 000) |
| Accrued wages expense | | | | (2 400) |
| Creditors | 15 000 | | (14 000) | (13 500) |
| Loan | 1 000 | | (12 000) | (11 000) |
| Capital | 5 000 | | (28 400) | (33 400) |
| Profit and Loss | | 14 300 | | (14 300) |
| Drawings of cash | 18 000 | | | 18 000 |
| Surplus/deficit of cash | (5 200) | | | |



Financial Accounting Exercises

Ledger reconstructions

Debtors a/c

| | | | | | |
|---------|--------------|---------------|---------|------------------|---------------|
| 1 Jan. | Balance | 22 000 | 30 Jun. | Bad debts | 400 |
| 30 Jun. | Credit sales | 60 000 | | Discount expense | 900 |
| | | | | Bank | 59 200 |
| | | | | Balance | 21 500 |
| | | 82 000 | | | 82 000 |

Rent revenue

| | | | | | |
|---------|---------------------|--------------|---------|----------------------|--------------|
| | | | 30 Jun. | Bank | 1 600 |
| 30 Jun. | Profit and Loss a/c | 1 500 | | Accrued rent revenue | 800 |
| | | 2 400 | | | 2 400 |

Creditors

| | | | | | |
|---------|---------|---------------|---------|---------------|---------------|
| 30 Jun. | Bank | 15 000 | 1 Jan. | Balance | 14 000 |
| | Balance | 13 500 | 30 Jun. | Stock control | 14 500 |
| | | 28 500 | | | 28 500 |

Stock control

| | | | | | |
|---------|-----------|---------------|---------|---------------|---------------|
| 1 Jan. | Balance | 3 500 | 30 Jun. | Cost of sales | 15 000 |
| 30 Jun. | Creditors | 14 500 | | Balance | 3 000 |
| | | 18 000 | | | 18 000 |

Advertising

| | | | | | |
|---------|---------------------|---------------|---------|---------------------|---------------|
| 1 Jan. | Prepaid advertising | 6 000 | 30 Jun. | Prepaid advertising | 5 400 |
| 30 Jun. | Bank | 6 000 | | Profit and Loss a/c | |
| | | 12 000 | | | 12 000 |

Wages

| | | | | | |
|---------|------|--------|--|--|--|
| 30 Jun. | Bank | 10 000 | | | |
|---------|------|--------|--|--|--|



Financial Accounting Exercises

| | | | | | |
|--|---------------|---------------|---------|------------------------|---------------|
| | Accrued wages | 2 400 | 30 Jun. | Profit and Loss a/c | 12 400 |
| | | 12 400 | | | 12 400 |

Calculation of depreciation

$$\$30\,000 \times 20/100 \times 6/12 = \$3000$$

Cash flow statement for the six months ending 30 June

| | | |
|--|----------|-----------------|
| Operating activities | | |
| Cash inflow | | |
| Cash sales | 30 000 | |
| Receipts from debtors | 59 200 | |
| Rent revenue | 1 600 | |
| Cash outflow | | |
| Cost of sales | (30 000) | |
| Advertising | (6 000) | |
| Wages | (10 000) | |
| Petrol | (2 000) | |
| Office expenses | (1 500) | |
| Office salaries | (6 500) | |
| Accounting expenses | (800) | |
| Security expenses | (200) | |
| Payments to creditors | (15 000) | |
| Net cash inflow from operations | | 18 800 |
| Investing | | |
| Cash outflow | | |
| Buying of equipment | | (10 000) |
| Financing | | |
| Cash inflow | | |
| Capital | 5 000 | |
| Cash outflow | | |
| Drawings | (18 000) | |
| Loan repayment | (1 000) | |
| Net cash inflow from financing | | (14 000) |
| Total net cash inflow | | (5 200) |
| Bank balance 1 Jan. | | 5 000 |
| Bank balance 30 June | | (200) |



