FORM 6

ACCOUNTANCY NOTES

PARTNERSHIP ACCOUNTING

A. PARTNERSHIP
WHAT IS IT?

Is a relationship between persons who have agreed to share profit and loss of the business carried by all with a profit meditative.

Partners: Are persons making an agreement to carry business for a common purpose/intention.

- Individual – these are partners (Persons by nature).
- Collectively – This is a firm (legal persons).

MAIN FEATURES OF PARTNERSHIP;

1. Two or more persons.
2. There must be an agreement between partners.
3. Lawful business.
4. Profit Motive.
5. Principal to agent relationship.
6. Unlimited liabilities.

B. CAPITAL ACCOUNTS

Capital can be contributed

(a) **In kind**

Anything equivalent to cash e.g. A house, a car etc

ENTRIES
DR ; Motor car A/c

CR ; Capital A/c
b**) In cash**
- It is in cash
ENTRIES
DR ; Cash A/c
CR ; Capital A/c
c) **Both cash and in kind**
- Partner brought part in cash and part in kind.

TYPES OF CAPITAL ACCOUNTS

There are two types of Capital Account

(a) **Fluctuating capital Account**

- Also it is known as floating capital account.
- This system partners capital account do not remain intact (as its original balance but fluctuates quite frequently)
- It means the capital account changes with all items concerning partners e.g. Interest on drawings, interest on capital, Partners salaries, commission, Drawings, Properties brought in, Profit and less distribution.

(b**)** **Fixed Capital Account**

Under this system the original capital invested by the partners remain unaltered unless additional capital is invested or capital itself is withdrawn by mutual agreement.

(c) Partner's Current Account

It is an account that carries all items concerning Partners e.g. Interest on capital, Interest on drawings, Drawings, Partner's salaries and wages/ commission to partner.

(d) Profit and Loss Appropriation Account

This is an extension of usual profit and loss Account, it Is prepared for adjusting transaction relating to the partnership deed.

Contents

- Interest on partner's capital.
- Interest on partner's drawings.
- Interest on partner's loans.
- Partners salaries.
- Partner's commission.

NOTE

These transactions are treated separately without mixing up with general trading transaction.

ENTRIES

		DR	CR
1	Interest on Partner's Capital		
	DR; Interest or past Capital a/c	xx	
	CR; Partner's capital (current a/c		xx
	Transfer (fx)		
	DR; Profit and loss appropriation a/c	xx	
	CR; Interest on Partner's capital		xx
2	Interest on drawings		
	DR; Partner's Capital/Current a/c	xx	
	CR; Interest on Partner's Drawings		xx
	Transfer (fx)		
	DR; Interest on Partner's Drawings a/c	xx	
	CR; Profit and loss Appropriation a/c		xx

3	Interest on Partner's Loans		
	DR; Interest on Partner's Loan	xx	
	CR; Partners capital a/c		Xx
	Transfer (fx)		
	DR; Interest on partner's Loan	xx	
	CR;		Xx
4	Partner's salaries/Commissions		
	DR; Partner's salaries/commission	xx	
	CR; Partner's capital a/c		Xx
	Transfer (fx)		
	DR; Profit and loss appropriation a/c	xx	
	CR; Partner's salaries/commission		Xx

EXERCISE 1

Amake and Babake started a partnership on 1st January, 2010. Both agreed in the partnership did the following;

1. To contribute Shs.100, 000 each as capital.
2. To share Profit and loss equally.
3. Interest on capital at a rate of 5%.
4. Interest on drawings at a rate of 10%.
5. Partner's salary Shs.50, 000 per month each.

Transactions for the Month of January, 2010

1st January,2010	Invested required capital as per deed	
"	Purchased goods from RTC	700000
"	Purchased goods from Ally cash	100000

“	Babake inject additional funds in cash	200000
“	Amake took 50,000 shs from the firm to pay school fees for his son	
31st January 2010	Sold goods to NMC worth	2,000,000
	Sold goods to NMC by cash	500,000
	Goods counted physically worth	100,000
	Paid rent	10,000
	Rent received	100,000
	Paid to partner’s January salaries	
	Paid salaries	2000
	Paid productive wages	5000

Required

-Journal Proper to record all the transaction (No narration needed)

-Prepare ledger a/c’s to record all transactions relating to the months 1/2010

-Prepare trading profit and loss a/c and appropriation account for the period in a question.

-Show by extracting financial position of the A and B partnership (Amake and Babake).

PROFIT AND LOSS APPROPRIATION ACCOUNT

Commission	xxx	Net profit b/d	Xxx
Net loss	xxx	interest on drawings	
partner's salaries A- xx		A - xx	
B - xx	xxx	B - xx	Xxx
Bonus to partner's			
Interest on loan xx			

general reserve xx			
Residual profit			
A - xx			
B - xx	xxx		
	xxxx	xxxx	

PROFIT APPORTIONMENT BASIS

We are having two Basis of Apportioning residual profits

1. Time Basis Apportionment.
2. Profit analysis basis.

TIME BASIS APPORTIONMENT

In this method profit is apportioned between the various periods. That is to say the profit is accrued evenly.

Example

A and B are in partnership with share profit of .3:2 respectively on 1st January their capital stood at 500,000 and 400000 respectively. They decided to admit C as a new partner on 1st October, 2010, their new share profit ratio is 2.2.1. During the year the following Transaction took place.

	Tshs	
Purchases were	1,000,000	
Sales were	2,500,000	
Partner's salaries	600,000	
C brought 100,000 as capital		
Interest on capital 10% p.a		
Electricity	100,000	

Salaries and wages	200,000	

Required;

-Prepare Profit and loss appropriation on time basis for A and B partnership and ABC partnership. Financial year ended 31st Dec. 2010:

Workings (W).

$$\text{Total } 1{,}000{,}000 \text{ x } \frac{9}{12} = 750{,}000$$

Sales (A and B)

$$\text{Total } 2{,}500{,}000 \text{ x } \frac{9}{12} = 1{,}875{,}000$$

Electricity (A and B)

$$\text{Total } 100{,}000 \text{ x } \frac{9}{12} = 75{,}000$$

Salaries and Wages (A and B)

$$\text{Total } 200{,}000 \text{ x } \frac{9}{12} = 150{,}000$$

Interest on Capital (A and B)

$$\text{Total A} - 600{,}000 \text{ x } \frac{10}{100} \text{ x } \frac{9}{12} = 45{,}000$$

$$\frac{10}{100} x \frac{9}{12} = 30{,}000$$

Partners Salaries (A)

Total 600,000 x $\frac{9}{12}$ = 450,000

Residual Profit (A and B)

For A; Total 375,000 x $\frac{3}{5}$ = 225,000

For B; Total 375,000 x $\frac{2}{5}$ = 150,000

A AND B

PROFIT AND LOSS APPROPRIATION ACCOUNT FOR THE PERIOD ENDED

30TH SEPTEMBER, 2010

(Trading)	(shs)		
Purchases	750,000.00	sales	1,875,000.00
gross profit c/d	1,125,000.00		
	1,875,000.00	1,875,000.00	
electricity	75,000.00	gross profit b/d	1,125,000.00
salaries and wages	150,000.00		
net profit c/d	900,000.00		
	1,125,000.00	1,125,000.00	
interest on capital		Net profit b/d	900,000.00
A - 45,000			
B - 30,000	75,000.00		

Partner's salary	450,000.00		
residual profit			
A - 225,000			
B - 150,000	375,000.00		
	900,000.00	900,000.00	

Working ; - W2purchases (A, B & C)

Total 1,000,000 x 9/12 = 250,000

Sales (A, B & C)

Total 2,500,000 x 9/12 = 625,000

Electricity (A, B &C)

Total 100,000 x 9/12 = 25,000

Salaries and wages (A, B & C)

Total 200,000 x 9/12= 50

Interest on capital (A, B & C)

Total A - 600,000 x10/100 x9/12 = 15,000

B - 400,000 x10/100 x 9/12= 10,000

C – 100,000 x x = 2500

Partner's salaries (A, B & C)

Total 600,000 x = 50,000

Residual value

For A; Total 123,500 x = 49,400

For B; Total 123,500 x = 49,400

For c; Total 123,500 x = 24,700

A, B & C PROFIT AND LOSS APPROPRIATION ACCOUNT FOR THE PERIOD END 30TH SEPT.

(Trading)	shs		
purchases	250,000	sales	625,000
gross profit c/d	375,000		
	625,000	625,000	
electricity	25,000	gross profit b/d	375,000
salaries and wages	50,000		
net profit c/d	300,000		
	375,000	375,000	
		net profit b/d	300,000
interest on capital			
A - 15,000			
B - 10,000			
C - 2500	27500		
Partner salary	150,000		
residual profit			
A - 49,400			
B - 49,400			
C - 24,700	123,500		
	300,000	300,000	

SECOND METHOD; PROFIT ANALYSIS BASIS

In this method profit is apportioned by using analyzed profit and loss. This requires the use of separated column in the profit and loss account for the period in question.

a) **Gross Profit**

Is apportioned between the period on basis of turn over.

b) **Fixed charges**

Fixed charges are apportioned on the basis of time.

c) **Variable charges**

Variable charges are apportioned on the basis of turnover.

d) **Other charges**

Other charges with special information given are apportioned according to that given information.

EXERCISE

X and Y are carrying on a business in partnership sharing profit and losses in the ratio of 3:2 but during the year ended Dec 31st 2007 two other member were admitted namely W and Z on July 1st and sept 30th 2007 respectively. Net sale during the year amounted to shs. 250,000, selling and distribution on expenses amount to shs. 12,000.

However the firms sales break down were;	Tshs.
January 1st to march 31st	62,500
April 1st to June 30th	93,750
July 1st to sept 30th	31,250
Oct 1st to Dec 31st	62,500

The firm normally fixes the Gross profit at 25% above the cost

Their profits and losses sharing ratios were;

X and Y and W was 2; 2; 1

X, Y, W and Z was 4; 3; 2; 1

Prepare;

a) The profit and loss account for the year ended 31st Dec 2007

b) An appropriation account for the year ended Dec 2007.

SOLUTION;

$W_{1;}$ **GROSS PROFIT AMOUNT**

If the gross profit is 25% above the cost

Thus

Sales are at 25%

G.P = x 250,000; from where r = rate

= 50,000

W_2**;** First 6 month's G.P; (sales; - 62500 + 93750 = 156250)

6 months G.P = Gross profit x sales for the period

= x 156,250 = 31250.

$W_{3;}$ Gross profit from July 1st - 30th sept (sales = 31250)

3 months G.P = x 31250

= 6250

W_4 = Gross profit from October1st- Dec 31st (sales = 62500)

Lost 3 month's G.P

= 12,500

$W_{5;}$ Administrative expenses 12,000

a) X 12,000 = 6000

b) X 12000 = 3000

c) X 12,000 = 3000

Selling and distribution expenses 25,000

a) For 6 month's sales = 156250

6 month's selling and distribution exp.

Total expenses x sale for the period

Total sales

25,000 x 156,250

250,000

= 15,625

b) For next 3 months sales = 31,250

3 months selling and distribution exp. = 25,000 x 31250

250,000

= 3125

c) For the last 3 month's sales = 62,500

Last 3 month's selling and distribution exp. =

25,000 x 62,500 = 6250

250,000

DR PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31ST DEC 2007 CR

DETAILS	6	3	3	DETAILS	6	3	3
Admin. Expenses	6000	3000	3000	Gross profit	31250	6250	12500
selling & distr. Exp	15625	3125	6250				
9625	125	3250					
	31250	6250	12500	31250	6250	12500	

PROFIT AND LOSS APPROPRIATION A/C FOR THE PERIOD ENDED 30/6/07

SHS		SHS	
Capital X ; ½ x 9625	5,775.00	Net profit b/d	9,625.00
Y ; 2/5 x 9625	3,850.00		
	9,625.00	9,625.00	

PROFIT AND LOSS APPROPRIATION FOR THE PERIOD ENDED 31ST DEC.2007

Capital X; 2/5 x 125	50		
Y ; 2/5 x 125	50	Net profit b/d	125
W ; x 125	25		
	125	125	

PROFIT AND LOSS APPROPRIATION A/C FOR THE PERIOD ENDED 31ST DEC.2007

Capital x: 4/10 x 3250	1300	Net profit b/d	3250
y: 3/10 x 3250	775		
z: 2/10 x 3250	650		
w: 1/10 x 3250	325		
	3250	3250	

ADMISSION OF PARTNERS

- When additional capital or managerial stalls or both are required in the course of expansion it is quite usual to take new partner or partners into partnership firm.
- The new partner usually invests additional capital to the firm.
- Admission of a new partner raises the following thins.

1. Treatment of Goodwill
2. Revaluation of Assets and liabilities
3. Re-arrangement of old partners capital balances after admission
4. Re-arrangement of old partners profit sharing rations

GOODWILL

- Goodwill simply means the good name or the reputation of the business
- Attraction of more customers depends on Goodwill and helps in earning more profit in future
- Goodwill is an asset
- New partner gets benefit of the extra asset and old ones lose their shares
- In other words when a new partner get some shares in the profit of the firm he acquire the same rights in the existing Assets of the firm and in the extra Asset (Goodwill).
- If that's the case automatically incoming partner, he has to compensate the old partners either:

  By paying in cash for his share of Goodwill

  By allowing the old partners capital account to be raised rate-ably

Method of Valuing Goodwill/Methods of calculating Goodwill

- The Goodwill of any business whether sole trader, Firm or company is generally determined by sharing.
- But it depends upon the following factors;

1. Present earning capacity of the business.
2. Results of the operations of a few previous years.
3. The future prospectors of the business.
4. Efficiency of management and employers.
5. Efficiency of advertising machinery and possession of trade marks.

