

Catherine Coucom

Cambridge IGCSE® and O Level

# Accounting

Coursebook

Second edition

Completely Cambridge  
Cambridge resources  
for  
Cambridge qualifications

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# Chapter 8

## Financial statements – Part A

### Learning objectives

*In this chapter you will learn to:*

- explain the advantages and disadvantages of operating as a sole trader 5.1
- explain the importance of preparing income statements 5.1
- explain the difference between a trading business and a service business 5.1
- prepare income statements for trading businesses and for service businesses 5.1
- make adjustments for goods taken by the owner for own use 5.1
- balance ledger accounts as required and make transfers to financial statements. 2.1

## 8.1 Introduction

All the previous chapters have covered the book-keeping records maintained by a sole trader. Similar records will be maintained by other types of businesses.

When a person is operating a business alone as a sole trader, he/she is entitled to all the profits the business makes, but will be responsible for any losses the business makes. Business decisions may be made quickly, as consultation is not necessary, but there is no one with whom to share the decision-making or the workload. The capital of the business will be restricted to what the trader is able to invest, whereas other forms of business have access to capital invested by other owners of the business.

When a person starts a business his/her aim is to make a profit. The profit (or loss) is calculated in the financial statements which are usually prepared at the end of each financial year. Financial statements basically consist of two parts:

- 1 An **income statement** which consists of two sections:
  - a **trading section** in which the **gross profit** of the business is calculated
  - a **profit and loss section** in which the **profit for the year** of the business is calculated.

The trading section and the profit and loss section of the income statement are part of the double entry system.

- 2 A **statement of financial position** shows the **assets and liabilities** of the business at a certain date. The statement of financial position is not part of the double entry system.

Financial statements are usually prepared from a trial balance. **Every item in a trial balance appears once in a set of financial statements.** As each item is used, it is useful to place a tick (✓) against the item. This ensures that no items are overlooked.

It is common to find notes accompanying a trial balance about various adjustments which are to be made (these are explained in the following chapters). **Any notes to a trial balance are used twice in a set of financial statements.** To ensure that this is done, it is useful to place a tick (✓) against the notes each time they are used.



LINK

You will learn about partnerships and limited companies in Chapters 19 and 21.



KEY TERM

An **income statement** is a statement prepared for a trading period to show the gross profit and profit for the year.



LINK

You will learn more about statements of financial position in Chapter 9.



TIP

Tick off the items from a trial balance and the notes to a trial balance as you use them so that nothing is omitted.



TIP

Every item in a trial balance is used once within a set of financial statements; any notes to a trial balance are used twice within a set of financial statements.

**Walkthrough 8.1**

The following trial balance was extracted from the books of Samir at 31 May 20–8.

This trial balance will be used in **Walkthrough 8.2** to **Walkthrough 8.7**.

| Samir                        |                |                |
|------------------------------|----------------|----------------|
| Trial balance at 31 May 20–8 |                |                |
|                              | Dr             | Cr             |
|                              | \$             | \$             |
| Revenue                      |                | 95 700         |
| Sales returns                | 1 000          |                |
| Purchases                    | 65 000         |                |
| Purchases returns            |                | 500            |
| Carriage inwards             | 1 500          |                |
| Inventory 1 Jun 20–8         | 7 100          |                |
| Discount received            |                | 400            |
| Discount allowed             | 900            |                |
| Wages                        | 11 200         |                |
| General expenses             | 2 800          |                |
| Property tax                 | 600            |                |
| Loan interest                | 500            |                |
| Premises                     | 80 000         |                |
| Fixtures and equipment       | 13 900         |                |
| Trade receivables            | 7 500          |                |
| Trade payables               |                | 7 800          |
| Bank                         | 3 300          |                |
| Cash                         | 100            |                |
| Long-term loan               |                | 10 000         |
| Capital                      |                | 90 000         |
| Drawings                     | 9 000          |                |
|                              | <u>204 400</u> | <u>204 400</u> |

**TIP**

The term 'revenue' is used instead of 'sales' in a trial balance and in an income statement.

- The inventory at 31 May 20–8 was valued at \$7 600.
- During the year ended 31 May 20–8, Samir took goods costing \$300 for his own use. No entries have been made in the accounting records.

## 8.2 Trading section of the income statement

The **trading section** is concerned with buying and selling, and its purpose is to calculate the profit earned on the goods sold. This is known as the **gross profit**. The formula for calculating gross profit is:

$$\text{Gross profit} = \text{Selling price of goods} - \text{Cost of sales}$$

The selling price represents the total sales less any sales returns.

The cost of sales represents the total cost of the goods actually sold. This is not necessarily the cost of goods purchased during the year: some goods may have been in stock at the start of the year, and some of the goods purchased during the year may remain unsold at the end of the year. The formula for calculating cost of sales is:

$$\text{Cost of sales} = \text{Opening inventory} + \text{Purchases} - \text{Closing inventory}$$

The purchases figure represents the total cost of purchases less any purchases returns. If carriage inwards has been paid on goods purchased this must be added to the purchases as it increases the cost of the goods. If the owner of the business has withdrawn goods for personal use the cost of these is credited to the purchases account, so reducing the cost of goods available for sale. If goods taken by the owner have not already been recorded they must be deducted from the purchases. The formula for calculating the net purchases figure is:

$$\text{Net purchases} = \text{Purchases} - \text{Purchases returns} + \text{Carriage inwards} - \text{Goods for own use}$$

The calculation of gross profit is shown in the trading section of the income statement. This must have a heading which includes the period of time covered by the statement. It is also usual to include the name under which the business trades.



### KEY TERM

The **gross profit** is the difference between the selling price and the cost of those goods.

### TEST YOURSELF 8.1

- 1 State what is calculated in:
  - a a trading account section of an income statement
  - b a profit and loss account section of an income statement.
- 2 State the formula for calculating gross profit.
- 3 State the formula for calculating cost of sales.

There are two ways in which a trading section of an income statement can be prepared – **horizontal** and **vertical**.

The **horizontal format** is similar to a traditional ledger account. Using this method, the revenue is shown on the credit side and the cost of sales on the debit side. The difference (or balance) between the two sides equals the gross profit.