Financial Accounting Exercises

Departmental Profit and Loss statement for the six months ending 30 June

| | Whips | Saddles | Total |
|--------------------------------|---------------|---------------|---------------|
| Cash sales | 20 000 | 10 000 | 30 000 |
| Credit sales | 40 000 | 20 000 | 60 000 |
| | 60 000 | 30 000 | 90 000 |
| Less cost of goods sold | 30 000 | 15 000 | 45 000 |
| Gross margin | 30 000 | 15 000 | 45 000 |
| less direct expenses | | | |
| Advertising | 3 300 | 3 300 | 6 600 |
| Wages | 5 000 | 7 400 | 12 400 |
| Petrol | 200 | 1 800 | 2 000 |
| Depreciation of equipment | 1 200 | 1 800 | 3 000 |
| | 9 700 | 12 200 | 24 000 |
| Contribution margins | 20 300 | 700 | 21 000 |
| plus rent revenue | | | 2 400 |
| | | | 23 400 |
| less general expenses | | | |
| Administrative expenses | | | |
| Office expenses | | 1 500 | |
| Office salaries | | 6 500 | |
| Accounting expenses | | 800 | |
| Security expenses | | 200 | |
| | | | 9 000 |
| Financial expenses | | | |
| Discount expense | | 900 | |
| Bad debts | | 400 | |
| | | | 1 300 |
| Net profit | | | 13 100 |



Financial Accounting Exercises

Balance sheet as at 30 June

| | | |
|--------------------------------|--------|---------------|
| Current assets | | |
| Accrued rent revenue | 800 | |
| Debtors | 21 500 | |
| Stock 30 June | 3 000 | |
| Prepaid advertising | 5 400 | |
| | | 30 700 |
| Non-current assets | | |
| Equipment | 40 000 | |
| less accumulated depreciation | 13 000 | |
| | | 27 000 |
| Total assets | | 57 700 |
| Current liabilities | | |
| Accrued wages expense | 2 400 | |
| Bank (overdraft) | 200 | |
| Creditors | 13 500 | |
| Loan | 1 000 | |
| | | 17 100 |
| Non-current liabilities | | |
| Loan | | 10 000 |
| Owner's equity | | |
| Capital | 35 500 | |
| plus net profit | 13 100 | |
| | 48 600 | |
| less drawings | 18 000 | |
| | | 30 600 |
| Total equities | | 57 700 |

Strategies For Overcoming Common Errors In The Preparation Of Departmental Profit And Loss Statements

- identifying the length of the reporting period; that is, for the six months ending
- identify the actual revenue centers
- is the specific activity a trading or service activity? Do not be surprised if there is one of each
- alternatively one activity may use the physical inventory method whilst the other uses the perpetual approach
- show all titles; for example, contribution margin, net profit
- do not get confused between receipts from debtors and credit sales. You have to show credit sales and may have to reconstruct debtors and creditors to find credit sales and credit purchases, respectively
- if showing stock loss it must be measured at 'cost' not 'selling' price!
- when using the perpetual approach don't deduct stock on hand from 'cost of goods sold'
- be careful when calculating depreciation, make sure you match it with the length of the reporting period
- use a check sheet to ensure items are not omitted
- be prepared to fully classify the Profit and Loss statement



Financial Accounting Exercises

Departmental Profit and Loss statement A– Exercise solution

Case study – Departmental Profit and Loss statement - Solution

Media World

Profit and Loss statement for the month of November

| | VCR | TV | Total |
|------------------------------------|---------------|---------------|---------------|
| Cash sales | 20 000 | 10 000 | 30 000 |
| Credit sales | 30 000 | 15 000 | 45 000 |
| | 50 000 | 25 000 | 75 000 |
| less cost of goods sold | 25 000 | 12 500 | 37 500 |
| Gross profit | 25 000 | 12 500 | 37 500 |
| less stock loss | 500 | | 500 |
| adjusted gross profit | 24 500 | 12 500 | 37 000 |
| less direct expenses | | | |
| Selling expenses | | | |
| Wages | 4 000 | 2 000 | 6 000 |
| Advertising | 2 000 | 1 000 | 3 000 |
| | 6 000 | 3 000 | 9 000 |
| Workshop/servicing | | | |
| Workshop wages | | 4 000 | 4 000 |
| Service wages | 2 000 | | 2 000 |
| Depreciation of workshop equipment | | 360 | 360 |
| Rent | 1 000 | 1 000 | 2 000 |
| | 3 000 | 5 360 | 8 360 |
| Direct expenses total | 9 000 | 8 360 | 17 360 |
| Contribution margin | 15 500 | 4 140 | 19 640 |
| less general expenses | | | |
| Office expense | | | |
| Office wages | | 4 000 | |
| Cleaning | | 2 000 | |
| Rent | | 1 000 | |
| | | | 7 000 |
| Finance expenses | | | |
| Bad debts | | 1 000 | |
| Interest on overdraft | | 100 | |
| Interest on loan | | 300 | |
| | | | 1 400 |
| | | | 8 400 |
| Net profit | | | 11 240 |