WHEN VALUATION NEEDED

(a) On admission of a new partner.

(b) On retirement of a new partner.

(c) When changing profit sharing ratios.

(d) On sale of the business.

(e) During Amalgamation.

(f) On dissolution.

METHOD OF VALUATION OF GOODWILL

We are having four methods of valuation of Goodwill

1. Purchases of Past profit methods
2. Purchase of super profits methods
3. Inferred or Implied Goodwill method
4. Valuation by bargaining (Arbitrary methods).

- The value of goodwill is decided by direct bargaining between the buyer and seller.

- For Examination purposes such an amount is usually mentioned.

(a) Purchase of Past Profit Method

In this method Goodwill is valued at an agreed number of years (2-3 years) of an average profits of a given number of past years) illustration.

Goodwill is valued at two years purchased of the average profits of four years.

- It means average of four years profit multiply by two

PROFITS	YEARS
60,000	2011
50,000	2010
40,000	2009
5,000	2008

Goodwill = x no. years of purchase

= x 2= 100,000/=

Goodwill = 100,000

B. Purchase of super profit method

Super profit is the difference (Excess) between average annual earning (actual) of the business and the expected or normal return on capital invested. If the average annual profit of the business is Shs.5000,000/= and the normal earning capacity is 6%, if the capital invested is shs.300,000. Find super profits.

Super Profit = Average profit (Actual) – Normal return of capital invested.

= 50000 - x 800,000

= 50000 – 48,000

= 2000

Then super profit is taken as a base in compilation of Goodwill.

The goodwill be valued at a certain years of purchase of that super profit

3 years purchase: 2000 x 3 = 6,000

C. Inferred or implied goodwill method

When a prospective buyer of a business agrees to pay more than the value of the business taken over, the difference between the purchase price and actual value of the business is known as inferred or implied goodwill.

Example

If the Assets worth 1,000,000 Tshs along with the liabilities of Tshs.30, 000 Tshs are taken over by a buyer for Shs.1, 000,000 then the goodwill is;

Goodwill = Purchase Price – Value of the business

= 1,000,000 = [1,000,000 – 30,000]

= 1,000,000 – 970,000

:. Goodwill 30,000

D. Valuation by bargaining (arbitrary valuation)

- The value of goodwill is decided by direct bargaining between the buyer and seller.

- For examination purposes such an amount is usually mentioned.

ACCOUNTING TREATMENT OF GOODWILL ON ADMISSION

There are two methods in which goodwill can be accounted in the books on admission

(a) When the goodwill is not appeared in the books

(b) When the goodwill is already appearing in the books (in the balance sheet)

(c) When goodwill is not appearing in the books

(d) When new partner pays cash for goodwill, it is always equal to his share in the total goodwill.

MODE OF PAYMENT

(i) Cash paid to all partners outside the business or paid privately

(ii) Cash paid through the firm or business, such cash may be

(a) Raised in the business as additional working capital

(b) written drawn by old partners either full or partial

(iii) Goodwill raised in the books

- When the new partner cannot pay in cash for his share in goodwill and partners capital accounts will be raised rate-ably by raising or bringing in goodwill in the books.
- In this case goodwill must be recorded at it is full value ways.

(i) Goodwill raised and retained in the books at full value

(ii) Goodwill raised and written off either fully or partly

(iii) Goodwill raised without opening goodwill account in the books

b) When the goodwill is already appearing in the Books

- When goodwill appears in the books (Appeared in the Balance sheet) it means it has been already recorded and credit given told partners
- Therefore new partner need not to contribute for goodwill
- If new partner brings in cash for goodwill in this case should treated as additional capital and the goodwill should cancelled out.

ACCOUNTING ENTRIES FOR GOODWILL

1. **When no goodwill appears in the balance sheet**

- When incoming pays money for goodwill privately

In this there is no Entry.

2. **When incoming partners brings in cash and is retained in the business**

Debit: Cash a/c (with cash) brought

Credit: Goodwill a/c

Debit; Goodwill a/c (Old profit)

Credit; old partner's capital a/c (sharing ratio)

Example I

A and B are partners carrying on a Business, their profit sharing ratio is 3:2. They decide to admit C in the firm. Their new profit sharing ratio is 2:2:1 for A, B and C respectively C pays shs.10, 000/= as goodwill. These money were left into the business.

Required; Draw journal entries to record the goodwill

JOURNAL ENTRIES

DETAILS	DEBIT	CREDIT
Cash a/c (premium)	10,000	
Goodwill a/c		10,000
(being cash received for goodwill)		
Goodwill a/c	10,000	
A's capital (3/5 x 10,000)		6000
B's capital (2/5 x 10,000)		4,000
(being the distribution of goodwill		

III. When incoming partner pays ash for Goodwill and that money is withdrawn by old partners

Debit; Cash a/c (with Cash brought)

Credit; Goodwill a/c

Debit; Goodwill a/c

Credit; old partner's capital a/c

Debit; old partner's capital a/c

Credit, Cash a/c

(With old profit sharing ratio).

Example 2

X and Y are equal partners carrying on business as accountants and auditors they decided to admit W with share of profit to the business. W paid Shs.30,000 as goodwill in the business in cash. But old partners decided withdraw all the money paid for business.

Required

-Draw up Journal entries to receive the above.

JOURNAL ENTRIES

DETAILS	DEBIT	CREDIT
Cash a/c	30,000.00	
Goodwill a/c		30,000.00
being cash received for goodwill		
Goodwill a/c	30,000.00	
X capital a/c		15,000.00
Y capital a/c		15,000.00
being the distribution of good		
will to partners		
X capital a/c	15,000.00	
Y capital a/c	15,000.00	
cash a/c		30,000.00
being withdrawal of money paid		
for goodwill		

IV When Incoming Partner does not Bring Cash

- When new partner does not bring cash for goodwill the goodwill accounts is raised in the books of account is raised in the books of accounts and it is allowed to remain in the books.
- It is agreed to estimate the value of Goodwill for that particular business. However an adjustment is made in the old partners capital accounts in proportion to less suffered by old partners

ENTRIES

1. **ADJUSTMENTS**

Dr: New partner's capital a/c

Cr: Old partner's capital a/c

Dr: Goodwill a/c

Cr: old partner's capital a/c (With old profit sharing ratio).

Example

M and N are partners with PSR 3:2. They decided to admit O as a new partner to the business; they agreed new profit sharing ratio is 4:3:3 for m, N and O respectively. But it was further agreed that unrecorded goodwill of Shs 105,000.00 is to be raised in the Books of the firm.

Required; Show journal entries to show

(a) Loss suffered by M and N

(b) Goodwill shared by M and N

Determine the proportion of loss suffered on admitting O

	M	N	O
Old Profit sharing ratio	x =	x =	-
Less;			

New profit sharing ratio	
Gain/Loss Ratio	()

Determine O share of Goodwill

O share = Amount of Goodwill x sacrificed Ratio

= 105000 x () = 31,500

	DETAILS	DEBIT	CREDIT
a)	O capital a/c	31,500.00	
	M (2/3 x 31500)		21,000.00
	N (1/3 x 31500)		10,500.00
	(Loss suffered by admission		
	of O)		
b)	Goodwill a/c	105,000.00	
	(M 3/5 x 10500		63,000.00
	(N 2/5 x 10500		42,000.00
	Goodwill distributed to old		
	partners)		

REVALUATION OF ASSETS AND LIABILITIES

When a new partner is admitted is very important to revalue all assets depending on market value rather than in their cost or written down value.

Open revaluation account

INCREASE IN ASSETS	DR	CR
Debit; Asset a/c	xx	
Credit; Revaluation a/c		Xx

Decrease in assets		
Debit; Revaluation a/c	xx	
Credit; assets a/c		Xx
(c) Increase in Liability		
Debit; Revaluation a/c	xx	
Credit; Revaluation a/c		Xx
d)Decrease in liability		
Debit; Liability a/c	xx	
Credit; Revaluation a/c		Xx

II. **Revaluation Account results (Transfer)**

In case of Profit on revaluation

Debit; revaluation a/c

Credit; Capital a/c

In case of loss on revaluation

Debit; capital a/c

Credit; Revaluation a/c

Exercise

BALANCE SHEET AS AT 31/12/1997

Capital		**Fixed Assets**	

S - 20,000		Free hold property	20,000.00
D - 10,000	30,000.00	Motor cars	5,000.00
		office equipments	3,000.00
Creditors	5,000		
		CURRENT ASSETS	
		Stock	3,000.00
		Debtors	2,500.00
		cash at bank	1,500.00

On First January 1998, they admit John to bring in 10,000 as capital, the profit and loss sharing ratio is 3:1:1 respectively, old profit and loss sharing ratio 3.2.

The Asset to be revealed.

Freehold = 27,000

Motor cars = 4,000

Office Equipment = 2500

Stock = 3750

Unrecorded liabilities = 500

Creditors' overcast by 200

Required;

-Journal Entries

JOURNAL ENTRIES AS AT 1ST JANUARY, 1998

DETAILS	DEBIT	CREDIT	
Free hold property a/c	7,000.00		
Revaluation a/c		7,000.00	
Revaluation a/c	1,000.00		
Motor car a/c		1,000.00	
Revaluation a/c	500.00		
office equipment a/c		500.00	
stock a/c			750.00
Revaluation a/c		750.00	
Revaluation a/c			500.00
Unrecorded liabilities a/c		500.00	
Creditors a/c	200.00		
Revaluation a/c		200.00	

EXERCISE

Ofwang and Onyango are in partnership sharing Profit and loss equally. They decided to admit Othorong'ong'o on agreement that goodwill will value at Shs.600, 000/= is to be introduced in the books. Othorong'ong'o was required to produce capital equal to that of onyango after he has been credited with his share of goodwill. The new sharing is to be 4:3:3 respectively. The balance sheet before admission of Othorong'ong'o was as follows;

Fixed Assets		1,500,000
cash		200,000
		1,700,000
Financed by		
capital - ojwang	800,000	
- onyango	400,000	1,200,000
current liabilities		500,000
		1,700,000

Required

1. Journal Entries for Admission of Othorong'o
2. Immediate balance sheet after admission of Othorong'ong'o

Solution

JOURNAL ENTRIES

DETAILS	DEBIT	CREDIT
Goodwill a/c	600,000.00	
Partners capital		
Ojwang A/c		300,000.00
Onyango A/c		300,000.00
Partners capital A/c		
Ojwang A/c	240,000.00	
Onyango A/c	180,000.00	
Othorong'ong'o A/c	180,000.00	
Goodwill A/c		600,000.00
Cash A/c	520,000.00	
Othorong'ong'o A/c		520,000.00

OJWANG, ONYANGO AND OTHORONG'ONG'O STATEMENT OF FINANCIALPOSITION AS AT DATE.

Fixed Assets		1,500,000.00
Current assets		
cash at bank		720,000.00
		2,200,000.00
Financed by;		
Capital - Ojwang	860,000	
Onyango	520,000	
Othorong'ong'o	340,000	1,720,000.00
current liabilities		500,000.00
		2,200,000.00

Exercises (NECTA 2002)

1. Polpot and Golberg are in partnership with capitals of Shs 20,000,000 and shs.12, 000,000 respectively. The partnership agreement provided that profits shall be shared and after giving Goldberg a salary of shs 2,240,000 and giving both partner interest on capital at 8 percent annum.

The Net profit for the year was Shs.10, 320,000, Shs.40, 000 is to be written off the Goodwill Account.

Required,

- Write up the Appropriation Account for the years.

DR Profit and Loss Appropriation A/C CR

DETAILS	AMOUNT	DETAILS	AMOUNT
Partner salary		Net profit (from P&L)	10,320,000.00
Goldberg - 2,240,000	2,240,000.00		
Interest on capital			
Goldberg 960,000			
Polpot 1,160,000	2,560,000.00		
share of profit			
Goldberg 3,450,000			
Polpot 2,070,000	5,520,000.00		
	10,320,000.00		10,320,000

1. Queen and Malkia are in partnership with capital of Tshs.10,000,000 and Tshs 6,000,000 respectively. The partnership agreement provides that profit and losses shall be shared and after giving Malkia a salary of Tshs 1,120,000 and giving both partners interest on capital at 8 percent per annum.

   The results for the year show a net loss of Tshs. 1,824,000, sh. 200,000 is to be written off the goodwill a/c.

   Required;-

- Write up Appropriation account for the year.

DR PROFIT AND LOSS APPROPRIATION ACCOUNT CR

	TSHS		TSHS
Net loss	1,824,000.00	share of loss	
Interest on capital;		Queen (5/8 x 4,224,000)	2,640,000.00
Queen 800,000		Malkia (3/8 x 4,224,000)	1,584,000.00
Malkia 400,000	1,200,000.00		
Partner salary			
Malkia	1,200,000.00		
	4224,000.00		**4,224,000.00**

RETIREMENT OF A PARTNER

This is when a partner leaves partnership firms due to various reasons e.g. Age, limit.