**Walkthrough 8.2**

Using the trial balance and accompanying notes shown in **Walkthrough 8.1**, prepare the trading section of the income statement of Samir for the year ended 31 May 20–8. Use the horizontal format.

| Samir   |              |               |                    |              |               |
|---|--------------|---------------|--------------------|--------------|---------------|
| Income statement (trading section) for the year ended 31 May 20–8 |              |               |                    |              |               |
|   | \$           | \$            |                    | \$           | \$            |
| Opening inventory   |              | 7 100         | Revenue            | 95 700       |               |
| Purchases   | 65 000       |               | Less Sales returns | <u>1 000</u> | 94 700        |
| Less Purchases returns  | <u>500</u>   |               |                    |              |               |
|   | 64 500       |               |                    |              |               |
| Less Goods for own use  | <u>300</u>   |               |                    |              |               |
|   | 64 200       |               |                    |              |               |
| Carriage inwards  | <u>1 500</u> | 65 700        |                    |              |               |
|   |              | 72 800        |                    |              |               |
| Less Closing inventory  |              | <u>7 600</u>  |                    |              |               |
| Cost of sales   |              | 65 200        |                    |              |               |
| Gross profit c/d  |              | <u>29 500</u> |                    |              |               |
|   |              | <u>94 700</u> |                    |              | <u>94 700</u> |

- As these items are entered in the trading section of the income statement, they should be ticked-off in the trial balance and accompanying notes.
- The gross profit is carried down to the profit and loss section (see Section 8.3).
- The first money column on each side has been used for adding and subtracting items and the final column had been used for the section total.

A trading section of an income statement can also be prepared using the **vertical format**. This is the format used by most businesses. A statement prepared using this method contains the same information as a horizontal account, but looks like an arithmetic calculation.

**Walkthrough 8.3**

Using the trial balance and accompanying notes shown in **Walkthrough 8.1**, prepare the trading section of the income statement of Samir for the year ended 31 May 20–8. Use the vertical format.

| Samir   |              |              |               |
|---|--------------|--------------|---------------|
| Income statement (Trading Section) for the year ended 31 May 20–8 |              |              |               |
|   | \$           | \$           | \$            |
| Revenue   |              | 95 700       |               |
| Less Sales returns  |              | <u>1 000</u> | 94 700        |
| Less Cost of sales  |              |              |               |
| Opening inventory   |              | 7 100        |               |
| Purchases   | 65 000       |              |               |
| Less Purchases returns  | <u>500</u>   |              |               |
|   | 64 500       |              |               |
| Less Goods for own use  | <u>300</u>   |              |               |
|   | 64 200       |              |               |
| Carriage inwards  | <u>1 500</u> | 65 700       |               |
|   |              | 72 800       |               |
| Less Closing inventory  |              | <u>7 600</u> | 65 200        |
| Gross profit  |              |              | <u>29 500</u> |

- The first two money columns have been used for adding and subtracting items and the final column for the final section total. For example, the first column has been used to adjust the purchases for returns, carriage and goods for own use and the final cost of purchases has been entered in the second column.

You can now answer Questions 1 and 2 at the end of this chapter.

### 8.3 Profit and loss section of the income statement

The **profit and loss** section of an income statement is concerned with profits and losses, gains and expenses. Its purpose is to calculate the final profit after all running expenses and other items of income. This is known as the **profit for the year**. The formula for calculating profit for the year is:

$$\text{Profit for the year} = \text{Gross profit} + \text{Other income} - \text{Expenses}$$

The profit and loss section of an income statement must have a heading which includes the period of time covered by the statement. It is also usual to include the name under which the business trades.

As with a trading section of an income statement, a profit and loss section can be prepared using either the **horizontal** or the **vertical** method. Using the horizontal format, the gross profit and any other income are shown on the credit side and the expenses are shown on the debit side. The difference (or balance) between the two sides equals the **profit for the year** (if the credit side is the largest) or the **loss for the year** (if the debit side is the largest).

#### Walkthrough 8.4

Using the trial balance and accompanying notes shown in **Walkthrough 8.1**, prepare the profit and loss section of the income statement of Samir for the year ended 31 May 20–8. Use the horizontal format.



#### KEY TERM

The **profit for the year** is the final profit after any other income has been added to the gross profit and the running expenses have been deducted.

| Samir   |    |               |                   |               |
|---|----|---------------|-------------------|---------------|
| Income statement (profit and loss section) for the year ended 31 May 20–8 |    |               |                   |               |
|   | \$ | \$            |                   | \$            |
| Discount allowed  |    | 900           | Gross profit      | b/d 29 500    |
| Wages   |    | 11 200        | Discount received | 400           |
| General expenses  |    | 2 800         |                   |               |
| Property tax  |    | 600           |                   |               |
| Loan interest   |    | 500           |                   |               |
| Profit for the year   |    | <u>13 900</u> |                   |               |
|   |    | <u>29 900</u> |                   | <u>29 900</u> |

- As these items are entered in the profit and loss section of the income statement they should be ticked-off in the trial balance and accompanying notes.
- The gross profit is brought down from the trading section where it was calculated.

A profit and loss section of an income statement can also be prepared using the vertical format. This format is used by most businesses. A statement prepared using this method contains the same information but looks like an arithmetic calculation.

### Walkthrough 8.5

Using the trial balance and accompanying notes shown in **Walkthrough 8.1**, prepare the profit and loss section of the income statement of Samir for the year ended 31 May 20–8. Use the vertical format.

| Samir   |    |            |               |
|---|----|------------|---------------|
| Income statement (profit and loss section) for the year ended 31 May 20–8 |    |            |               |
|   | \$ | \$         | \$            |
| Gross profit  |    |            | 29 500        |
| Add Discount received   |    |            | <u>400</u>    |
|   |    |            | 29 900        |
| Less Discount allowed   |    | 900        |               |
| Wages   |    | 11 200     |               |
| General expenses  |    | 2 800      |               |
| Property tax  |    | <u>600</u> | <u>15 500</u> |
| Profit from operations  |    |            | 14 400        |
| Less Loan interest  |    | <u>500</u> | <u>13 900</u> |
| Profit for the year   |    |            | <u>13 900</u> |

- Using the vertical presentation it is easy to show the profit earned from the normal trading or operating activities and then final profit for the year after the deduction of any finance costs.

**TEST YOURSELF 8.2**

- 1 Suggest **six** business expenses (excluding those shown in the walkthroughs).
- 2 State the formula for calculating profit for the year.

The two sections of the income statement are usually presented in the form of one combined statement, which is normally presented in vertical format. The profit and loss section follows on immediately after the trading section, with the words ‘gross profit’ being written only once. The heading of the income statement includes the period of time covered by the statement and the name under which the business trades.

As most businesses prepare their income statements using the vertical format this method will be followed in the remainder of this book.