Financial Accounting Exercises

Cash versus profit – Case Study Solution

Reconstruction of accounts

Debtors

| | | | | | |
|---------|--------------|---------------|---------|------------------|---------------|
| 1 Jan. | Balance | 5 400 | 30 Jun. | Bank | 76 000 |
| 30 Jun. | Credit sales | 80 000 | | Discount expense | 800 |
| | | | | Sales returns | 1 000 |
| | | | | Balance | 7 600 |
| | | 85 400 | | | 85 400 |

Creditors

| | | | | | |
|---------|---------|---------------|---------|---------------|---------------|
| 30 Jun. | Bank | 74 000 | 1 Jan. | Balance | 6 000 |
| | Balance | 5 500 | 30 Jun. | Stock control | 73 500 |
| | | 79 500 | | | 79 500 |

Stock control

| | | | | | |
|---------|-----------|---------------|---------|---------------|---------------|
| 30 Jun. | Creditors | 73 500 | 30 Jun. | Cost of sales | 70 000 |
| | | | | Balance | 3 500 |
| | | 73 500 | | | 73 500 |

Cost of sales

| | | | | | |
|---------|---------------|--------|---------|-----------------------------|--------|
| 30 Jun. | Stock control | 70 000 | 30 Jun. | Profit and Loss summary a/c | 70 000 |
|---------|---------------|--------|---------|-----------------------------|--------|

Prepaid rent expense

| | | | | | |
|--------|---------|--------------|---------|--------------|--------------|
| 1 Jan. | Balance | 2 000 | 30 Jun. | Rent expense | 1 200 |
| | | | | Balance | 800 |
| | | 2 000 | | | 2 000 |

Rent expense

| | | | | | |
|---------|----------------------|-------|---------|---------------------------------|-------|
| 30 Jun. | Prepaid rent expense | 1 200 | 30 Jun. | Profit and Loss summary expense | 1 200 |
|---------|----------------------|-------|---------|---------------------------------|-------|



Financial Accounting Exercises

Disposal of asset

Vehicles

| | | | | | |
|--------|---------|---------------|---------|---------------------|---------------|
| 1 Jan. | Balance | 30 000 | 1 Jan. | Disposal of vehicle | 30 000 |
| | Bank | 45 000 | 30 Jun. | Balance | 45 000 |
| | | 75 000 | | | 75 000 |

Accumulated depreciation of vehicles

| | | | | | |
|---------|----------------------|---------------|---------|--------------------------|---------------|
| 1 Jan. | Disposal of vehicles | 15 000 | 1 Jan. | Balance | 15 000 |
| 30 Jun. | Balance | 2 700 | 30 Jun. | Depreciation of Vehicles | 2 700 |
| | | 17 700 | | | 17 700 |

Disposal of vehicles

| | | | | | |
|--------|----------|---------------|--------|--------------------------------------|---------------|
| 1 Jan. | Vehicles | 30 000 | 1 Jan. | Accumulated Depreciation of vehicles | 15 000 |
| | | | | Bank | 13 500 |
| | | | | Loss on sale | 1 500 |
| | | 30 000 | | | 30 000 |

Loss on sale

| | | | | | |
|--------|----------------------|-------|---------|-----------------------------|-------|
| 1 Jan. | Disposal of vehicles | 1 500 | 30 Jun. | Profit and Loss summary a/c | 1 500 |
|--------|----------------------|-------|---------|-----------------------------|-------|