Example; NECTA 2007

A, B, and C were carrying on a business as partner's sharing profit in the ratio of 5:3:2 respectively on 31st March 1991 their balance sheet stood as follows;

LIABILITIES	Tshs	ASSETS	Tshs
A	100,000.00	free hold premises	75,000.00
B	60,000.00	furniture &fittings	22,500.00
C	35,000.00	stock	69,840.00
Trade creditors	31,180.00	Trade debtors	26,900.00
outstanding expenses	2,745.00	Bills	10,000.00
		cash at bank	24,635.00

	228,925.00		228,925.00

C Retired on the above mentioned date on the following terms;

(a) Freehold Premises to be appreciated by 20%

(b) Furniture & Fitting to be reduced by Tshs 2,255

(c) Provision for doubtful debts to be created on trade debtors at 5%

(d) Goodwill account be raised by Tshs 60,000 the agree value of the firm's goodwill. The amount finally due to C be paid immediately A and B brings in Tshs 20,000 each to facilitate the payment. A and B agree to share profits in the ratio of 3:2 respectively immediately after c's retirement and write off goodwill account.

You are required to prepare;

-Partner's capital a/c

-Cash Book.

-The balance sheet of A and B for the year ended March 1994

DR PARTNER'S CAPITAL ACCOUNT CR

DETAILS	A	B	C	DETAILS	A	B	C
Goodwill A/c	36000	24,000	-	Balance b/d	100,000	60,000	35,000
cash A/c	-	-	49,280	Revaluation A/c			
Balance c/d	119700	77420	-	share of profit	5700	3420	2280
				Goodwill A/c	30,000	18,000	12,000
				cash A/c	20,000	20,000	-
	155,700	101,420	49280		155,700	101,420	49,280

DR CASH AT BANK CR

Balance b/d	24,635	To c's capital	49,280
A's capital	20,000	Balance c/d	15,355
B's capital	20,000		
	64,635		64,635

BALANCE SHEET FOR THE YEAR ENDED 31ST MARCH 1994

LIABILITIES	**AMOUNT**	**Fixed Assets**	**AMOUNT**
Capital		Freehold premises	90,000
A - 119,700		furniture & fittings	20,295
B - 77,420	197,120	Current Assets	
		stock	69,840
Current liabilities		Bills	10,000
trade creditors	31,180	Trade debtors 26,900	
outstanding expenses	2745	less;prov.for BD 1345	25,555
		cash at bank	15,355
	230,145		230,145

RETIREMENT OF A PARTNER:

We have discussed the accountancy problems that arise on admission of a new partner.

In this character, we shall look at the problems that arise on retirement or death of a partner which are;

(a) Treatment of Goodwill

(b) Revaluation of Assets and liabilities

a) Treatment of Goodwill;

on the retirement or death of a partner, his share of Goodwill will have to be valued in according with the terms of the partnership Deed, and in the absence of such provision in the Deed, by mutual agreement or understanding among the partner. Then one of the following courses may be adopted to give to the distribution in the Books of Accounts.

1. Goodwill raised in the Books:

   Entries are

   Debit; Goodwill Account,

   Credit: are all partners' (including retiring) Capital Accounts in their profit sharing proportions.

ii) Goodwill raised in the Books but immediately written off Entries are;

Debit; Goodwill Account

Credit; All partners' (including retiring) capital Access in their profit sharing proposition.

Debit; Remaining partner' (In new profit sharing proportion)

Credit: Goodwill Account.

iii). Only Goodwill share of the retiring partner is brought into books. The entry is,

Debit; Goodwill Account

Credit; Retiring partner (with his share)

It is advisable to write – off the goodwill to the remaining partners in the ratios in which they gain on the retirement.

It may be noted carefully that if Goodwill Account already exists in the books, entries for raising Goodwill should be made only for difference.

Illustration; Mukosa, Mosoke and Ochieng are partners sharing profit in the proportion of and respectively. Mosoke retires and the Goodwill is valued at Tshs 21,600/=. No Goodwill Account appears in the books of the firm. Assuming that Mukasa and Ochieng share future profit in the ratio of 5:3, pass entries for Goodwill if (a) Goodwill is raised in the books (b)Goodwill is raised and written – off (c)Goodwill share of the retiring partner only is brought into the books.

1968	**Particular**	**Debit**	**Credit**
CASE A	Goodwill account raised		
	Goodwill A/c	21600	
	To Mukasa capital A/c(4/9)		9600
	To Musoke's capital A/c(3/9)		7200
	To Ochieng's A/c (2/9)		4800
	(value of Goodwill raised		
	on Musoke's retirement		
CASE B	Goodwill Account raised but w.off		
	I) Goodwill A/c	21600	
	To Mukasa's capital A/c (4/9)		9600
	To Musoke's capital A/c(3/9)		7200
	To ochieng's capital A/c (2/9)		4800
	value of Goodwill raised on		
	Musoke's retirement		
	II) Mukasa's capital A/c (5/8)	13500	

	Ochieng's capital A/c(3/8)	8100	
	To Goodwill A/c		21600
	C Goodwill written off to		
	remaining partners in their		
	new profit sharing ratio		
CASE C	Only Musoke's share of		
	Goodwill		
	I) Goodwill account	7200	
	To Musoke's capital account		7200
	C Musoke's share (3/9) of		
	Goodwill will be paid.		
	II) Mukasa's capital A/c(13/24)	3900	
	Ochieng's capital A/c(11/24)	3300	
	Musoke's capitl A/c		7200

REVALUATION OF ASSETS AND LIABILITIES

After ascertaining the share of good will payable to the retiring partner. The next problem that arises in the revolution of assets and liabilities for the purpose of ascertaining the fair amount due to the out-going partner in respect of his share of firm's assets.

Even if the partnership deed is silent on this point Assets and liabilities should normally be valued. The partner can, of course, agree not to revolve the assets and liabilities either on retirement or death or on both but such provision in the Deed is, that the balance of his capital Account represents his true interest in the partnership. Apart from the question of Goodwill which has already been dealt with some of the assets may have appreciated in value without any adjustment having been made in the books, whilst others may have been insufficiently depreciated or completely written-off.

A Revolution Account for profit and loss Adjustment (is prepared to which all differences in value are debited or credited as the case may be and the resultant balance is transferred to all the partners including retiring) in the

old profit sharing ratios. The Assets and liabilities appear in the books of the new firm at the changed values.

But if it's desired that Assets and liabilities should continue to appear in the books at the old values. A memorandum Revolution Account is prepared. It's balance will be transferred to all the partner in the profit sharing ratio's, and then the same account will be put on the reverse side and transferred to the remaining partners in the new profit sharing ratio.

Important Hints, Any reserve or accumulated profit appearing in the books should be transferred to all partners in their old profit sharing ratios. Alternatively only the retiring partner may be credited with his share and the remaining reserve side and transferred to the remaining reserve side and transferred to the remaining reserve may continue to appear in the books and the reduced figure.

Payment to the retiring partner.

When the accounting formalities are over, the final balance standing to the credit of a retiring partner's capital Account in paid either in cash (if cash position permit) or transferred to his loan account until it paid off. In the modern business world, some other method s are also evolved for payment of the amount such as÷

(i) Policy of survivorship assurance.

(ii) Annuity method.

(iii) Installment method

Example 1.

The balance sheet of A and B partnership, who are sharing profits and losses in the ratio 2:1 between A and B respectively as on 31st Dec 1984.

BALANCE SHEET AS AT 31ST DEC 1984

capital	A	100,000.00	Fixed Assets	
	B	50,000.00	plant & machinery	90,000.00
			furniture and fittings	20,000.00
current a/c	A	75,000.00	vehicles	50,000.00
	B	(5,000.00)		
Long-term liabilities		40,000.00		
current liabilities		20,000.00		
		280,000.00		280,000.00

On 1st January 1985 they decided to admit (into Partnership on the following terms;

(i) "C" to bring in Tshs.75, 000 in cash for his capital.

(ii) Profit sharing ratio to be 3:2:1 as for A, B and C respectively

(iii) Goodwill to be revalued at shs12, 000/= but is not be maintained in the books "C" is to pay for his share of goodwill

(iv) Plant and Machinery Furniture and Fittings and Vehicle to be revalued at Shs120, 000, 15,000 and 70,000 respectively.

(iv) 5% of stock is absolute. 10% of Debtors to written off

(v) Current liabilities amounting to Tshs 500/= was overlooked

(vi) Long term liabilities to forge Tshs.2000/=

(vii) A and B are to pay Tshs 8,000/= in respect of the revaluation costs

Required;

show the following: - 1. Revaluation account 2.Bank account.

DR REVALUATION ACCOUNT CR

furniture & fittings	5,000.00	plant & machinery	30,000.00
stocks	4,000.00	vehicles	20,000.00
provision for bad debts	3,000.00	long term liabilities	2,000.00
revaluation costs		current liabilities	5,000.00
A - 5333			
B- 2667	8,000.00		
To partners current A/c			
A - 24,667			
B- 12,333	37,000.00		
	57,000.00		57,000.00

DR PARTNER'S CURRENT ACCOUNT CR

Details	A	B	C	Details	A	B	C
Balance b/d	-	5000	-	Balance b/d	75,000	-	-
				revaluation costs	5333	2667	
balance c/d	105,000	10,000	-	revaluation(profit)	24667	12,333	-
	105,000	15,000	-		105,000	15,000	

A, B & C BALANCE SHEET AS AT DATE

Capital A/c A - 102,000		**Assets**	
B - 50,000		furniture &fittings	15,000
C - 73,000	225,000	plant &machinery	120,000
		vehicles	70,000
CURRENT A/C		Current Assets	
A - 105,000		stock	76,000
B - 10,000	115,000	bank	85,000
Long-term liabilities	38,000	debtors 30,000	
current liabilities	15,000	less; provision .for BD 3000	27,000
	,		
	393,000		393,000

BALANCE SHEET AS AT 1ST JAN 1998

Capital S; 23750		**Fixed Assets**	
D; 12,380		Freehold premises	90,000.00
J; 10,000	45,950.00	Motor cars	4,000.00

		office equipment	2,500.00
CURRENT LIABILITIES		**Current Assets**	
Creditors	4,800.00	stock	3,750.00
Unrecorded liabilities	500.00	Debtors	2,500.00
		cash at bank	11,500.00
	51,250.00		51,250.00

PARTNERSHIP (CONTRACT).

Death of a partner:

From the Accountancy point of view, the only difference between retirement and the death of the partner is that in the former case the retiring partner's share if not paid at once is credited to "loan Account" in the name of the outgoing partner, where as in the case of a partner is death, the adjusted balances of a capital and current Accounts of the deceased partner are transferred to an account called "Executor's to Deceased" pending payment.

There are no special problems of death except that death may occur any time of the year and this would mean Executors of the deceased partner would be entitled to his share of profit arising after the last closing up to the date of his death.

Death/Retirement.

Treatment of Goodwill

Goodwill Account existed before retirement or death.

(i) Increase in values Goodwill

DR; Goodwill A/c

CR; All partners' capital A/c, In old sharing ratios

(ii) Decrease in values of Goodwill.

DR; All partners' capital A/c

C/R; Goodwill A/c, In old sharing ratios.

Admission of New Partner.

Treatment of Goodwill

A new partner pays as his/her share of Goodwill. If a new partner to pay a portion of his Goodwill in cash, such cash paid is called **PREMIUM**.

Entries;

Cash received from a new partner as his share of Goodwill

DR; Cash/Bank A/c

CR; Premium A/c

Premium is divided between old partners in old profit sharing ratio.

DR; Premium A/c

CR; Old partner's capital A/C

DISSOLUTION OF A PARTNERSHIP.
Is the situation whereby the firm ceases its operation and its property are disposed off.

REASONS FOR DISSOLUTION
Partnership firm or organization may dissolve due to the following reasons;
(a) If entered into for a specific reason they by expire of that term.

(b) If entered for a single adventure by termination of that adventure.

(c) If entered for undefined time but one partner giving notice to other one his intention to dissolve partnership.

Upon dissolution the following are formulae to follow

(a) Open a realization account and debt it with the total of assets except cash or a debit balance of partners capital.

(b) Open account for cash, creditors, partner's loan (if any) partner's capital.

(c) Debit cash and credit realization account with the proceeds from sell of asset.

(d) Credit cash and debit realization account if any of the assets are not sold but are taken over by one of the partner then debit that partner capital account and credit realization account with the agreed value.

(e) Credit cash and debit realization account with the expenses of winding up.

(f) Pay off (a) creditors (b) partners loans i.e credit cash and debit these accounts.

(g) Balance the realization account and transfer the balance profit/ loss the partner's capital accounts.

(h) Balance partner's capital accounts and divide cash according to this credit balances of capital.

Example 1

Pendo and Upendo decided to dissolve their partnership on 31st Dec 2010. They shared profit and equally. Their balances as the date on dissolution were as follows.