**Walkthrough 8.6**

Using either the trial balance and accompanying notes shown in **Walkthrough 8.1** or the separate sections of the income statement prepared in **Walkthroughs 8.3** and **8.5**, prepare the income statement of Samir for the year ended 31 May 20–8.

| Samir   |              |               |               |
|---|--------------|---------------|---------------|
| Income statement for the year ended 31 May 20–8 |              |               |               |
|   | \$           | \$            | \$            |
| Revenue   |              | 95 700        |               |
| Less Sales returns                              |              | <u>1 000</u>  | 94 700        |
| Less Cost of sales                              |              |               |               |
| Opening inventory                               |              | 7 100         |               |
| Purchases                                       | 65 000       |               |               |
| Less Purchases returns                          | <u>500</u>   |               |               |
|   | 64 500       |               |               |
| Less Goods for own use                          | <u>300</u>   |               |               |
|   | 64 200       |               |               |
| Carriage inwards                                | <u>1 500</u> | 65 700        |               |
|   |              | <u>72 800</u> |               |
| Less Closing inventory                          |              | 7 600         | 65 200        |
| Gross profit                                    |              |               | <u>29 500</u> |
| Add Discount received                           |              |               | <u>400</u>    |
|   |              |               | 29 900        |
| Less Discount allowed                           |              | 900           |               |
| Wages   | 11 200       |               |               |
| General expenses                                | 2 800        |               |               |
| Property tax                                    | <u>600</u>   |               | 15 500        |
| Profit from operations                          |              |               | <u>14 400</u> |
| Less Loan interest                              |              | <u>500</u>    |               |
| Profit for the year                             |              |               | <u>13 900</u> |



You will learn more about income statements in Chapters 11, 12 and 13.

You can now answer Questions 3 and 4 at the end of this chapter.



**d**

| Wages account |               |       |               |        |                  |       |               |
|---------------|---------------|-------|---------------|--------|------------------|-------|---------------|
| Date          | Details       | Folio | \$            | Date   | Details          | Folio | \$            |
| 20–8          |               |       |               | 20–8   |                  |       |               |
| May 31        | Total to date |       | 11 200        | May 31 | Income statement |       | 11 200        |
|               |               |       | <u>11 200</u> |        |                  |       | <u>11 200</u> |

- The entries shown as ‘totals to date’ represent the total of the individual entries made in the account for the year ended 31 May 20–8.
- All the other items in the income statement (excluding inventory, gross profit and profit for the year) have similar transfers from the appropriate ledger accounts.
- The gross profit technically has a double entry within the income statement as it is transferred from the trading account section to the profit and loss account section (refer to **Walkthroughs 8.2 and 8.4**).
- The entries for inventory and profit for the year are explained next.

There are two entries for inventory in the income statement – the inventory at the start of the year and the inventory at the end of the year. The inventory account will have a debit balance representing the inventory at the start of the year – this is credited to the inventory account and transferred to the debit of the income statement. The inventory at the end of the year is shown as a deduction from the debit entries in the income statement (which is equal to a credit entry), so this must be debited in the inventory account.

### Walkthrough 8.8

Using the income statement prepared for Samir in **Walkthrough 8.6**, prepare the inventory account in Samir’s ledger on 31 May 20–8.

| Samir<br>Nominal ledger<br>Inventory account |                  |       |              |        |                  |       |              |
|--|------------------|-------|--------------|--------|------------------|-------|--------------|
| Date   | Details          | Folio | \$           | Date   | Details          | Folio | \$           |
| 20–7   |                  |       |              | 20–8   |                  |       |              |
| Jun 1  | Balance          | b/d   | 7 100        | May 31 | Income statement |       | 7 100        |
|  |                  |       | <u>7 100</u> |        |                  |       | <u>7 100</u> |
| 20–8   |                  |       |              |        |                  |       |              |
| May 31                                       | Income statement |       | 7 600        |        |                  |       |              |

- The entry of \$7 600 on the debit side, representing the inventory at the end of the financial year on 31 May 20–8, becomes the opening inventory for the year beginning 1 June 20–8.

A profit for the year represents the return on the owner’s investment. This will appear as a debit entry in the income statement and should be transferred to the credit of the capital account as it increases the amount the business owes the owner. A loss for the year will



#### TIP

The income statement consists of the trading account and the profit and loss account which are part of the double entry system.

appear as a credit entry in the income statement and should be transferred to the debit of the capital account as it reduces the amount the business owes the owner.

As explained in Chapter 2, the total of the drawings account is transferred to the capital account at the end of the year.

### Walkthrough 8.9

On 1 June 20–7 the credit balance on Samir’s capital account was \$90 000. During the year ended 31 May 20–8 he had withdrawn \$9 000 in cash and \$300 in goods. His profit for the year ended 31 May 20–8 was \$13 900.

Prepare the capital account and the drawings account in Samir’s ledger on 31 May 20–8.

| Samir<br>Nominal ledger<br>Capital account |          |       |                |        |         |       |                |
|--|----------|-------|----------------|--------|---------|-------|----------------|
| Date                                       | Details  | Folio | \$             | Date   | Details | Folio | \$             |
| 20–8                                       |          |       |                | 20–7   |         |       |                |
| May 31                                     | Drawings |       | 9 300          | Jun 1  | Balance | b/d   | 90 000         |
|  | Balance  | c/d   | 94 600         | 20–8   |         |       |                |
|  |          |       |                | May 31 | Profit  |       | 13 900         |
|  |          |       | <u>103 900</u> |        |         |       | <u>103 900</u> |
|  |          |       |                | 20–8   |         |       |                |
|  |          |       |                | Jun 1  | Balance | b/d   | 94 600         |

| Drawings account |               |       |              |        |         |       |              |
|------------------|---------------|-------|--------------|--------|---------|-------|--------------|
| Date             | Details       | Folio | \$           | Date   | Details | Folio | \$           |
| 20–8             |               |       |              | 20–8   |         |       |              |
| May 31           | Total to date |       |              | May 31 | Capital |       | 9 300        |
|                  | Cash          |       | 9 000        |        |         |       |              |
|                  | Purchases     |       | <u>300</u>   |        |         |       |              |
|                  |               |       | <u>9 300</u> |        |         |       | <u>9 300</u> |



**TIP**

If a business makes a profit it is credited to the capital account as it increases the owner’s capital. If a business makes a loss it is debited to the capital account as it reduces the owner’s capital.