Depreciation calculation

Vehicles $\$45\,000 \times 12/100 \times 6/12 = \2700



Financial Accounting Exercises

Departmental profit and loss statement B- Exercise Solution

Matts World

Departmental Profit and Loss statement for the month of November

| Bicycle sales | \$ | \$ | \$ |
|------------------------------------|-----------|-----------|---------------|
| Revenue | | | |
| Cash sales | 40 000 | | |
| Credit sales | 60 000 | | |
| | | 100 000 | |
| less cost of goods sold | | 50 000 | |
| Gross profit | | 50 000 | |
| less stock loss | | 1 500 | |
| adjusted gross profit | | 48 500 | |
| less direct expenses | | | |
| Wages | 4 200 | | |
| Advertising | 3 600 | | |
| Delivery costs | 1 800 | | |
| Rent | 800 | | |
| | | 10 400 | |
| Contribution margin | | | 38 100 |
| Bicycle repairs | | | |
| Revenue | | | |
| Cash fees | | 20 000 | |
| Less direct expenses | | | |
| Wages | 6 300 | | |
| Depreciation of workshop equipment | 720 | | |
| Rent | 800 | | |
| Advertising | 2 400 | | |
| | | 10 220 | |
| Contribution margin | | | 9 780 |
| Total contribution margin | | | 47 880 |
| less general expenses | | | |
| Office expenses | | | |
| Office wages | 4 200 | | |
| Cleaning | 500 | | |
| Rent | 800 | | |
| | | 5 500 | |
| Finance expenses | | | |
| Bad debts | 600 | | |
| Interest on overdraft | 600 | | |
| Interest on loan | 1 600 | | |
| Interest on mortgage | 4 000 | | |
| | | 6 800 | |
| | | | 12 300 |
| Net profit | | | 35 580 |



Financial Accounting Exercises

A stock control problem – Exercise Solution

Stock card

Item: Walkmans

| Date | Particulars | IN | | OUT | | BALANCE | | |
|--------|-------------|-----|------|-----|------|---------|------|-------|
| | | Qty | Unit | Qty | Unit | Qty | Unit | Total |
| 1 Oct. | Balance | | | | | 4 | 70 | 280 |
| 6 | Inv. 161 | 3 | 72 | | | 4 | 70 | 280 |
| | | | | | | 3 | 72 | 216 |
| 10 | Rec. 200 | | | 1 | 70 | 3 | 70 | 210 |
| | | | | 1 | 72 | 2 | 72 | 144 |
| 13 | Drawings | | | 1 | 72 | 3 | 70 | 210 |
| | | | | | | 1 | 72 | 72 |
| 18 | CN 29 | 1 | 70 | | | 4 | 70 | 280 |
| | | | | | | 1 | 72 | 72 |
| 20 | Rec. 213 | | | 3 | 70 | 1 | 70 | 70 |
| | | | | | | 1 | 72 | 72 |
| 22 | Inv. 302 | 6 | 72 | | | 1 | 70 | 70 |
| | | | | | | 7 | 72 | 504 |
| 24 | Advertising | | | 1 | 72 | 1 | 70 | 70 |
| | | | | | | 6 | 72 | 432 |
| 31 | Rec. 299 | | | 2 | 72 | 1 | 70 | 70 |
| | | | | | | 4 | 72 | 288 |
| | Stock loss | | | 1 | 72 | 1 | 70 | 70 |
| | | | | | | 3 | 72 | 216 |

Stock control

| Date | Particulars | \$ | Date | Particulars | \$ |
|--------|---------------|------------|---------|---------------|------------|
| 1 Oct. | Balance | 280 | 31 Oct. | Drawings | 72 |
| 31 | Cost of sales | 70 | | Advertising | 72 |
| | Creditors | 648 | | Cost of sales | 496 |
| | | | | Stock loss | 72 |
| | | | | Balance | 286 |
| | | 998 | | | 998 |

You will notice that the closing balance in the stock card agrees with the balance in the stock control account.

Stock write down

The application of the principle of conservatism means that stock is valued at the 'lower of cost and net realisable value'. In the example above the closing stock has two cost values, \$70 and \$72. It may be the case that the net realisable value is lower than the cost of the stock. This happens, for instance, when items of stock become out of fashion, are obsolete or are replaced by superior items.

In the example, assume the Walkmans now have a net realisable value of \$65. Therefore the stock has to be 'written down'. It is due to the application of the principle of conservatism that states that revenue shall not be recognised until earned, however, losses should be recognised as soon as they are anticipated.