Liabilities;			**Assets**		
capital			Premises	120,000	
Pendo	250,000		fittings	25,000	145,000
Upendo	200,000	450,000			
			Current Assets		

current liabilities	150,000	cash	30,000	
		stock	250,000	
		Debtors	175,000	455,000
	600,000			600,000

Additional Information's

(i) Sale proceeds were as follow from their Assets

(ii) Premises 140,000 stock was Tshs 270,000

(iii) Stock was 270,000 Debtors was 170,000

(iv) Upendo took over the fittings at an agreed Price of 20,000

(v) Dissolution expenses was Tshs.10, 000

Cash at bank Tshs.30, 000

Required;

Prepare the Necessary book of Accounts

DR REALIZATION ACCOUNT CR

Details	**Amount**	**Details**	**Amount**
premises	120,000.00	premises	140,000.00
fittings	25,000.00	stock	270,000.00
stock	250,000.00	Debtor	170,000.00
Debtors	175,000.00	Upendo (fittings)	20,000.00
Dissolution expenses	10,000.00		
To partners capital			
profit on realisation			
Upendo - 10,000			
pendo - 10,000	20,000.00		

	600,000.00		600,000.00

DR CASH ACCOUNT CR

DETAILS	AMOUNT	DETAILS	AMOUNT
Balance b/d	30,000.00	Dissolution Expenses	10,000.00
Premises	140,000.00	creditors	150,000.00
stock	270,000.00	Pendo	260,000.00
Debtors	170,000.00	Upendo	190,000.00
	610,000.00		610,000.00

DR PARTNER'S CAPITAL ACCOUNT CR

DETAILS	PENDO	UPENDO	DETAILS	PENDO	UPENDO
Realization (fittings)	-	20,000.00	Balance b/d	250,000.00	200,000.00
cash	260,000.00	190,000.00	profit on realization	10,000.00	10,000.00
	260,000.00	210,000.00		260,000.00	210,000.00

LOSS ON REALIZATION

Any Partner with a deficit capital Account must paying efficient cash to clear the deficit cash

GARNER VERSUS MURRAY'S RULE CASE;

This rule states that, in the event of a partner's insolvency share of deficiency shall be borne by solvent partner in their capitals and not in their P & L sharing ratio.

Example

Assume capital Account of A;B;C Tshs 200,000, Tshs 300,000, Tshs 100,000, C's capital A/c run top a debit balance of Tshs 95,000 thousand out of which he is able to pay 45,000 on his own bank A/c. This will leave a deficiency of Tshs. 50,000 in his capital a/c and this deficiency will be borne by A and B in the ratio of their capital immediately before dissolution.

Soln;

1. Tshs 200,000
2. Tshs 300,000

A share to C – x 50,000 =20,000

B share's to C= x 50,000=30,000

JOURNAL ENTRIES

DETAILS	DEBIT	CREDIT
Bank	45,000	
C's capital		45,000
A's capital	20,000	
B's capital	30,000	
C's capital		50,000

DR PARTNER'S CAPITAL ACCOUNT CR

DETAILS	A	B	C	DETAILS	A	B	C
C's capital	20,000	30,000		Balance b/d	200,000	300,000	100,000
Motor van	10,000			A's capital	-	-	20,000
Investment	-	80,000	-	B's capital	-	-	30,000
loss on realization	19,500	19,500	19,500	Realization expenses	-	600	-
	-	1,000	-	Cash	25,000	-	45,000
Balance c/d	175,000	175,500	175,500				
	225,000	306,000	195,000		225,000	306,000	195,000
				Balance b/d	175,000	175,000	175,000

AMALGAMATION OF PARTNERSHIPS

Amalgamation, this is when two or more firms join together to form a partnership firm.

Amalgamation can be between;-

1. A sole trader and sole trader
2. A sole trader and partnership
3. A partnership and a partnership

- Each business must choose its own books of accounts and transfer them to a new partnership firm
- But before closing the books of the following adjustment might own; Reserves are shared by partners in profit or loss sharing ratios of the old business.

CONDITION NECESSARY FOR PARTNERSHIP TO AMALGAMATE.

(a) To see each other Balance sheet presents a true statement of financial position of each business.

(b) Asset must be stated at their fair value and all liabilities to be disclosed.

Unequal goodwill of the business will be assessed accordingly at the time of amalgamation by making the right allowances to compensate the owner of the more valuable business.

(c) Balance sheet business is redrafted taken into consideration the adjustment agreed up and this re-drafted balance sheets is then combined to form the initial balance sheet of the partnership. Statement used in the process of Amalgamation.

Statement used on the Process of Amalgamation

(a) A completed and signed copy of form of articles of amalgamation

(b) A completed and signed copy of form of initial registered office address and first board of directors.

(c) A statutory declaration from a director or office of each amalgamation/corporation

(d) Name search report unless the amalgamated corporation will use the corporate name of the amalgamation corporation

(e) B/sheet of the two amalgamations

PAYROLL ACCOUNTING/EMPLOYEES PAY

All business entities have to pay employee's for the services. An employee is the one who perform services, subject to the supervision and control of another part known as an employer.

Relationship between employee and Employer

The employer has the power to terminate services offered by the employee.

Employer sets the hours of work for the employee's. The employer provides to the employees with place to work.

Objective of Payroll Accounting

-To provide accurate payment of remuneration to employee promptly

-To provide and maintain the necessary employee and employer record statements and any report relevant to and required by the government agencies and statutory.

-To prevent fraud

-To control salaries and wages expenses

Employees are paid either a wage or a salary. If you see an advert for a job and it mentions that the rate of pay will be pound 8 per hour that is an example of a wage. If on the other hand, an advert refers to an annual amount that is a salary.
Wage is paid daily or weekly depending on hours worked WHILE Salary is paid at the end of every month.

Basic Pay

Is made up of an employee's remuneration fixed at the time of employment before taking accounts of other benefits.

- Salary are not linked to weekly or piece rate, they are paid on a monthly basis
- Wages are associated with employee's paid weekly, often on the basis of a piece of an hourly rate.

<u>Monetary Benefits</u>

There are certain benefit's some time are accrue, to employee's when such benefits are received in monetary form they increase employee's

monetary earning and are part of payroll form e.g. transport allowance, Housing Allowance.

Some of the benefits are exempt from tax and some are not. It is important to distinguish the tax status in order to compute. (Pay as you earn) Tax.

Gross Pay

Is obtaining by the summation of all sources of employee's and overtime payments. Gross means before deductions.

PAYROLL DEDUCTION AND STATUTORY CONTRIBUTIONS

Payroll accounting is significant influenced by legislation and acted by government. This law affects payroll accounting because they levy taxes based on payroll amounts and their exactly statutory contribution by both employer and employee.

1. STATUTORY CONTRIBUTIONS

(a) Payee tax (Pay as you earn)

Income tax Act (1973) and financed bills passed each budget session governed payment of individual tax. Is a tax levied on monthly income of individuals.

Monthly income for this purpose will be Gross pay reduced by earning which are not taxable.

(b) NSSF, PPF, PSPF, LAPF NHIF and Others

NSSF Act requires every employee and employer toward the fund. Upon retirement a lump-sum is paid to employee from the fund depending on his contributions;

(i) Employee contribution (10% at the basic pay)

(ii) Employer contribution (10% at the basic pay)

Others

PPF 5% to be contributed by the employee and 15% be contributed by the employer.
PSPF employee and employer contribute 10% each on basic salary.

2. DEDUCTIONS

Salary Advances and Staff Loans

Employees will sometimes want to receive their salary or part of their salary of in advance. At the end of the month an employee's net pay must be reduced by the salary receive before the month end.

Loans are advances to staff to be received in more than one month. Usually there will be an agreement as to athere at of loan repayment.

Repayment Installments will be reduced from an employee Net pay.

Voluntary Deductions

Employee can choose to contribute towards any organization. Individual. In this case written employee concern and the stated amount will be deducted from the employee's salary and resettled by the employer to the stated person e.g. Lion Club, Rotary Club, Simba Club etc.

PAYROLL RECORDS

Employer's are required to maintain records with information of each employee salary and hours worked the rate of pay, Total overtime, entitlement and additions to salary, reductions from salary and employee's net salary pay.

Employee's earning statement (Salary slip)

This record contain information on the employee earning and reductions, clearly analyzed and showing how net pay has been arrived at the end of each month this statement is sent to every employee to communicate her earning information of the month. This statement is known as Salary Advice or Salary Slip.

SALARY ADVICE OR SALARY SLIP

Name of employee		
No		
Basic pay		xxx
Add; overtime payment	xx	
Transport allowance	xx	
Rent allowance	xx	
Meal allowance	xx	
Gross pay		xxxx
less; Deductions		
salary advance/loan	xx	
Trade union	xx	
NSSF / PPF / LAPF/GEPF/NHIF	xx	
P.A.Y.E	xx	
xx	xxx	
Net pay		xxxx

Example I

Silunka Company has four persons (all married) and pays the weekly salaries. The detail of the firm is as follow,

Name	Weekly Pays (Tshs)	Deduction per week Medical Insurance (Tshs)
Aisha	7500	300
Safina	8000	300
Blandy	7800	400

Pyurity	6200	300

Addition Information

(i) Each employee pays 5% for income tax per week.

(ii) All employees contribute 10% monthly for PSPF.

Required;-

(a) Prepare the payroll journal for the month of June, 2006 using the headings which will accomplish the purpose.

(b) Using a general journal as a Memorandum record only, prepare a journal entry to record the payroll.

Payroll Journal (Summary for the Month of June 2006

S/N	Name of Employee	Basic pay	Gross pay	Income tax	Medical insur.	PSPF	Net pay
1	Aisha	30,000	30,000	1500	1200	3000	24,300
2	Safina	32,000	32,000	1600	1200	3200	26,000
3	Blandy	31,200	31,200	1560	1600	3120	24,920
4	Pyurity	24,800	24,800	1240	1200	2480	19,880
	TOTALS	**118,000**	**118,000**	**5900**	**5200**	**11,800**	**95,100**

JOURNAL ENTRIES

DATE	PARTICULARS	DEBIT	CREDIT
	Salary expenses a/c	118,000	
	Income Tax payable a/c		5,900

	Medical Insurance payable		5200
	PSPF a/c		11,800
	Net pay a/c		95,100
	being recognition of		
	payable salary		
	Profit & loss a/c	118,000	
	salary expenses		118,000

Payroll Summaries/Journal

Some organization will have several departments or operating units. Usually payroll is prepared along departmental lines. From the information on the salary slip, it should be possible to prepare a payroll summary for the department.

KIBASILA HIGH SCHOOL

ECA DEPARTMENT

PAYROLL SUMMARY /JOURNAL MONTH ENDING.....

Employee's name	Basic pay	Gross pay	Advance	Loan	P.A.Y.E	NSSF	Net pay
Juma	89,000	110,000	40,000	-	8,630	8,900	52,470
Rashid	120,000	135,000	-	60,000	12,380	12,000	50,620
Mary	86,000	120,000	-	-	10,120	8,600	101,280
Frida	150,000	160,000	50,000	-	16,620	15,000	78,380
George	140,000	158,000	-	70,000	16,620	14,000	57,780

TOTALS	**585,000**	**683,000**	**90,000**	**130,000**	**63,970**	**58,500**	**340,530**

From the Departmental Payroll summaries it should be possible to prepare an organization summary.

This would be a list of departments together with department totals of contents of salary slips.

KIBASILA HIGH SCHOOL

ALL DEPARTMENTS

PAYROLL SUMMARY MONTH ENDING

DEPARTMENT	BASIC PAY	GROSS PAY	ADVANCE	LOAN	PAYE	NSSF
ECA	585000	683,000	90,000	130,000	63,970	58,500
HGE	490,000	525,000	90,000	60,000	47,750	44,500
EGM	229,000	268,000	40,000	70,000	24,850	22,900
TOTAL	**1,304,000**	**1,476,000**	**220,000**	**260,000**	**136,570**	**125,900**

ACCOUNTING ENTRIES

Payroll Accounting involves accounting Principles and techniques covered previously;

In some organization payroll entries passed to the General ledger directly, in this case, the payroll summary act as a special Journal.

But, in most cases, payroll summary is not part of double entry, it only save as a working paper, for preparation of General Journal. Kibasila High School. Payroll summary for all departments will be recorded in general Journal basis/follows:

Dr, ECA salary Expenses	683,000	
Dr; HGE Salary Expenses	525,000	
Dr; EGM Salary expenses	268,800	
Cr; Salary Advance		220,000
Cr; Loans		260,000
Cr; PAYE		136,570
CR; NSSF Payable		125,900
CR, Salary Expenses (Payable)		733,530

One transaction that needs recording is employer's contribution to NSSF since it is 10% of each employee's

Basic pay will be Tshs. 125, 900

Dr, NSSF Employers Contribution 125,900

Cr, NSSF Payable 125,900

At the end of the month

Dr; Salary payable 733,530

CR; Cash A/C 733,530

Being payment of salaries to employee's

DR, NSSF payable 251,800

Cr, Cash A/C 251,800

Remittance to NSSF employee's and employer contribution

DR, P.Y.E 136,570

Cr, Cash 136,570

Mode's of Payment of salaries

i) Currency (notes & coins)

ii) By cheques

iii) Credit transfer to employees bank account.

Overtime Payments

Usually employees are required to work 8 hours a day, 40 hours a week or 176 hours a month.

If an employee works more than he mentioned hours about the entitled to overtime payment.

On a normal working day overtime is paid at one and half times the normal rate of pay.

On weekends or Holidays overtime is paid at twice the normal rate of pay.