#### TEST YOURSELF 8.3

- 1 Explain why it is necessary to make two transfers from the income statement to the inventory account at the end of the financial year.
- 2 Explain why a loss for the year is debited to the owner’s capital account.

You can now answer Question 5 at the end of this chapter.

## 8.5 Income statement of a service business

A **service business** is one which does not buy and sell goods, such as an accountant, an insurance company, a travel agent, a hairdresser and so on. At the end of the financial year, these businesses still need to prepare financial statements. However, the trading account section of the income statement is not prepared as no goods are bought and sold. Only the profit and loss section of the income statement and a statement of financial position are prepared.

In the income statement all the items of revenue receivable such as fees from clients, commission and other income are credited and expenses are debited. The statement of financial position is exactly the same as the statement of financial position of a **trading business**.



### KEY TERMS

A **service business** is one which provides a service.

A **trading business** is one which buys and sells goods.

### Walkthrough 8.10

Anita is a business consultant. She provided the following information at the end of her financial year on 30 September 20–5.

|                         | \$     |
|-------------------------|--------|
| Property tax            | 6 400  |
| General expenses        | 8 950  |
| Insurance               | 2 670  |
| Printing and stationery | 4 560  |
| Loan interest           | 1 500  |
| Wages                   | 43 500 |
| Rent receivable         | 7 300  |
| Commissions received    | 92 150 |

- a** Prepare the income statement for Anita for the year ended 30 September 20–5. Use the horizontal format.

| Anita   |    |               |                      |    |               |
|---|----|---------------|----------------------|----|---------------|
| Income statement for the year ended 30 September 20–5 |    |               |                      |    |               |
|   | \$ | \$            |                      | \$ | \$            |
| Property tax  |    | 6 400         | Commissions received |    | 92 150        |
| General expenses                                      |    | 8 950         | Rent receivable      |    | 7 300         |
| Insurance   |    | 2 670         |                      |    |               |
| Printing and stationery                               |    | 4 560         |                      |    |               |
| Loan interest   |    | 1 500         |                      |    |               |
| Wages   |    | 43 500        |                      |    |               |
| Profit for the year                                   |    | <u>31 870</u> |                      |    |               |
|   |    | <u>99 450</u> |                      |    | <u>99 450</u> |

**TIP**

The income statement of a service business does not have a trading account section.

- b** Prepare the income statement for Anita for the year ended 30 September 20–5. Use the vertical format.

| Anita   |    |               |               |
|---|----|---------------|---------------|
| Income statement for the year ended 30 September 20–5 |    |               |               |
|   | \$ | \$            | \$            |
| Commissions received                                  |    |               | 92 150        |
| Add Rent receivable                                   |    |               | <u>7 300</u>  |
|   |    |               | 99 450        |
| Less Property tax                                     |    | 6 400         |               |
| General expenses                                      |    | 8 950         |               |
| Insurance   |    | 2 670         |               |
| Printing and stationery                               |    | 4 560         |               |
| Wages   |    | <u>43 500</u> | <u>66 080</u> |
| Profit from operations                                |    |               | 33 370        |
| Less Loan interest                                    |    |               | <u>1 500</u>  |
| Profit for the year                                   |    |               | <u>31 870</u> |

You can now answer Question 6 at the end of this chapter.

## Revision checklist

- The difference between the selling price and the cost price is known as the gross profit. This is calculated in the trading account section of the income statement.
- The difference between the gross profit, plus other income, less expenses is known as the profit for the year. This is calculated in the profit and loss account section of the income statement.
- All the items appearing in the income statement are transferred from the ledger accounts to complete the double entry.
- A profit for the year is transferred to the credit of the capital account and a loss for the year is transferred to the debit of the capital account.
- A business which provides a service only prepares the profit and loss account section of the income statement.

## Exam-style questions

1 How is the cost of sales calculated?

- A opening inventory + purchases – carriage inwards – purchases returns – closing inventory
- B opening inventory + purchases – carriage inwards + purchases returns – closing inventory
- C opening inventory + purchases + carriage inwards – purchases returns – closing inventory
- D opening inventory + purchases + carriage inwards + purchases returns + closing inventory

2 At the end of his first year of trading, Rashid provided the following information.

|                   |        |
|-------------------|--------|
|                   | \$     |
| Revenue           | 72 500 |
| Purchases         | 49 700 |
| Closing inventory | 4 800  |
| Carriage inwards  | 1 150  |
| Carriage outwards | 2 950  |

What was Rashid's gross profit?

- A \$22 800
- B \$24 650
- C \$26 450
- D \$27 600

3 Mai, a fashion retailer, did not record goods costing \$500 taken for personal use.

What was the effect of this error?

|   | Gross profit |             | Profit for the year |             |
|---|--------------|-------------|---------------------|-------------|
|   | Overstated   | Understated | Overstated          | Understated |
| A | ✓            |             | ✓                   |             |
| B |              | ✓           |                     | ✓           |
| C | ✓            |             |                     | ✓           |
| D |              | ✓           | ✓                   |             |

- 4 Leo is a wholesaler. He has little knowledge of accounting. He prepared the following income statement which contains some errors.

| Leo   |                        |              |               |
|---|------------------------|--------------|---------------|
| Income statement for the year ended 30 April 20-1 |                        |              |               |
|   |                        | \$           | \$            |
| Revenue   |                        |              | 82 300        |
| Add   | Discount received      |              | 110           |
|   | Opening inventory      |              | <u>4 910</u>  |
|   |                        |              | 87 320        |
| Less  | Purchases              | 49 520       |               |
|   | Returns from customers | <u>1 190</u> |               |
|   |                        | 50 710       |               |
|   | Less Closing inventory | <u>5 080</u> | <u>45 630</u> |
|   | Profit on goods        |              | 41 690        |
| Add   | Discount allowed       |              | <u>220</u>    |
|   |                        |              | 41 910        |
| Less  | Rent payable           | 8 100        |               |
|   | Less Rent receivable   | <u>6 000</u> |               |
|   |                        | 2 100        |               |
|   | Wages                  | 12 100       |               |
|   | Carriage inwards       | 100          |               |
|   | Sundry expenses        | <u>960</u>   | <u>15 260</u> |
|   | Final profit           |              | <u>26 650</u> |

Prepare a corrected income statement for Leo for the year ended 30 April 20-1.

