

Workbook



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End of year adjustments

General

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Exercise 1 – WMB

WMB is a small local car dealership representing a large car manufacturer. It has two owners and several employees. Its business model involves taking orders from customers and placing them with the manufacturer. The customer has to place a 10% deposit based on the selling price of the car on order. It also has a small stock of cars (used and new) which are available for immediate delivery. Delivery of the new cars takes place three months after an order is placed.

Its trial balance on 31/12/X1 is given below (all figures in CU)

	Dr	Cr
Property, plant and equipment (PP&E)	220,000	
Inventory at 30/11/X1	1,300,000	
Accounts receivable	98,500	
Bank	73,000	
Accounts payable (Suppliers)		125,000
Cost of sales	1,550,000	
Sales		3,650,000
Salaries, wages and bonuses	550,000	
Administrative expenses	103,500	
Share capital		30,000
Retained earnings 31/12/X0		90,000

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3,895,00	3,895,000
0	

Orders by customers for new cars placed in the last three months of the year ended 31 December 20X1 (to be delivered in 20X2) are as follows (in CU, totals):

Total sales value	
Month	CU
October	520,000
November	350,000
December	330,000
Total	1,200,000

Additional information:

1. Sales personnel get paid a bonus of 2% of the value of each order placed and are paid three months in arrears, when the car is delivered. The trial balance does not reflect the bonuses for any of the orders placed in the last quarter of 20X1.
2. The 10% deposit received from order-placing customers in the last quarter of 20X1 has been recognised as part of sales.
3. A physical count of inventory was conducted on 31/12/20X1. It revealed that the cost of physical inventory on hand was only CU 1,260,000. Upon further investigation it was found that the difference between the physical stock count and the amount shown in the trial balance represents sales of cars from stock for which the accountant had not recorded the cost of the sale. The cash received from the sale had been properly credited to sales.
4. On 31/10/X1 WMB purchased an annual insurance policy on its PP&E. At that time it paid CU 9,000 and recorded the full amount in administrative expenses.
5. The tax on profits is 20% of the pre-tax profit. This tax is due for payment in 20X2. No journal entries have been processed in this regard.

Required:

- a) Record the journal entries required for preparing the final trial balance at 31/12/20X1.
- b) Prepare the adjusted trial balance at 31/12/20X1.
- c) Prepare the income statement for the year ended 31/12/20X1.
- d) Prepare the balance sheet at 31/12/20X1.

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Exercise 2 - Ama

Ama is a service company which started operations in July 20X0. Its financial year-end is 31 December.

Ama receives cash from its customers which it immediately recognises in revenue. However, some of the cash received from customers is paid in advance for services not yet provided. The table below summarises annual revenue recorded before any adjustment is made to account for unearned revenue as well as the estimate of the % of unearned revenue in each year 20X0 - 20X3:

Year	Revenue Recorded (CU)	Unearned Revenue as % of Recorded Revenue
20X0	800,000	5%
20X1	1,000,000	12%
20X2	1,200,000	11%

Unearned revenue at the end of a financial year is always subsequently earned, and thus recognised as revenue, in the following year.

Required:

- Determine the amount of revenue to be recognised in the income statement of Ama for the years ending 31 December 20X0, 20X1 and 20X2.
- Determine the amount of the unearned revenue to be recognised on the balance sheet of Ama at 31 December 20X0, 20X1 and 20X2.

Workings

Year	Revenue Recorded (CU)	Unearned Revenue as % of Recorded Revenue
20X0	800,000	5%
20X1	1,000,000	12%
20X2	1,200,000	11%

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W1 – 20X0

		Assets	Liabilities	Equity	
		Cash	Unearned Revenue	Revenue	Retained Earnings
Opening balance		0	0	0	
Revenue recognised		800,000		800,000	
Unearned revenue	800,000 x 5%		40,000	(40,000)	
		800,000	40,000	760,000	
Retaining profit or loss				(760,000)	760,000
Carried forward		800,000	40,000		760,000

Workings

Year	Revenue Recorded (CU)	Unearned Revenue as % of Recorded Revenue
20X0	800,000	5%
20X1	1,000,000	12%
20X2	1,200,000	11%

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W2 – 20X1

		Assets	Liabilities	Equity	
		Cash	Unearned Revenue	Revenue	Retained Earnings
Opening balance		800,000	40,000		760,000
Unearned revenue from prior year recognised in current year			(40,000)	40,000	
Revenue recognised		1,000,000		1,000,000	
Unearned revenue	$1,000,000 \times 12\%$		120,000	(120,000)	
		1,800,000	120,000	920,000	
Retaining profit or loss				(920,000)	920,000
Carried forward		1,800,000	120,000		1,680,000

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Workings

Year	Revenue Recorded (CU)	Unearned Revenue as % of Recorded Revenue
20X0	800,000	5%
20X1	1,000,000	12%
20X2	1,200,000	11%

W3 – 20X2

		Assets	Liabilities	Equity	
		Cash	Unearned Revenue	Revenue	Retained Earnings
Opening balance		1,800,000	120,000		1,680,000
Unearned revenue from prior year recognised in current year			(120,000)	120,000	
Revenue recognised		1,200,000		1,200,000	
Unearned revenue	1,200,000 x 11%		132,000	(132,000)	
Balance		3,000,000	132,000	1,188,000	
Retaining profit or loss				(1,188,000)	1,188,000

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Carried forward		3,000,00 0	132,000		2,868,00 0
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Exercise 3 - Pour

Pour is a service company which started operations in July 20X0. Its financial year-end is 31 December.

Pour purchases an annual insurance policy for which payment takes place on 1 July of each year. The following table shows amounts paid on 1 July in each year in respect of this policy:

Year	Insurance premium paid CU
20X0	60,000
20X1	72,000
20X2	84,000
20X3	90,000

Required:

- Determine the amount of the *insurance expense* to recognise in the **income statement** of Pour for the years ending 31 December 20X0 - 20X3.
- Determine the balance of *pre-paid insurance* on the **balance sheet** of Pour at 31 December 20X0 - 20X3.

*For the solution see the videos