Formula for overtime Payments;- (Basic pay x factor x hours of overtime)/(176 hrs)

Example 1

HGK Company employs four people, each of whom is married, whose monthly salaries are;

Sadiki	Tshs	85,000
Zuberi	Tshs	90,000
Rehema	Tshs	96,000
Mgaya	Tshs	120,000

Determine the correct amount of P.A.Y.E and Net Pay for each employee

Additional Information;-

Income Exceeds Tshs 65,000 but not exceeds Tshs.85,000 is Tshs 9500 plus 5% of the Excess of Tshs 65,000

Income Exceeds Tshs 86,000 but not exceeds Tshs.100,000 is Tshs 10,500 plus 6% of the excess of Tshs.86,000

Income Exceeds Tshs 100,000 but not exceeds Tshs.120,000 is Tshs.11,500 plus 15% of the excess of Tshs.100,000.

Solutions

Payee for SADIKI and Net Pay

= (85,000 – 65,000) x 5% + 9500

= 1000 + 9500

= **10,500**

Net Pay = 85,000 – 10,500

= 74,500

ZUBERI

PAYE = 240 + 10,500

= 240 + 10,500

= 10,740

Net pay = 90,000 – 10740

= 79,260

REHEMA

PAYE = (96,000 – 86,000) x 6% + 10,500

= 600 + 10, 500

= 11,100

Net pay = 96,000 – 11,100= 84,900

MGAYA

PAYE = (120,000 – 100,000) x 15% + 11,500

= 20,000 x 15% + 11,500

= 3,000 + 11,500

= 14,500

Net Pay = 120,000 – 14,500

= 105,500

Example 2

In the following summary of data obtained from 1 MICU Company's payroll records some amounts have been intentionally omitted.

	Earnings	Tshs
I	Basic Pay	-
Ii	Overtime	504,000
Iii	Gross Pay	-
	Deductions	
Iv	PAYE Tax	-
V	NSSF (on Gross pay)	580,650
Vi	Worker association contribution	77,000
	Total deduction	2,087,750
	Net pay	-

	Account debited	
Ix	Factory Wages	2,124,500
X	Sales salaries	-
Xi	Office Salaries	1,652,000

Required

-Determine amounts omitted in (i) (iii), (iv), (Vii) and x

Workings

If 580,650 = 10%

Then x = 10%

x= 580650 x 10

x = 5,806,500

: Gross pay 5,806,500

Basic Pay = Gross pay – Overtime

= 5,806,500 – 504,000

Basic pay =6,310,500

PAYE Tax = Total deduction – Worker Association –(on Gross pay)

= 2,087,750 – 77,000 – 580 650

= 1,430,100

PAYE Tax 1,430,100

Net pay = Gross pay – Total Deduction

= 5,806,500 – 2,087,750

= 3,718,750

(x) Gross pay and NSSF (Employer contribution = Salaries Expenses)

5806 500 + 580,650 = 6,387,150

Salaries Expenses 6,387,150

Sales salaries = Salaries Expenses – Office Salaries – Factory Wages

= 6,387,150 – 1,652,000 – 2,124,500

= 2,610,650

EXERCISE

The following are details related to the coming of two Employees during the week ended 28/2/2001.

Employee	Omega	Alfa
Piece work rate per unit	240	260
Units produced	400	280
Hours Worked	40	44
Hourly rate of pay	750	820

A 40 hours week is in operation and overtime is paid at time and quarter. If an employee's piece work earnings fall below his earnings rate at the hourly rate, then the hourly rate then the hourly rate earning are paid. Both employees have the following deductions.

Pension Scheme – 2% of Gross pay.

NSSF – 10% of Gross Pay.

PAYE – 25% of all earning in excess of 150% per week your are required to calculate the Gross and Net wages of each employee showing clearly the amount of each deduction.

CONTAINER ACCOUNTS

CONTAINER ACCOUNTS

What is a container?

Container is anything in which goods are contained.

Container is used in parking goods. Examples are the cigarette packets, bottles, crates, gas cylinder etc.

Types of containers.

1. Non returnable containers
2. Returnable container

1. **NON – RETURNABLE CONTAINERS**:-

   Like; cigarette packets

These are the containers which no charge is made to customers. They are usually disposed off by the customer at will. Usually the containers for such items as cigarette, foods are an integral part of the goods sold. Therefore the cost for the containers should be taken to the manufacturing A/C as it is part of the factory/pan cost. But if the containers and the contents are regarded as distinct items the cost of such containers is a distribution expenses and so taken to a profit and loss A/C.

2. **RETURNABLE CONTAINERS:**

   Example: gas cylinder

These are the containers which a customer is required to return to its container and a refund being made once the container is return to the supplier within time stipulated and in a good condition.

Deposit is charged to the customer, the customer may with hold the container after use.

The deposit should be enough to discourage the customer from, with holding the container but it should not be too much to make goods unaffordable.

Deposit = charge out price

Refund = credit back price

Usually the customer is refunded with an amount less than that given by him as deposit. The difference is called **Hiring charge.**

Hiring charge = charge out price - credit back price.

ACCOUNTING PART.

In the supplier's books two accounts can be opened, these are the container stock A/C and container suspense A/C.

CONTAINER STOCK A/C

It shows the movement of contained owned by the supplier to and from the warehouse.

It can also be used in determining a profit / loss on container. Usually a valuation of stocks. Both at the supplier's premises and those held by customers (time not expired) are made. Both stocks at the start and end of a period are shown in this account.

DR CONTAINER STOCK ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT

CONTAINER SUSPENSE A/C

It shows deposits returnable to customers.

It's ruling – same as the container stock A/C.

JOURNAL ENTRIES / ACCOUNTING ENTRIES

1. For the stocks (both open and close) of containers in the customers hands + at the supplier's Premises.

   For opening stocks - debited to the container stock A/C as balance b/d

   For closing stock - Credited to the container stock A/C as balance c/d

   The valuation figure is in use.

2. Purchase of new containers for cash

   Dr Container stock A/C

   Cr cash A/C

1. Sale of containers for cash

   Dr Cash A/C

   Cr container stock A/C

2. Repair charge for containers

   Dr Container stock A/C

   Cr cash A/C

3. For opening and closing deposit returnable stock with customer.

For opening stock - credited to the container suspense A/C as b/d.

For closing stock - debited to the container suspense as c/d

4. For charge out price (container sent/ charged / invoiced to customer)

Dr. Container suspense A/C

Cr. Container Debtors A/C with charged out price

1. For credit bank price (containers returned by the customer to the supplier)

Dr Container suspense A/C

Cr container debtors A/C With credit back price

1. For containers retained by customers (time expired)

Dr Container suspense A/C

Cr container stock A/C with credit back price

For hiring charge i.e. charge out price > credit back price

Dr Container suspense A/C

Cr container stock A/C

N.B :-

After all the appropriate entries have been made in container A/C the balance. Figure represent the profit or loss of container uses.

Example

Kimburumatari supplies gas in expensive containers which are returnable. These containers cost Tshs 20 each and are charged out to customers at Tshs 30. Provided they are returned within six months, they are credited at Tshs 25 each. At the end of the year the company valued all returnable in containers customers hands and customers held on stock at Tshs 15 each.

You are provided;-

	Beginning of the year	End of the year
container held by company	2760	3144
Returnable container	4760	

During the year some containers were purchased, 20,620 were invoiced to customers and 17,980 were returned, 1,000 containers were held by the customers beyond the time stipulated. On inspection 260 containers were repaired costing Tshs 325,56 containers had to be sold as scrap for Tshs 600, 400 containers were lost in container dealers premises.

Required:-

1. Container stock A/C
2. Container suspense A/C

DR **CONTAINER STOCK ACCOUNT** **CR**

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	A
Bal. b/d at premises	2760	15	41400	cont;susp;retained	1000	25	25
- with customers	4790	15	71850	cash;scrap & sold	56		
cash; repair			325	containers lost	400		
cash; purchases	3480	20	69600	cont; suspilting charge			10
31/12/profit on container			89135	Bal. c/d premises	3144	15	47

				- customers	6430	15	96
	11,030		272310		11,030		27
balance b/d - premises	3144	15	47160				
customers	6430	15	96450				

DR CONTAINER SUSPENSE ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT
Returned	17980			Deposit returnable b/d	4790	25	119750
hiring charge			103100	charged/sent to			
Retained	1000	25	25,000	Customers	202620	30	618600
Deposit returnable c/d	6430	25	160,750				
	25410	-	738350		25410	-	738350
				Balance b/d returnable	6430	25	160,750

If you are told to open balance sheet

BALANCE SHEET

CURRENT LIABILITIES		CURRENT ASSETS	
Deposit returnable	160,750	Stocks - at prem.	47160
		Customers	96450

EXERCISE

1. Daramu ltd sell their products in containers which cost Tshs 50 each. They are charge out to customers at Tshs 100 and credited at Tshs 75 each if returned in good condition within three month. At the year end all containers owned by the company, whether within the factory or in the customers hands are valued at Tshs 25 each for accounting purposes.

On 1st January 1996 the company owned 24,000 containers in the factory and 30,000 containers which had been in the hands of customers for less than three months.

During 1996, 20,000 containers were purchased, 60,000 were returned within the prescribed period and 2,000 were receipt by customers over the three months limit 800 containers were sold for shs 20 each during the year, 300 were scrapped, and when the stock was taken on 31st Dec 1996 there was a deficiency of 900 containers.

On 31st 1996 the company owner 38,000 container in the factory and 32,000 containers which had been in the hands of customers for less than the three months.

Required

To prepare for the year 1996

1. Containers stock A/C
2. Containers suspense A/C

2 .A firm carrying on business as pottery manufactures market their own packing cases, which are charged to customers at 100 percent over cost, but are returnable, full credit being give.

The following are the items relating there in respect of the year ended 31st Dec 1999:-

	Tshs
Stock of cases, 1-1-1999	596
Case in hand of customers as per ledger	
Balances (1-1-1999)	840
Cases charged to customers	3140
Materials used	38
Wages paid for marking and repairing cases	156
Cases returned by the customers	3260
Cases paid for by customers (retained)	140
Stock of case in factory (31-12-1999)	280

The cases in the hands of customers were valued at cost less 20%.

Required:-

1. Container stock A/C
2. Container suspense A/C

SOLUTION (1)

DR CONTAINER STOCK ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT
Bal. b/d - premises	24,000	25	600,000	sales	800	10	8,000
- customers	30,000	25	750,000	loss on container	900		
cash purchases	20,000	50	1,000,000	scrapped	300		
Profit			1,158,000	Retained	2,000	75	150,000
				hiring charge			1,600,000
				balance c/d - factory	38,000	25	950,000
				- customer	32,000	25	800,000
	74,000		3,508,000		74,000		3,508,000
Balance b/d - premises	38,000	25	950,000				
customers	32,000	25	800,000				

DR CONTAINER SUSPENSE ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT
Returned	60,000	75	4,500,000	deposit returnable b/d	30,000	75	2,250,000
Retained	2000	75	150,000	charge out	64,000	100	6,400,000
hiring charge			1,600,000				
Deposit returnable c/d	32,000	75	2,400,000				
	94,000	-	8,650,000		94,000	-	8,650,000

				Deposit returnable b/d	32,000	75	2,400,00

SOLUTION (2)

DR CONTAINER STOCK ACCOUNT CR

DETAILS	AMOUNT	DETAILS	AMOUNT
Balance b/d - premises	596	Retained cases	140
customers	336		
material used	38	loss on container	474
Repairs	156	Balance c/d: premises	280
		Customer	232
	1126		1126

DR CONTAINER SUSPENSE CR

DETAILS	AMOUNT	DETAILS	AMOUNT
Returned	3260	Balance b/d	840
Retained	140	Charged to customers	3140
hiring charge	580		
	3980		3980

Valuations:

Opening stock with customers. Cost - 100 x cost

= 840 - ½ x840 = 420

= cost - x cost = 420 x 420 = 336

= closing stock = 580 - ½ x 580 = 290

= 290 - 20/100 x 290 = 237

STATEMENT OF PROFIT OR LOSS ON CONTAINER

Hiring charge(charge out price -credit back price) x containers sent	
Add; profit on containers retained;(credit back - valuation)	
No. of containers retained.	
Deduct ; Depreciation of containers (cost of new container - valuation)X New container bought xx	
new container bought	
Repairs	xx
loss on container scrapped & sold ; sales - (valuation of container) x (No. of container) xx	
Profit on container	

The use of containers trading A/C

In this case the container trading A/C will be used in determining a profit or loss on container.

The container stock A/C will then be used in deducing an amount for depreciation of containers.

DR CONTAINER STOCK ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE
Balance b/d -premises	x	valuation	xxx	c.retained	xx	Value
customers	x	valuation	xxx	c.scrapped	xx	Tion
cash purchases	xx	cost price	xxx	depreciation		
				31/12/ bal.c/d premises	xx	Value
				- customers	xx	Tion
	xxxx		xxxx		xxxx	

DR CONTAINER TRADING ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT
Returned	xx	CR back price	xxx	opening deposit return	x	credit back price	xxx
Retained	xx	valuation	xxx	charged to customer	xxx	charge out .pr	xxx
Scrapped	x	valuation	xx	sale of container			
Depreciation			xx	scrapped	x	Valuation	xx
Repairs			xx				
Profit			x				
		credit					
closing deposit	xx	back price	xxx				
			xxxx				xxxx

DR CONTAINER DEBTORS CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT
1/1 Bal.b/d	x		xxx	Returned		CR back	xx
				Receipt			xx
Trading to customer	xxx	Charge out price	xxx	Retained	xx		-
				31/12 Bal.c/d	xx		xxx
	xxx		xxxx		xxx		xxxx
Balance b/d	xx		xxxx				

EXERCISE

Pankraparcrimparcat co ltd sells oil in drums which are charged at Tshs 10 each. Customers returning drums within a month are credited with Tshs 7.