- 5 Oliver has been in business as a retailer for one year. He is unsure about some of the terms used in business.
- a Explain the difference between the following terms and how they are recorded in an income statement:
- i gross profit and profit for the year
  - ii carriage inwards and carriage outwards
  - iii discount allowed and discount received
  - iv purchases returns and sales returns

Oliver provided the following totals for the year ended 31 December 20–5:

|                      | \$    |
|----------------------|-------|
| Rates                | 3 140 |
| Office expenses      | 1 170 |
| Commissions received | 5 830 |
| Sales returns        | 1 480 |

- b** Enter these totals in the appropriate accounts. Close the accounts by making transfers to the income statement.

- 6** Candy provided the following information at the end of her financial year on 30 September 20–3:

|                            | \$      |
|----------------------------|---------|
| Capital at 1 October 20–2  | 198 000 |
| Fees received from clients | 82 300  |
| Staff wages                | 49 600  |
| Rent and rates             | 7 420   |
| Insurance                  | 3 830   |
| Commissions received       | 4 810   |
| Light and heat             | 2 180   |
| Office expenses            | 1 730   |
| Drawings                   | 18 750  |

- a** State whether Candy's business is a trading business or a service business. Give a reason for your answer.
- b** Prepare Candy's income statement for the year ended 30 September 20–3.
- c** Prepare Candy's capital account on 30 September 20–3. Balance the account and bring down the balance on 1 October 20–3.

# Chapter 16

## Control accounts

### Learning objectives

*In this chapter you will learn to:*

- understand the purposes of purchases ledger and sales ledger control accounts 3.4
- identify the books of prime entry as sources of information for the control account entries 3.4
- prepare purchases ledger and sales ledger control accounts to include credit purchases and sales, receipts and payments, cash discounts, returns, irrecoverable debts, dishonoured cheques, interest on overdue accounts, contra entries, refunds, opening and closing balances (debit and credit within each account). 3.4

## 16.1 Introduction

Control accounts are also known as **total accounts**. If the trial balance fails to balance and the error cannot be readily located, it is necessary to check all the accounting records. This can take a considerable amount of time. The checking process can be speeded up if a control account for the sales ledger (which contains the accounts of the debtors) and a control account for the purchases ledger (which contains the accounts of the creditors) have been prepared. These accounts act as a check on the individual accounts within these ledgers.

Like the trial balance, however, these accounts can only check the arithmetical accuracy: errors such as omission and commission will not be revealed by a control account.

## 16.2 Advantages of control accounts

Where a full set of accounting records is maintained, it is usual to prepare a **sales ledger control account** and a **purchases ledger control account**. The advantages of preparing these accounts are as follows:

- 1 They can assist in locating errors when the trial balance fails to balance.
- 2 They are proof of the arithmetical accuracy of the ledgers they control.
- 3 The balances on these accounts are regarded as being equal to the total of the trade receivables and the total of the trade payables, so this information is available immediately.
- 4 Draft financial statements can be prepared quickly because of the balances provided by the control accounts.
- 5 They help to reduce fraud as the control accounts are prepared by someone who has not been involved in making the entries in those particular ledgers.
- 6 They provide a summary of the transactions affecting the trade receivables and trade payables for each financial period.

### TEST YOURSELF 16.1

- 1 Name the account which summarises all the sales ledger accounts.
- 2 Name the account which summarises all the purchases ledger accounts.
- 3 State **three** reasons for preparing control accounts.

## 16.3 Sales ledger control account

This is also referred to as a **total trade receivables account**. This account resembles the account of a credit customer, but instead of containing transactions concerned with just one person or business it contains transactions relating to *all* the debtors. A typical sales ledger control account is shown here.



### LINK

You learned about the division of the ledger in Chapter 4.



### LINK

You learned about the errors not revealed by a trial balance in Chapter 3.



### KEY TERMS

A **sales ledger control account** is an account summarising all the accounts of the trade receivables and a **purchases ledger control account** is an account summarising all the accounts of the trade payables.

| Nominal ledger               |                      |       |       |      |                     |       |       |
|------------------------------|----------------------|-------|-------|------|---------------------|-------|-------|
| Sales ledger control account |                      |       |       |      |                     |       |       |
| Date                         | Details              | Folio | \$    | Date | Details             | Folio | \$    |
|                              | Balance              | b/d   |       |      | Sales returns       |       |       |
|                              | Sales                |       |       |      | Cash                |       |       |
|                              | Bank                 |       |       |      | Bank                |       |       |
|                              | (dishonoured cheque) |       |       |      | Discount allowed    |       |       |
|                              | Bank/Cash (refunds)  |       |       |      | Irrecoverable debts |       |       |
|                              | Interest charged     |       | _____ |      | Balance             | c/d   | _____ |
|                              | Balance              | b/d   | _____ |      |                     |       | _____ |

As this account acts as a check on the individual credit customers' accounts, it should be prepared independently and information in the individual accounts of the credit customers must **not** be used. (An error in the sales ledger would not be revealed if the control account is prepared from the accounts in that ledger.) **The information to prepare a sales ledger control account is obtained from the books of prime entry.** The sources of information are summarised as follows:

| Item                                  | Source of information |
|---------------------------------------|-----------------------|
| Sales                                 | Sales journal         |
| Sales returns                         | Sales returns journal |
| Receipts from credit customers        | Cash book             |
| Discounts allowed to credit customers | Cash book             |
| Dishonoured cheques                   | Cash book             |
| Refunds to credit customers           | Cash book             |
| Irrecoverable debts written off       | Journal               |
| Interest charged on overdue accounts  | Journal               |

The sales ledger control account is drawn up at the end of the financial period (often monthly) and balanced. The total of the balances on all the individual credit customers' accounts should agree with the balance on the control account. If they differ, it indicates that there is an error in one of the customers' accounts or an error in the control account, so further checks are required.



**TIP**

A sales ledger account is a summary of the accounts of credit customers (trade receivables) so will not include items which do not appear in the account of a credit customer, such as cash sales and provision for doubtful debts.

**Walkthrough 16.1**

Shweta maintains a full set of accounting records and prepares control accounts at the end of each month.