Financial Accounting Exercises

The consequence of the application of this rule applies to:

- the stock card
- general journal
- stock control account
- Profit and Loss statement
- balance sheet

Extract of Stock card (Identified cost)

| Date | Particulars | IN | | OUT | | BALANCE | | |
|---------|------------------|-----|------|-----|------|---------|------|-------|
| | | Qty | Unit | Qty | Unit | Qty | Unit | Total |
| 31 Oct. | Rec. 299 | | | 2 | 72 | 1 | 70 | 70 |
| | | | | | | 4 | 72 | 288 |
| | Stock loss | | | 1 | 72 | 1 | 70 | 70 |
| | | | | | | 3 | 72 | 216 |
| | Stock write down | | | 1 | 5 | | | |
| | | | | 3 | 7 | 4 | 65 | 260 |

General journal

| Date | Particular | \$ | \$ |
|---------|---------------------------------|----|----|
| 31 Oct. | Stock write down | 26 | |
| | Stock Control account | | 26 |
| | Adjustment for anticipated loss | | |

Stock control

| Date | Particular | \$ | Date | Particular | \$ |
|--------|---------------|------------|---------|------------------|------------|
| 1 Oct. | Balance | 280 | 31 Oct. | Drawings | 72 |
| 31 | Cost of sales | 70 | | Advertising | 72 |
| | Creditors | 648 | | Cost of sales | 496 |
| | | | | Stock loss | 72 |
| | | | | Stock write down | 26 |
| | | | | Balance | 260 |
| | | 998 | | | 998 |

extract of Profit and Loss statement

| | | |
|------------------|-----------|-------|
| Gross profit | | xxxxx |
| less Stock loss | 72 | |
| Stock write down | <u>26</u> | |
| | | 98 |

extract of balance sheet

| | |
|----------------|--------------------------------------|
| Current assets | |
| Stock 31 Oct. | 260 (i.e. net of the amount of \$26) |



Financial Accounting Exercises

Perpetual stock - Exercise Solution

November and December Stock card entries - Solution

Stock card for November

Item: Tabletop

| Date | Particulars | IN | | OUT | | BALANCE | | |
|--------|------------------|-----|------|-----|------|---------|------|-------|
| | | Qty | Unit | Qty | Unit | Qty | Unit | Total |
| 1 Nov. | Balance | | | | | 10 | 9 | 90 |
| 12 | Inv. 099 | 25 | 9 | | | 35 | 9 | 315 |
| 16 | Inv. 211 | | | 7 | 9 | 28 | 9 | 252 |
| 23 | CN 96 | | | 2 | 9 | 26 | 9 | 234 |
| 30 | Advertising | | | 6 | 9 | 20 | 9 | 180 |
| | Donations | | | 2 | 9 | 18 | 9 | 162 |
| | Drawings | | | 4 | 9 | 14 | 9 | 126 |
| | Stock loss | | | 3 | 9 | 11 | 9 | 99 |
| | Stock write down | | | 10 | 1 | 12 | 7 | 84 |

Stock card for December

Item: Tabletop

| Date | Particulars | IN | | OUT | | BALANCE | | |
|--------|------------------|-----|------|-----|------|---------|------|-------|
| | | Qty | Unit | Qty | Unit | Qty | Unit | Total |
| 1 Dec. | Balance | | | | | 11 | 7 | 77 |
| 3 | Inv. 890 | 20 | 8 | | | 11 | 7 | 77 |
| | | | | | | 20 | 8 | 160 |
| 6 | Inv. 091 | | | 6 | 7 | 5 | 7 | 35 |
| | | | | | | 20 | 8 | 160 |
| 9 | Inv. 092 | | | 10 | 8 | 5 | 7 | 35 |
| | | | | | | 10 | 8 | 80 |
| 14 | CN 033 | 2 | 8 | | | 5 | 7 | 35 |
| | | | | | | 12 | 8 | 96 |
| 22 | Drawings | | | 3 | 7 | 2 | 7 | 14 |
| | | | | | | 12 | 8 | 96 |
| 27 | Donations | | | 2 | 8 | 2 | 7 | 14 |
| | | | | | | 10 | 8 | 80 |
| 31 | Stock write down | | | 11 | 2 | 11 | 7 | 77 |