The following information is available from the books:

1. Drums returnable on 1.1.999 4000
2. Drums in stock as on 1.1.999 8000
3. Drums purchased in 1999 at Tshs 5 each 30000
4. Drums sent out in 1999 500000
5. Drums returnable by customers 480,000
6. Drums scrapped in 1999 (sold for 6000) 2000
7. Drums sent out in Dec 1999 lying with customers 10000
8. All drums at 31st Dec 1999 are to be valued at 50% of the cost price
9. All drums as on 1.1.1999 were valued at Tshs 2/50 each
10. Amount received from drum debtors as on 1.1.1999 was Tshs 1580000

Required:-

1. Prepare the drums trading account and drums debtors A/c

2. Prepare a statement of profit of loss on drums for the year ended 31st December 1999.

DR DRUMS STOCK ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	A
Bal.b/d -premises	8000	2.5	20,000	Drums Trading scrapped	2000	2.5	5
with customers	4000	2.5	10,000	Retained	14,000	-	4
cash;purchases	30000	5	150,000	Depreciation			6
				Bal,c/d - premises	16,000	2.5	4
				- customer	10,000	2.5	2
	42,000		180,000		42,000		1
Balance b/d premises	16,000	2.5	40,000				
customer	10,000	2.5	25,000				

DR DRUMS DEBTORS ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT
Drum D Returned	480,000	7	3,336,000	Bal.c/d	4,000	7	28,000
Drum stock scrapped	2000	2.5	5000	Drum debtor sent	500,000	10	5,000,000
Retained	14,000		45,000	cash sale of scrapped	2000		6000
Depreciation			65,000				
Profit			1,489,000				

31/12 Bal.c/d	10,000	7	70,000				
	506,000		**5,034,000**		**506,000**		**5,034,000**

FIFO method is used:

Valuation drum retained = 10000 @2.50 = 25000

4000@5 = 20000

45000

Statement to profit or loss

Hiring charge = (10 - 7) 500000	1500000
Add: profit on co. Retained = (7-2.50) 14000	63000
	1563000
Deduct: depreciation = (5 -2.50) 30000	7500
Loss on sales = 6000 - (2.50 x 2000)	1000
Profit	1487000

EXERCISE

Madras chemicals ltd supply their products in returnable drums which are charged out at Tshs 20 each. Customers returning the drums within a month are credited with Tshs 18. The company's procedure is to retain Tshs 18 in deposit account till the expiry of the option period for return of the drums.

The following particulars are available from the drums:-

	Numbers
Returnable drums are as on 1.1.1991	8000
Drums in stock as on 1.1.1991	16000
Drums purchased during 1991 at shs 15 per drum	20000
Drums sent to customers during 1991	300000
Drums returned by customers in 1991	288000
Drums returnable on 31.12.1991	15000
Drums scrapped in 1991 sold for Tshs 10000	2000

All drums as on 31.12.90 and 31.12.91 are to be valued at Tshs 10 each. All the amounts due in respect of drums had been collected from the customers

You are asked to show the ledger a/c for 1991 for:-

1. Drums stock.
2. Drums debtors
3. Drums trading a/c

DR DRUMS STOCK ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT
Balance b/d - premises	16,000	10	160,000	scrapped	2,000	10	20,000
with customer	8000	10	80,000	Retained	5000	10	50,000
purchases	20,000	15	300,000	Depreciation			100,000

				Balance c/d - premises	22,000	10	220,000
				customer	15,000	10	150,000
	44,000		**540,000**		**44,000**		**540,000**
balance b/d - premises	22,000	10	220,000				
with customers	15,000	10	150,000				

DR DRUMS TRADING ACCOUNT CR

	QTY	RATE	AMOUNT		QTY	RATE	AMOUNT
Returned	288,000	18	5,184,000	Balance b/d	8,000	18	144,000
Scrapped drum stock	2000	10	20,000	Drum debtor sent	300,000	20	6,000,000
Retained	5000	10	50,000	sale on scrapped	2000		10,000
Depreciation			100,000				
profit			530,000				
Balance c/d	15,000	18	270,000				
	310,000		**6,154,000**		**310,000**		**6,154,000**

DR DRUMS DEBTORS ACCOUNT CR

DETAILS	QTY	RATE	AMOUNT	DETAILS	QTY	RATE	AMOUNT
Balance b/d	8,000		80,000	Returned	288,000	18	5,184,000
Drum Tr				Retained	5000		

Drum Trading sent	300,000	20	6,000,000				
				Balance c/d	15,000		896,000
	308,000		6,080,000		308,000		6,080,000
Balance b/d	**15,000**		**896,000**				

Statement on profit:

Hiring charge = (20 - 18)
300000 600000

Add: purchase on retained = (18 – 10)
5000 40,000

64
0,000

Less: depreciation (15 – 10) 2000 100,000

Loss on sales = 10000 - (10 x 2000) 10,000

Profit 530,000

STOCK VALUATION

Concept;

Stock/inventory;

The Tanzania statement of Accounting Guidelines No 2 which deals with the valuation of inventories in the context of the historical cost system states that the term stock/inventories include the following;

1. Goods or other assets purchased
2. Consumable stores/consumer goods
3. Raw materials and components purchased for incorporation in its products for sale
4. Products and services in intermediate stages of completion
5. Finished goods
6. Long-term contract balance
7. Farms crops
8. Livestock

CLASSIFICATION AND COST

- Stock taking; Is the process of determining the quantities of all items of merchandize owned by the business firm at the certain date, usually at the end of accounting period. This involves the actual accounting, measure and weighing of all items of unsold merchandize (stock) in the store.
- Inventories/stock is classified as assets (currents) in the balance sheet as it is expected that this stock will be sold and be replaced within one accounting period.
- Accounting for inventories normally follows the cost concept which means stocks are recorded at acquisition cost or whichever is lower.

NOTE;

1. All items of due stock belonging to the business even those in transit have been included in the inventory figure.
2. All items of merchandize (stock) recorded in the inventory list are legally owned by the business.

STOCK COSTING METHOD

After determining the quantity of merchandize stock at the end of the accounting period, (the balance sheet date) the next step is to assign a cost to each item of merchandize in order to arrive at the value of the ending inventory to be presented in the financial statement

There are two stock/inventory systems which are;

1. Perpetual stock system
2. Periodic stock system

Certain assumptions are needed to be made on the flow of goods and their related costs.

1. First in first out (FIFO); the assumption is that the oldest items in the stock are the first ones sold. Under this method, the ending inventory is assumed to be comprised of the latest purchases. This is a logical assumption for businesses dealing in perishable goods; FIFO represents a natural flow of merchandize.
2. Last in first out (LIFO); the assumption is that, the most recent items in stock are the first ones sold. Example of these is fashionable goods. Under this method the ending stock is assumed to be comprised of the earliest purchases.
3. Average cost (AVCO), the stock items has been intermingled, so that the goods sold and the ending stock consists of mixed units. Under this method a weighted average unit cost is calculated for all stock items.

W.A.C= Weighted Average Cost

W.A.C = (Total cost purchase + opening stock)/(Total unit)

PERIODIC

METHOD

$$\frac{(Units\ purchased x Unit cost) + (Opening\ sock\ units x unit\ cost)}{Total\ units}$$

EXAMPLE

Date:purchases

1/1 = 100 units @ 30/=

5/1 = 50 units @ 40/=

10/1 = 40 units @ 50/=

Sales = 2/1 = 90 units @ 60/=

6/1 = 40 units @ 70/=

11/1 = 30 units @ 50/=

Required: By using periodic method calculate the value of closing stock by FIFO and LIFO

FIFO; total amount of sales → 160=90+40+30

Amount of purchases = 190 units= 100+50+40
Closing stock=190-160=30 units

30 x 50 = 1500

;. Closing stock of FIFO = 1500
NOTE: Closing stock by FIFO will be valued by the last units value to be purchased.

LIFO; Total amount of sales = 160

Amount of purchases → last in first out 190 =100+ 50 + 40

Closing stock = 190-160

30 x 30 = 900

:. Closing stock of LIFO = 900.
NOTE: Closing stock by LIFO will be valued at 30@, the value of list units to be purchased

Workings

Total purchase

1/1/ 100 units @30= 3000

5/1 50 units @ 40= 2000

10/1 40 units @ 50= 2000

7000

Total sales

2/1 90 units @ 60 = 5400

6/1 40 units @70 = 2800

11/1 30 units 50 = 1500

9700

Prepare financial statement for the year/period ending 31Jan.

Note: Using periodic method by FIFO, LIFO and WAC

	FIFO	**LIFO**	**WAC**
Sales	9700	9700	9700
Less: LOGS			
	7000	7000	7000
	(1500)	(900)	(1105)
LOGS	5500	6100	5895
Gross profit	4200	3600	3805

$$W.A.C = \frac{(100x30) + (50x40) + (40x50)}{100 + 50 + 40}$$

$$\frac{7000}{190}$$

=36.84
Closing stock value=30 unitsx36.84
=1105

ILLUSTRATION 2

Sinza wholesaler deals in locally made door mats. During 199x, its records show the following transactions related to this particular merchandize.

Stock on hand at 31.12.199x was 70 units (650-580)

Total sales for the year was Tshs.250,000

Using a period inventory system

1. **First-in first-out (FIFO) method**

   The 70 units on hand will be assigned the following costs;

   50 x 340 = 17,000 (Nov purchases).

   20 x 330 = 6,600 (August purchases).

   23,600

Note that in this method it is assumed that the ending inventory consists of units from the most recent purchases

The cost of goods sold will be calculated as follows;

Total purchases	208,000
Less; ending inventory	23,600

Cost of goods sold 184,400

2. **Last-in-first-out(LIFO) Method**

The 70 units on hand will be assigned to the following costs;

60x 300 = 18,000 (Jan purchases)

10/70 x 310 = 3,100 (March purchases)

21,100

Note that in this method it is assumed that the ending inventory consists of units from the earliest

The cost of goods sold will be calculated as follows;

Total purchases	208,000
Less; Ending inventory	21,100
Cost of goods sold	186,900

3. **Average cost (AVCO) method;**

This method will use a weighted a average cost for the year calculated as follows;

Weighted Average cost = Total cost of purchases + opening stock

Tshs. 208,000/ = 320/=

650 units

The ending inventory will be assigned this cost which is 70 units @ shs. 320 = 22,400

The cost of goods sold will be;

Total purchases	208,000
Less; ending inventory	22,400

185,600

-Note that the goods sold have the same shs. 320 unit cost (580 units. @ 320= 185,600).

COMPARISON OF INVENTORY COSTING METHOD UNDER PERIODIC SYSTEM

	FIFO	**LIFO**	**AVCO**
	shs	shs	shs
Sales	250,000	250,000	250,000
less ; cost of goods sold			
Purchases	208,000	208,000	208,000
less ; Ending inventory	23,600	21,000	22,400
	184,400	186,900	185,600
	65,600	63,100	64,400

During the period of rising prices as in this illustration. The FIFO method results in the highest gross profit. This is due to assigning the most recent prices (Higher prices) to the ending inventory. This means the cost of goods sold is assumed to be from the earlier purchases (lower prices).

STOCK LEDGER CARD

II. **PERPETUAL SYSTEM OF INVENTORY**

-Physical movement of stock.

ILLUSTRATION 3

On 2nd may, M.LTD received 500 units at 20/=

8th may received; 300 units at 22/=

10th issued 400 units at -

15th issued 200 units at -

20th received 600 units at 22/=

25th issued 300 units at –

27th received 200 units at 26/=

30th issued 100 units at -

Standard price for each unit for the month of May was 24/= each, market price of these materials on 3rd June is 27 per unit and 400 units were purchased on that day.

Calculate closing stock under periodic method applying FIFO, LIFO and Average cost (weighted average).

USING A PERPETUAL INVENTORY SYSTEM

1. **First-in-first-out (FIFO)Method**

A stock record card for the door mats will be maintained as in the next and page.