She provided the following information:

|      |          |  |            |
|------|----------|--|------------|
|      |          | \$   |            |
| 20–8 | March 1  | Sales ledger control account balance                             | 1200 debit |
|      | March 31 | Totals for the month:  |            |
|      |          | Sales journal  | 4890       |
|      |          | Sales returns journal  | 250        |
|      |          | Cheques and bank transfers received from credit customers        | 3892       |
|      |          | Discount allowed to credit customers                             | 8          |
|      |          | Cash received from credit customers                              | 120        |
|      |          | Cash refunds to credit customers                                 | 19         |
|      |          | Cheque received (included in the above figure) later dishonoured | 80         |
|      |          | Irrecoverable debts written off                                  | 94         |

Prepare Shweta's sales ledger control account for the month of March 20–8.

| Shweta<br>Nominal ledger<br>Sales ledger control account |                              |       |      |        |                     |       |      |
|--|------------------------------|-------|------|--------|---------------------|-------|------|
| Date   | Details                      | Folio | \$   | Date   | Details             | Folio | \$   |
| 20–8   |                              |       |      | 20–8   |                     |       |      |
| Mar 1  | Balance                      | b/d   | 1200 | Mar 31 | Sales returns       |       | 250  |
| 31   | Sales                        |       | 4890 |        | Cash                |       | 120  |
|  | Bank (dishonoured<br>cheque) |       | 80   |        | Bank                |       | 3892 |
|  | Cash (refunds)               |       | 19   |        | Discount allowed    |       | 8    |
|  |                              |       |      |        | Irrecoverable debts |       | 94   |
|  |                              |       |      |        | Balance             | c/d   | 1825 |
|  |                              |       | 6189 |        |                     |       | 6189 |
| 20–8   |                              |       |      |        |                     |       |      |
| Apr 1  | Balance                      | b/d   | 1825 |        |                     |       |      |

## 16.4 Purchases ledger control account

This is also known as a **total trade payables account**. This account resembles the account of a credit supplier, but instead of containing transactions concerned with just one person or business it contains transactions relating to **all** the creditors. A typical purchases ledger control account is shown here.

| Nominal ledger                   |                   |       |       |      |                        |       |       |
|----------------------------------|-------------------|-------|-------|------|------------------------|-------|-------|
| Purchases ledger control account |                   |       |       |      |                        |       |       |
| Date                             | Details           | Folio | \$    | Date | Details                | Folio | \$    |
|                                  | Purchases returns |       |       |      | Balance                | b/d   |       |
|                                  | Cash              |       |       |      | Purchases              |       |       |
|                                  | Bank              |       |       |      | Interest charged       |       |       |
|                                  | Discount received |       |       |      | Bank/Cash<br>(refunds) |       |       |
|                                  | Balance           | c/d   | _____ |      |                        |       | _____ |
|                                  |                   |       | _____ |      | Balance                | b/d   | _____ |



### TIP

The accounts in the sales and purchases ledgers are not used to provide information for preparing a control account otherwise errors in the ledgers would not be revealed.

This account serves a similar purpose to the sales ledger control account. It acts as a check on the individual credit suppliers' accounts and must be prepared independently and **not** from information in the individual accounts of the credit suppliers. **The information to prepare a purchases ledger control account is obtained from the books of prime entry.** The sources of information are summarised as follows:

| Item                                     | Source of information     |
|--|---------------------------|
| Purchases                                | Purchases journal         |
| Purchases returns                        | Purchases returns journal |
| Payments to credit suppliers             | Cash book                 |
| Discounts received from credit suppliers | Cash book                 |
| Refunds from credit suppliers            | Cash book                 |
| Interest charged on overdue accounts     | Journal                   |

Like the sales ledger control account, the purchases ledger control account is drawn up at the end of the financial period (often monthly) and balanced. The total of the balances on all the individual credit suppliers' accounts should agree with the balance on the control account. If they differ it indicates that there is an error in one of the suppliers' accounts or the control account, so further checks are required.



### TIP

A purchases ledger account is a summary of the accounts of credit suppliers (trade payables) so will not include items which do not appear in the account of a credit supplier such as cash purchases.

**Walkthrough 16.2**

Shweta maintains a full set of accounting records and prepares control accounts at the end of each month.

She provided the following information:

|      |          |   |             |
|------|----------|---|-------------|
|      |          |   | \$          |
| 20–8 | March 1  | Purchases ledger control account balance            | 1880 credit |
|      | March 31 | Totals for the month:                               |             |
|      |          | Purchases journal                                   | 4230        |
|      |          | Purchases returns journal                           | 180         |
|      |          | Cheques and bank transfers paid to credit suppliers | 3900        |
|      |          | Discount received from credit suppliers             | 104         |
|      |          | Cheque refunds from credit suppliers                | 100         |
|      |          | Interest charged on overdue account                 | 12          |

Prepare Shweta's purchases ledger control account for the month of March 20–8.

| Shweta<br>Nominal ledger<br>Purchases ledger control account |                   |       |             |       |                  |       |             |
|--|-------------------|-------|-------------|-------|------------------|-------|-------------|
| Date   | Details           | Folio | \$          | Date  | Details          | Folio | \$          |
| 20–8   |                   |       |             | 20–8  |                  |       |             |
| Mar 31   | Purchases returns |       | 180         | Mar 1 | Balance          |       | 1880        |
|  | Bank              |       | 3900        | 31    | Purchases        |       | 4230        |
|  | Discount received |       | 104         |       | Bank (refunds)   |       | 100         |
|  | Balance           | c/d   | <u>2038</u> |       | Interest charged |       | <u>12</u>   |
|  |                   |       | <u>6222</u> |       |                  |       | <u>6222</u> |
|  |                   |       |             | 20–8  |                  |       |             |
|  |                   |       |             | Apr 1 | Balance          | b/d   | 2038        |



You will learn about the use of total accounts for calculating missing information in Chapter 17.

You can now answer Questions 1 and 2 at the end of this chapter.

**TEST YOURSELF 16.2**

- 1 Explain why the information used for preparing control accounts must be obtained from books of prime entry.
- 2 State the source of information for **each** of the following:
  - a purchases returns
  - b discount allowed
  - c irrecoverable debts.

## 16.5 Balances on both sides of a control account

Occasionally a credit customer’s account may show a credit balance. This may occur due to:

- an overpayment by the customer
- the customer returning goods after paying the account
- the customer paying in advance for the goods
- cash discount not being deducted before payment was made.

In the sales ledger control account it is usual to keep any credit balance separate from the debit balance. The control account will, therefore, have two balances – the usual debit balance representing money owing **by** credit customers, and the more unusual credit balance representing money owing **to** credit customers. Any credit balance is entered on the debit side of the control account and carried down as a credit balance. The account can then be balanced in the usual way.

### Walkthrough 16.3

Shweta maintains a full set of accounting records and prepares control accounts at the end of each month.

She provided the following information:

|      |          |   | \$          |
|------|----------|---|-------------|
| 20–8 | April 1  | Sales ledger control account balance                      | 1 825 debit |
|      | April 30 | Totals for the month:                                     |             |
|      |          | Sales journal   | 4 910       |
|      |          | Sales returns journal                                     | 210         |
|      |          | Cheques and bank transfers received from credit customers | 4 788       |
|      |          | Discount allowed to credit customers                      | 12          |
|      |          | Interest charged on overdue account                       | 10          |
|      | May 1    | Sales ledger credit balances                              | 115         |

Prepare Shweta’s sales ledger control account for the month of April 20–8.

| Shweta                       |                  |       |       |        |                  |       |       |
|------------------------------|------------------|-------|-------|--------|------------------|-------|-------|
| Nominal ledger               |                  |       |       |        |                  |       |       |
| Sales ledger control account |                  |       |       |        |                  |       |       |
| Date                         | Details          | Folio | \$    | Date   | Details          | Folio | \$    |
| 20–8                         |                  |       |       | 20–8   |                  |       |       |
| Apl 1                        | Balance          | b/d   | 1 825 | Apl 30 | Sales returns    |       | 210   |
| 30                           | Sales            |       | 4 910 |        | Bank             |       | 4 788 |
|                              | Interest charged |       | 10    |        | Discount allowed |       | 12    |
|                              | Balance          | c/d   | 115   |        | Balance          | c/d   | 1 850 |
|                              |                  |       | 6 860 |        |                  |       | 6 860 |
| 20–8                         |                  |       |       | 20–8   |                  |       |       |
| May 1                        | Balance          | b/d   | 1 850 | May 1  | Balance          | b/d   | 115   |

In a similar way, a credit supplier's account can show a debit balance. This may occur due to:

- an overpayment to the supplier
- returning goods to the supplier after paying the account
- paying the supplier in advance for the goods
- cash discount not being deducted before payment was made.

As in the sales ledger control account, the debit balance and the credit balance are shown separately in the purchases ledger control account. The purchases ledger control account will, therefore, have two balances – the usual credit balance representing money owing **to** credit suppliers, and the more unusual debit balance representing money owing **by** credit suppliers. Any debit balance is entered on the credit side of the control account and carried down as a debit balance. The account can then be balanced in the usual way.

### TEST YOURSELF 16.3

- 1 Explain how it is possible for a customer's account to have a credit balance.

You can now answer Questions 3 and 4 at the end of this chapter.

## 16.6 Contra entries in control accounts

**Contra entries** are also known as **inter-ledger transfers** or **set-offs**.

It may happen that a business sells goods to another business and also buys different goods from that business. This means that there will be two ledger accounts for that business – one in the sales ledger and the other in the purchases ledger.

Rather than each business sending the other a cheque to cover the amount due, they may agree to set one account off against the other. Any remaining amount will be settled by one business issuing a cheque.



### KEY TERM

**Contra entries** may be referred to as inter-ledger transfers or set-offs and are when a transfer is made from an account in the sales ledger to an account of the same business/person in the purchases ledger.

### Walkthrough 16.4

Shweta provided the following information:

20–8

- May 15 Sold goods, \$190, on credit to Mansingh Road Stores
- 22 Bought goods, \$320, on credit from Mansingh Road Stores
- 30 The balances of the two accounts for Mansingh Road Stores were set-off and Shweta sent a cheque for the remaining balance.

Record these transactions in the account for Mansingh Road Stores in the sales ledger and the account for Mansingh Road Stores in the purchases ledger.

| Shweta<br>Sales ledger<br>Mansingh Road Stores account |         |       |            |        |                  |       |            |
|--|---------|-------|------------|--------|------------------|-------|------------|
| Date   | Details | Folio | \$         | Date   | Details          | Folio | \$         |
| 20–8   |         |       |            | 20–8   |                  |       |            |
| May 15   | Sales   |       | 190        | May 30 | Purchases ledger |       | 190        |
|  |         |       | <u>190</u> |        |                  |       | <u>190</u> |

**TIP**  
A contra entry, sometimes known as an inter-ledger transfer or set-off, is recorded in both the sales ledger control account and the purchases ledger control account.

| Purchases ledger<br>Mansingh Road Stores account |              |       |            |        |           |       |            |
|--|--------------|-------|------------|--------|-----------|-------|------------|
| Date   | Details      | Folio | \$         | Date   | Details   | Folio | \$         |
| 20-8   |              |       |            | 20-8   |           |       |            |
| May 30   | Sales ledger |       | 190        | May 22 | Purchases |       | 320        |
|  | Bank         |       | <u>130</u> |        |           |       |            |
|  |              |       | <u>320</u> |        |           |       | <u>320</u> |

- A journal entry would be made for the transfer of \$190 on 30 May as it is a non-regular transaction.
- As the transfer of \$190 on 30 May affected both the accounts in sales ledger and purchases ledger, it would affect both the sales ledger control account and the purchases ledger control account. See Walkthrough 16.5.

### Walkthrough 16.5

Shweta provided the following information for the month of May 20-8.

|   | \$    |
|---|-------|
| 20-8  |       |
| May 1 Sales ledger control account debit balance          | 1 850 |
| Sales ledger control account credit balance               | 115   |
| Purchases ledger control account credit balance           | 2 118 |
| 31 Totals for the month:                                  |       |
| Sales journal   | 5 360 |
| Purchases journal   | 5 110 |
| Sales returns journal                                     | 134   |
| Purchases returns journal                                 | 216   |
| Cheques and bank transfers received from credit customers | 4 965 |
| Cheques and bank transfers paid to credit suppliers       | 4 508 |
| Discount received from credit suppliers                   | 92    |
| Irrecoverable debt written off                            | 35    |
| Interest charged by credit supplier on overdue account    | 14    |
| Contra entry  | 190   |
| June 1 Sales ledger control account debit balance         | ?     |
| Purchases ledger control account credit balance           | ?     |
| Purchases ledger control account debit balance            | 135   |

Prepare Shweta's sales ledger control account and purchases ledger control account for the month of May 20-8. Balance the accounts and bring down the balances on 1 June 20-8.