STOCK CARD

DATE	PURCHASES/ RECEIVED			SALES/ISSUED			BALANCE		
	QTY	UNIT COST	TOTAL COST	QTY	UNIT COST	TOTAL COST	QTY	UNIT COST	TOTAL COST
2-May	500	20	10,000				500	20	10,000
8-May	300	22	6600				300	22	6600
			16,600				800		16,600
10-May	-	-	-	400	20	8000	100	20	2000
							300	22	6,600
							400		8600

15-May	-	-	-	100	20	2000	200	22	4,400
				100	22	2200			
							200		4,400
20-May	600	25	15,000	-	-	-	200	22	4,400
							600	25	15,000
							800		19,400
25-May	-	-	-	200	22	4400			
				100	25	2500	500	25	12,500
							500		12,500
27-May	200	26	5200	-	-	-	500	25	12,500
							200	26	5,200
							700		17,700
30-May	-	-	-	100	25	2500	400	25	10,000
							200	26	5,200
							600		15,200
		Purchases	36,800	COGS		21,600	600		15,200

2. By LIFO method (Last In First Out)

STOCK CARD

DATE	PURCHASES			SALES			BALANCE		
	QTY	UNIT COST	TOTAL COST	QTY	UNIT COST	TOTAL COST	QTY	UNIT COST	TOTAL COST
2-May	500	20	10,000	-	-	-	500	20	10,000
8-May	300	22	6,600	-	-	-	300	22	6600

							800		16,600
10-May	-	-	-	300	22	6600			
				100	20	2000	400	20	8,000
							400		8000
15-May	-	-	-	200	20	4000	200	20	4,000
20-May	600	25	15,000	-	-	-	200	20	4,000
							600	25	15,000
							800		19,000
25-May	-	-	-	300	25	7500	200	20	4,000
							300	25	7,500
							200	26	5,200
							700		16,700
30-May	-	-	-	100	26	2600	200	20	4,000
							300	25	7,500
							100	26	2,600
							600		14,100

3.By Average Method

Date	Purchases/Received			Sales/Issued		Unicost Balance			
	Cash	Unit cost	Cost	Q	R		Q	R	Cost
2 May	500	20	10,000				500	20	10,000
	300	22	6,600				300	22	6,600

8 May									
							800	20.75	16,600
10 May				400	20.75	8300	400	20.75	8300
15 May				200	20.75	4150	200	20.75	4150
							200	20.75	4150
20 May	600	25	15,000				600	25	15,000
							800	24	19,150
25 July				300	24	7200			
							500	24	11,950
27 May	200	26	5200				200	26	5200
							700	24.5	17,150
31 May				100	24.5	2450			
PURCHASES			36,000	Cost of goods sold		22,100	600	24.5	14,700

14,700= Closing stock

ESTIMATING STOCK

When a business firm does not maintain a perpetual inventory system, It has no way of determining the **actual stock** or inventory on hand unless the physical stock taking is done on a particular date. This will cumbersome and costly if it has to be done several times during an accounting period.

In order to avoid these inconveniences, the business will use an estimated figures its ending inventory.

There are occasions when it is necessary to estimate inventory. For-example when goods are lost or due to theft, a brokerage or natural deterioration or evaporation.

There are two common approaches to estimate stock;

1. Gross profit method
2. Retail method

1. **GROSS PROFIT METHOD**

This method of estimation uses Gross profit margin or average mark up in order to determine the cost of goods sold (cost of sales).

*Margin = profit/selling price.

* Mark up = profit/cost price.

ILLUSTRATION 1

ABC LTD TRADING A/C FOR THE YEAR ENDED 30/06/2009

Sales	780,000		
less; Return inwards	30,000	750,000	
less; cost of goods sold			
opening stock	120,000		
Add; purchases	660,000	780,000	
less; closing stock	180,000	600,000	
Gross profit		150,000	

Calculate;

1. Gross margin in percentage
2. Average mark up in percentage

Solution;

1. Gross profit margin = profit/selling price x 100%

$$= \frac{150,000 \times 100}{750,000}$$

= 25%

ILLUSTRATION 2

Assume in illustration (i.) in the previous page during July, August, September ABC has made;

Purchases 240,000

Net sales 350,000

Calculate inventory on 30th September, use gross profit method to estimate the

Given data;-

Stock as at 30th/6 180,000

Purchases 240,000

Sales 350,'000

Margin 20%

Calculate closing stock.

sales		350,000
Opening stock	180,000	

Add ; purchases	240,000	
cost of goods available for sale	420,000	
less ; Closing stock	140,000	
Cost of goods`sold		
Gross profit		70,000

ILLUSTRATION 3

On 1st January 2004, J.M valued his stock at cost, 12,300. During the first week of January 2004, his transactions in his stock were as follows;

Purchases	8,100
Sales	13,600
Returns inwards	800
Returns outwards	300

He sells his goods at 25% above cost of goods available for sale.

Calculate the cost of his stock at 7th January 2004

Sales		13,600	
less ; Return inwards		800	12,800
less ; cost of goods sold			
Opening stock	12300		
Add ; purchases	8100		
	20,400		
less ; Returns outwards	300		

Cost of goods available for sale	20100		
less; closing stock	9860		
Cost of goods sold.			10,240
Gross profit			2560

Gross profit P2?800x
Chane mark-up→Margin
25% →20%
20%x12,800→Gross profit Tshs 2560

RETAIL METHOD

- This estimation technique is employed to business with large amount of stocks of relatively low unit's values.
- Usually all items are quoted at retail prices

Example of business using retail method is;

1. Large chain store
2. Supermarket

This method employs the following steps;

1. obtain the cost of goods available for sale
2. if sales figure is given taking the value of goods available for sale at retail the sales figure should give the value of closing stock at retail
3. the value of closing stock at retail can be converted to an approximate cost figure by using the ratio of cost retail value worked out at (a) above.

ILLUSTRATION

On 1st June;	**COST**	**RETAIL**
Opening stock	180,000	288,000

30th; purchases	145,000	212,000
30th; sales	â”€	170,000

Calculate;

1. cost retail ratio
2. closing stock at retail value
3. Conversion of closing stock at retail value to cost.

Solution

Cost to retail ratio

	COST	RETAIL
Opening stock	180,000	288,000
Add; purchases	145,000	212,000
	325,000	500,000

Ratio = cost/Retail x 100

= 325,000 x 100

500,000

= 65%

Closing stock at retail value

	COST	RETAIL
Opening stock	180,000	288,000
Add; purchases	145,000	212,000
	325,000	500,000
Less; Net sales		170,000

Closing stock		330,000

Conversion of closing stock at retail value to cost

Closing stock = 330,000

65 x 330,000

100

= 214,000

Conversion of closing stock = 214,000

WEAKNESS OF ESTIMATION METHOD

1. The stock estimation technique covered has assumed that the gross profit margin is stable in the period of estimation.
2. They also assume that closing stock will be representative of all items which were available for sale.
3. If these assumptions are not true, then misleading values will be produced.
4. These techniques have to take accounts of realities encountered if they are to yield/ to get/to gain acceptable approximation.

On 1st April 2012; Stock at cost was 30,000/=

Purchases 15,000/=

Sales 10,000/=

The normal rate of Gross profit on cost price is 25% however it is known that allowances of 2,000/= have been made to customers.

Calculate;

- Closing stock estimate as at 30th April 2012.

Exercise 2.

Due to administrative reasons W.mahwa, the wholesaler, had to take his stock on 28th December 2004, on which date it was valued at cost at 73,260. The following transactions took place in the next 3 days.

1. Sales book 3400
2. Cash sales 1940
3. Purchases book total 2310
4. Returns inward book 220
5. Returns outward book 170
6. Carriage inward 425

A detailed examination of the books also revealed the following information

1. Sales book includes one invoice for 280/= against which goods were delivered on 2nd January 2005.
2. Cash sales includes sales of an item that had a cost value of 42/= but was sold for 36/= as it has been damaged in store
3. All purchases made had been dully received from supplier
4. A customer returned books that has been invoiced to him at 80/= on 29th December 2004 but was issued with a credit loan on 3rd January 2005
5. Carriage inward was paid in respect of goods bought in December 2004
6. Stock with a cost value of 295/= had stayed in store for too long and estimated to have realizable value of only 178/=.
7. Goods costing 126 were returned to a supplier on 30th December 2004 but the credit note was received four days later.
8. No records have been made of drawings in the form of goods by the owner of this business, W. Mahwa of 203.
9. The usual gross profit margin is 33% on cost.

Calculate the cost, net realizable value whichever is the lowest of the stock of 31st December 2004.

INSURANCE CLAIM

ILLUSTRATION 1

J.A has insured a stock for 10,000/=. On 31st March 2008 when the total cost value of stock in his store was 12,000, his store caught fire, the value of stock salvaged from fire was 3,000/=. Calculate the amount he can claim from the insurance company.

NOTES

If stock is not fully insured, that is if the value of stock in store is more than the sum insured, insurance company paid the following portion of the value of stock destroyed from fire

$$\text{Insurance claim} = \frac{10{,}000 \times 9{,}000}{12{,}000}$$

Insurance claim = 7,500

- Owner J.A of the go down should claim 7,500 before his insurance company.

ILLUSTRATION 2

Stock on 31st March 2005 (last year end) 6200/=

Debtors on 31st March 2005 was 4600/=

Creditors on 31st March 2005 was 5400

Receipt from debtors (1st April to 5th May) was 5700/=

Discount allowed to debtors 100/=

Discount received from creditors 180/=

Payment to creditors 5120/=

Stock donated to a charity (cost value) 340/=

Stock salvaged from fire 600/=

Gross profit margin 25% cost

Calculate;

1. The cost value of stock in store on 5th May 2005 considering that on that day debtors amounted to 6500 and creditors to 4900.
2. The amount to be claimed from insurance company

Solution; Exercise 2.

STOCK AS AT 28TH DECEMBER 2004

WORKINGS

- **NOTE (i)**

Sort out all items concerning with sales

Cash sales	1940
Credit sales	3400
	5340
Less; goods not delivered	280
	5060
Less; damaged value	36
Net sales	5024
5024 x 75% =	3768
Add; cost before damage	42
COGS	**3810**

NOTE (ii)

Stock with a cost value = 295

Less; Realizable value = (178)

Loss in value of stock 117

ESTIMATION OF STOCK

Stock as at 28th December 2004		73,200
Add; purchases	2310	
Carriage inwards	425	
(80 x 75%)	60	
Cost of value of Return inwards		
(220 x 75%)	165	2960
		76,160
Less; cost of goods sold .(note (i))	3810	
Return outwards	126	
Return outward book value	170	
Drawings	203	
Loss value in stock (note (ii))	117	-4426
Closingstock		71743

ROYALTY

. Concept of Royalty

. Minimum rate and short workings.

. Accounting entries in the books of lesser / landlord.

. Accounting entries in the books of lessee / tenant.

This is the remuneration payable to a person in respect of the use of an asset, calculated with reference to the quality produced/sold as result of use of such asset.

The loyalty is a periodic payment to the owner of an asset for the use of his ownership right that is royalty is a compensation made to the owner of an asset in exchange for the right to use that asset.

Royalty may arise in respect of the following;

a) For the extraction of minerals / materials from the ground.

b) For the publishing and books from the permission of the author.

c) For the use of the artistic work like movies e.t.c

Any lump sum amount paid for the use of any asset in never called royalty because it is capital payment.

TERMS USED IN THIS TOPIC:

i) **Lesser / Land lord**: This is owner of the asset, the person whom the right to use the land is granted is called tenant / lessee.

ii) **Short workings**: This is the difference between royalty and minimum rent/excess of minimum rent over royalty.

iii) **Minimum rent / dead rent / rock rent / flat rent**
Is the guaranteed amount that is landlord or the owner of the copy right is to receive.

iv) **Recoupment of a short working**; according to the short workings closed or contract, the tenant is empowered to cover the amount paid in excess of actual royalty out of the excess royalty over minimum rent (surplus). Until the stage of recovery is reached , he can accumulate the short workings and when once the stage of surplus is reached, he can go on recovering the excess of minimum rent, and after full recovery , pay the actual royalty. Usually in contracts where there is provision of minimum rent, there is also a provision of equipment of short workings. Generally, recoupment is the right of getting back from the land lord excess payment made by the tenant in the earlier years. The right to recoupment short workings may be either; a.1 fixed b.1 A floating type.

In case of a Fixed right or recoupment of short workings, the right is available only for a fixed period of time.

In case the tenant is not in a position to recoup the short workings during this period, the balance amount will be a loss to him which will be w/o from the profit and loss (P + L) a/c.

Illustration 1

A limited Co. leases a mine at a loyalty of 20/= each pert tone of coal raised which a dead rent for 400,000 per annum and further to recouped short workings during the first five years of the lease. Output during the first five years is as follows;

YEAR	PRODUCTION(TONNES)
1	2500
2	12,000
3	20,000
4	30,000
5	40,000

Required:

Show journal entries and ledger accounts in the books of lessor and lessee

Note: All workings should be shown

ROYALTY TABLE

				SHORT WORKING		
YEAR	**PRODUCTION**	**ROYALTY**	**M/RENT**	**RESULTED**	**RECOUPED**	**W/OFF**
1	2500	50,000	400,000	350,000	-	-
2	12,000	240,000	400,000	160,000	-	-
3	20,000	400,000	400,000	-	-	-
4	30,000	600,000	400,000	-	200,000	-
5	40,000	800,000	400,000	-	310,000	-

The following account made in;

A) When there is no provision for dividend or minimum rent.

i) Royalty based on actual production.

DR: Royalty payable a/c

CR: Land lord's a/c

ii) Cash paid to the land lord.