| Shweta<br>Nominal ledger<br>Sales ledger control account |          |       |              |       |                    |       |              |
|--|----------|-------|--------------|-------|--------------------|-------|--------------|
| Date   | Details  | Folio | \$           | Date  | Details            | Folio | \$           |
| 20-8   |          |       |              | 20-8  |                    |       |              |
| May 1  | Balance  | b/d   | 1 850        | May 1 | Balance            | b/d   | 115          |
|  | 31 Sales |       | 5 360        | 31    | Sales returns      |       | 134          |
|  |          |       |              |       | Bank               |       | 4 965        |
|  |          |       |              |       | Irrecoverable debt |       | 35           |
|  |          |       |              |       | Contra entry       |       | 190          |
|  |          |       |              |       | Balance            | c/d   | 1 771        |
|  |          |       | <u>7 210</u> |       |                    |       | <u>7 210</u> |
| 20-8   |          |       |              |       |                    |       |              |
| June 1   | Balance  | b/d   | 1 771        |       |                    |       |              |

| Shweta<br>Nominal ledger<br>Purchases ledger control account |                   |       |              |        |                  |       |              |
|--|-------------------|-------|--------------|--------|------------------|-------|--------------|
| Date   | Details           | Folio | \$           | Date   | Details          | Folio | \$           |
| 20-8   |                   |       |              | 20-8   |                  |       |              |
| May 1  | Purchases returns |       | 216          | May 1  | Balance          | b/d   | 2 118        |
|  | Bank              |       | 4 508        | 31     | Purchases        |       | 5 110        |
|  | Discount received |       | 92           |        | Interest charged |       | 14           |
|  | Contra entry      |       | 190          |        | Balance          | c/d   | 135          |
|  | Balance           | c/d   | 2 371        |        |                  |       |              |
|  |                   |       | <u>7 377</u> |        |                  |       | <u>7 377</u> |
| 20-8   |                   |       |              | 20-8   |                  |       |              |
| June 1   | Balance           | b/d   | 135          | June 1 | Balance          | b/d   | 2 371        |

**TEST YOURSELF 16.4**

- 1 In connection with control accounts, explain the meaning of a contra entry.

You can now answer Questions 5 and 6 at the end of this chapter.

**Revision checklist**

- The main purpose of control accounts is to assist in locating errors in the sales ledger and the purchases ledger.
- A sales ledger control account resembles the account of a credit customer but contains transactions affecting all credit customers.
- A purchases ledger control account resembles the account of a credit supplier but contains transactions affecting all credit suppliers.
- The information to prepare control accounts is obtained from the books of prime entry.
- It is possible to have a balance on each side of a control account.
- If a business is both a customer and a supplier, a contra entry may be made to transfer a balance from the sales ledger account to the purchases ledger account.

## Exam-style questions

- 1 What is the purpose of preparing a sales ledger control account?
  - A to calculate the total credit sales for the period
  - B to calculate the total sales for the period
  - C to check the arithmetical accuracy of the sales account
  - D to check the arithmetical accuracy of the sales ledger accounts
  
- 2 What may appear on the debit side of a purchases ledger control account?
  - A credit purchases
  - B discount allowed
  - C payments to credit suppliers
  - D returns by credit customers
  
- 3 Shilpa's sales ledger control account had an opening credit balance. What does this mean?
  - A total amount owing by credit customers
  - B goods returned by credit customers
  - C interest charged on credit customers' accounts
  - D overpayment made by credit customers

- 4 Hamir is a trader who maintains full set of accounting records. He divides his ledger into three sections – nominal (general), sales and purchases.

- a State **one** advantage of dividing the ledger into these sections.
- b State **two** advantages of maintaining a purchases ledger control account.

Hamir provided the following information for the month of May 20–1:

|        |                                     | \$    |
|--------|-------------------------------------|-------|
| May 1  | Debit balances in purchases ledger  | 105   |
|        | Credit balances in purchases ledger | 4 897 |
| May 31 | Totals for the month:               |       |
|        | Credit purchases                    | 5 424 |
|        | Purchases returns                   | 657   |
|        | Payments to suppliers               | 4 312 |
|        | Discount received                   | 88    |
|        | Interest charged by credit supplier | 20    |
| June 1 | Debit balances in purchases ledger  | 76    |

- c Prepare the purchases ledger control account for the month of May 20–1. Balance the account and bring down the balances on 1 June 20–1.
- d Name the book of prime entry Hamir would use to provide information about:
  - i interest charged by credit supplier
  - ii purchases returns
  - iii discount received.

- 5 a** Complete the following table to state where the items would appear in a purchases ledger control account. For each item name the book of prime entry from which the information would be obtained.

|            |  | Entry in purchases ledger control account |        | Source of information |
|------------|--|---|--------|-----------------------|
|            |  | Debit                                     | Credit |                       |
| <b>i</b>   | payments to credit suppliers                       |   |        |                       |
| <b>ii</b>  | cheques paid to credit suppliers later dishonoured |   |        |                       |
| <b>iii</b> | credit purchases                                   |   |        |                       |
| <b>iv</b>  | contra entry to sales ledger account               |   |        |                       |
| <b>v</b>   | discount received                                  |   |        |                       |
| <b>vi</b>  | interest charged by supplier on overdue account    |   |        |                       |
| <b>vii</b> | returns to credit suppliers                        |   |        |                       |

- b** Explain why the information required to prepare a purchases ledger control account is not obtained from the purchases ledger.
- c** Explain the contra entry to the sales ledger and why it was needed.

- 6** Eva is a trader who maintains a full set of accounting records and prepares control accounts at the end of each month. She provided the following information:

|             |   |       |
|-------------|---|-------|
| 20–5        |   | \$    |
| February 1  | Debit balance in the sales ledger control account   | 2 470 |
|             | Credit balance in the sales ledger  | 110   |
|             | Provision for doubtful debts  | 100   |
| February 28 | Totals for the month:   |       |
|             | Credit sales  | 3 480 |
|             | Cash sales  | 1 950 |
|             | Returns by credit customers   | 118   |
|             | Cheques received from credit customers  | 3 403 |
|             | Cheque received from credit customer (included in the cheques received above) later dishonoured | 104   |
|             | Discount allowed  | 144   |
|             | Discount received   | 176   |
|             | Irrecoverable debts written off   | 200   |
|             | Contra entry  | 240   |
| March 1     | Debit balance in the sales ledger control account   | ?     |
|             | Credit balance in the sales ledger control account  | 95    |

- a** Select the relevant figures and prepare the sales ledger control account for the month of May 20–1. Balance the account and bring down the balances on 1 June 20–1.
- b** For each entry (excluding the balances) in the sales ledger control account prepared in **a** name the book of prime entry which would be used as a source of information.
- c** Select **two** items listed that should not appear in a sales ledger control account and explain why they do not appear.
- d** Suggest **two** reasons for the credit balance on the sales ledger control account on 1 March 20–1.