DR: Land lord a/c

CR: Cash a/c

B) When there is provision for minimum rent

i) Royalty based on production

DR: Royalty payable a/c

CR: Land lord a/c

ii) Short workings to be recovered in Future

DR: Short workings a/c

CR: Landlord a/c

iii) Cash paid to landlord

DR: Landlord a/c

CR: Cash a/c

iv) Short working unrecovered (if any)

DR: Profit & loss a/c (Bad debts)

CR: Short workings a/c

c) When royalty exceed minimum rent

i) Royalty based on actual production

DR: Royalty payable a/c

CR: landlord a/c

ii) Short working recouped, if any

DR: Landlord a/c

CR: Short working a/c

iii) Cash paid to landlord

DR; Land lord a/c

CR; cash a/c

Note: Cash paid to landlord must not be less than minimum rent

iv) Short workings irrecoverable

DR; profit & loss a/c

CR; short working a/c

Workings:

DR ROYALTY PAYABLE ACCOUNT CR

DATE	DETAILS	AMOUNT	DATE	DETAILS	AMOUNT
1ST YEAR	A.LTD COY	50,000		Manufacturing a/c	50,000
2ND YEAR	A.LTD COY	240,000		Manufacturing a/c	240,000
3RD YEAR	A.LTD COY	400,000		Manufacturing a/c	400,000
4TH YEAR	A.LTD COY	600,000		manufacturing a/c	600,000
5TH YEAR	A.LTD COY	800,000		Manufacturing a/c	800,000

DR A. LTD's ACCOUNT CR

DATE	DETAILS	AMOUNT	DATE	DETAILS	AMOUNT
1st year	Bank	400,000	1st year	Royalty payable	50,000
				short workings	350,000
		400,000			400,000
2nd year	Bank	400,000	2nd year	Royalty payable	240,000
				short workings	160,000
		400,000			400,000
3rd year	Bank	400,000	3rd year	Royalty payable	400,000

4th year	Bank	600,000	4th year	Royalty payable	600,000
5th year	Bank	800,000	5th year	Royalty payable	800,000

DR LAND LORD ACCOUNT CR

DATE	DETAILS	AMOUNT	DATE	DETAILS	AMOUNT
2000	Bank	200,000	2000	Royalty payable	100,000
			2000	short workings	100,000
		200,000			200,000
2001	Bank	200,000	2001	Royalty payable	150,000
				short workings	50,000
		200,000		short workings	200,000
2002	Bank	200,000	2002	Royalty payable	200,000
2003	Bank	200,000	2003	Royalty payable	225,000
	short workings	**25,000**			
		225,000			**225,000**
2004	Bank	200,000	2004	Royalty payable	250,000
	short workings	50,000			
		250,000			**250,000**

DR ROYALTY RECEIVABLE CR

DATE	DETAILS	AMOUNT	DATE	DETAILS	AMOUNT
2000	Manufacturing a/c	100,000	2000	S.G COY LTD	100,000
2001	Manufacturing a/c	150,000	2001	S.G COY LTD	150,000
2002	Manufacturing a/c	200,000	2002	S.G COY LTD	200,000
2003	Manufacturing a/c	225,000	2003	S.G COY LTD	225,000
2004	Manufacturing a/c	250,000	2004	S.G COY LTD	250,000

DR TENANT ACCOUNT (S.G COY LTD) CR

DATE	DETAILS	AMOUNT	DATE	DETAILS	AMOUNT
2000	Royalty receivable	100,000			
	short workings	100,000	2000	Bank	200,000
		200,000			200,000
2001	Royalty receivable	150,000			
	short workings	50,000	2001	Bank	200,000
		200,000			200,000
2002	Royalty receivable	200,000	2002	Bank	200,000

2003	Royalty receivable	225,000	2003	Bank	200,000
				short workings	25,000
		225,000			225,000
2004	Royalty receivable	250,000	2004	Bank	200,000
				short workings	50,000
		250,000			250,000

DR ROYALTY SUSPENSE ACCOUNT CR

DATE	DETAILS	AMOUNT	DATE	DETAILS	AMOUNT
31.12.2000	Balance c/d	100,000	2000	S.G COY LTD	100,000
31.12.2001	Balance c/d	150,000	2001	Balance b/d	100,000
			2001	S.G COY LTD	50,000
		150,000			150,000
31,.12.2002	Balance c/d	150,000	2002	Balance b/d	150,000
	S.G COY LTD	25,000	2003	Balance b/d	150,000
31,12,2003	Balance c/d	125,000			
		150,000			150,000
	S.G COY LTD	50,000	2004	Balance b/d	125,000
31.12.2004	Balance c/d	75,000			
		125,000			125,000

			2005	Balance b/d	75,000

ILLUSTRATION III;Mr. R Company leased a Royalty from Mr. A of 1 E per tone's which a minimum rent of 30,000 E.P.A each years of excess of dead rent over royalty is recoverable out of the royalties of the next five (5) years. In the event of strike and the minimum rent not being reached. The lease provided that the actual royalty and for the year should be paid, the result of workings were as follows;

YEARS	PRODUCTION
2001	-
2002	9750
2003	27750
2004	33750
2005	42000
2006	52500
2007	28500
2008	45,000

SUB- LEASE

- The lease agreed sometimes gives right to the lessee to sub contact the right for the use of asset, this is known as "Sub – lease".
- And the person who is sub – contracted is known as sub lessee / sub tenant.
- The accounting treatment for the sub lease and the lease and the lessee is similar to that of the land lord and sub lease.
- In the case of sub- lease, the lessee takes the legal stand of the land lord to the sub-lessee.
- It must be noted that there is no agreement between the original landlord and the sub- lessee as per the original agreement terms. But what eventually is paid to the original land lord is calculated based on the total output of the both lessee and sub- lessee.

- The lessee is paid based on the output produced or manufactured by sub – tenant.
- In most cases the lessee chargers higher price to the sub-lessee than be is charged to the original landlord. Profit of the such price are transferred to the P + L A/C

ACCOUNTING TREATMENTS:

i) Royalty payable (own + sub- lessee)

DR: Royalty payable a/c

CR: Land lord's a/c

ii) Royalty receivable a/c (Based on sub – tenant production)

DR: Sub tenant a/c

CR: Royalty receivable a/c

iii) Short working recoverable in future by sub – Lessee

DR: Sub – tenants

CR: Short workings

iv) Royalty payable by tenants on sub-tenants production

DR: Royalty Receivable a/c

AC: Royalty payable a/c

v) Profit on sub – lease;

DR; Royalty Receivable a/c

CR: P + L a/c

ILLUSTRATION

Doti limited acquired rights from Note ltd to manufacture and sell a certain brand of perfume on the following terms;

i) Royalty shall be paid on number of bottles manufactured at 20/= per bottle /per unit.

ii) The minimum royalty in any one year shall be 500,000/=

iii)Short working will be recouped within the first two year of short workings.

iv)The agreement to become effective on 1st July 2000.

v) All settlement were made on 31st December on each year.

On 1st January 2000, Doti limited granted right to Mwingine Ltd to manufacture and sell the same perfumes on the following terms;

a) Royalty shall be paid on number of bottles manufactured at 30/= per bottle/ per unit.

b) The minimum royalty in any one year shall be 200,000/=

c) Short working recouped only in the year

Following the year of short workings.

The following information is provided;

YEARS	DOTI LTD	MWINGINE LTD
2000	80,000	-
2001	11,000	6000
2002	14,000	7000
2003	16,000	11,000
2004	12,000	5000

Required;

Show ledger account in the books of Doti LTD.

ROYALTY TABLE (i) ORIGINAL LEASE

YEARS	PRODCTN	ROYALTY	M.RENT	SHORTWORKINGS			AM
				RESULTED	RECOUPED	W/OFF	PA
2000	8000	160,000	500,000	340,000	-	-	500
2001	17,000	340,000	500,000	160,000	-	-	500
2002	21,000	420,000	500,000				
2003	27,000	540,000	500,000		40,000	40,000	
2004	17,000	340,000	500,000	160,000	-	160,000	500

ROYALTY TABLE (ii)

YEARS	PRODCTN	ROYALTY	M.RENT	SHORTWORKINGS			AM
				RESULTED	RECOUPED	W/OFF	PA
2000	-	-	200,000				200
2001	6000	180,000	200,000	20000		20,000	200
2002	7000	210,000	200,000		10,000	10,000	200
2003	11,000	330,000	200,000		130,000		
2004	5000	150,000	200,000				

Profit on sub- lease:

Royalty payable - 20/=

Royalty receivable - 30/=

10/=

2001 : 6000 x 10 = 60,000

2002: 7000 x 10 = 70,000

2003: 11000 x 10 = 110,000

2004: 5000 x 10 = 50,000

COMPANY ACCOUNT 1.1

What is a company?

It is a voluntary association of persons formed to carry out some business for profit , with capital divisible into transferable shares, having a corporate legal entity and a common seal.

In law a company can be defined as a fictitious but legal person that can enter into contract sue others and being sued by others, having a banning A/C in its own name owe money or be a creditor and can do any other things which it has been formed.

Characteristics of a Company:-

(a) Voluntary association

(b) Independent legal entity

- A company is distinct and separate from its members.

(c) **Limited liability**

Usually the liability of a company is limited to the extent of unpaid value of shares held by the members.

(d) **Common seal**

The company acts through natural persons called directors. The directions are the agents of the company.

All the act of the company are authorized by its common seal. The common seal is the official signature of a company. Any document not bearing the common seal will not binding on company.

(e) Transferability of shares:-

Usually in a limited company shares are freely transferable. But in the case of a private limited company share are transferable subject to conditions laid down by the company's articles.

(f) Perpetual existence;-

In this case the life of a company is perpetual and so it can never be affected by the life of its members.

TYPES OF COMPANIES

1. STATUTORY COMPANIES

These are companies formed by a special act passed in parliament. Usually such companies are established in order to carry out some special public undertaking requiring extra – ordinary power and privilege.

Such companies are established not to earn profit but serve people.

2. GOVERNMENT COMPANIES (PARASTATAL COMPANIES)

These are companies which not less than 51% of its issued paid up capital is held by the central government.

3. REGISTERED COMPANIES:-

These are companies formed and registered under companies acts. Here in Tanzania it is the 1961 act cap. 212. Such companies may be limited by shares guarantee or unlimited companies.

1) Companies limited by shares:-

In this case the liability of members is limited into the extent of the unpaid value of the shares held by them.

2) Companies limited by guarantee:-

In this case the liability of members is limited to the amount that they undertake to contribute in the event of bankruptcy.

3) Unlimited companies:-

In this case the liability of members is not restricted.

FORMATION / FLOATATION OF A COMPANY

It is the promoter who thinks about the idea of a business to be carried out by a proposed company.

They undertake extensive investigations to its successful operation viability and feasibility.

They then prepare the following documents and send them to the register with a request to register the company.

1) **Memorandum of Association**

- It is the main document of a company.

- It is a charter or constitution of a company's power and scope of operation.

This document contains the following things:-

(a) The name of a company with the world Ltd at the end of the name. Name clause

(b) The objective of a company i.e. the purpose of formation. It should state:-

(i) The main of the company's objective

(ii) Objective incidental to the main objectives.

(iii) Others objectives.

(iv) Objective clause

(c) A declaration that the liability of a members is limited ''liability clause"

(d) The domicile of the company i.e. the place of the company's registered office , situation clause.

(e) Association clause:-

Under this clause it is stated here that people putting their signatures to the memorandum are desirous of forming themselves into company.

The memorandum should be signed by at least two persons in the case of a private company and seven persons in the case of a public company agreeing in both case to take up to at least one share each.

2). **ARTICLES OF ASSOCIATION:-**

It is a document defining rules and regulations for the conduct of the company's business.

It establishes a contract between the company on one hand and the shareholders on the other and between the shareholders.

It has the following content:-

a) Share capital and its division into various types and the right attaching there to.

b) Direct their members power duties and qualifications

c) Proceeding of the directors meeting general and extra ordinary investing.

d) Calls on shares.

e) Common seal.

f) Accounts and Audit.

g) Forfeiture of shares.

h) Dividend and reserves.

i) Voting rights of members.

j) Notices

3). **A statement of nominal capital:-**

It specifies the different classes of shares that comprises the share capital of a Company.

4). A list of persons who have consented to act as directors.

5). A written consent by the directors to act in that capacity.

6). A written undertaking by the directors to take up and pay for their qualification shares.

7) Particulars of directors and secretary.

8) A notice of the address of the company's registered office.

9) A declaration by a solicitor, attorney, accountant or secretary that all the requirements of the company's acts have been complied with.

On receipt of such documents the register will then scrutinize them to see to it that they are okay and if he find them to be order he will issue or certificate of incorporation (after payment of the registration fees.)

This certificate signifies that a company has legal existence the register then will put the name of the company into the register.

A private limited company may commence a business on its incorporation but not for the public ltd company.

The caller has to receive a certificate of commencement of business Trading certificate) prior to its commencement of business.

A private company is a company which by its articles:-

(i) Does restrict the rights of its shareholders to transfer shares.

(ii) Limit the number of its shareholders to fifty excluding the post and present employees who are also the members of the company.

(iii) Does not invite the public to the subscription of shares or debentures.

A public Ltd company is a company which is not as **private Ltd company** i.e. it does not observe any of the above characteristics;-

Before receiving the trading certificate the private Ltd Company has to issue a prospectus and its copy then being kept by the register.

A prospectus

This is a circular, advertisement or any document inviting offers from the public to the subscription of any shares or debenture of anybody corporate.

The prospectus invites public to buy its shares or debentures in order to raise the necessary funds.

Some of the matters contained in this prospectus:-

(i) Contents of the memorandum.

(ii) Names and addresses of the directors.

(iii) Names and addresses of the auditor if any.

(iv) Qualification and remuneration of the directors.

(v) The minimum subscription and the amount payable on application and allotment.

(vi) Brokerage or underwriting commission on placing shares or debentures.

(vii) In case of already established company import by the auditors about the dividend or profit paid in each of 3 proceeding years.

ALLOTMENT OF SHARES:-

After the issue of prospectus, the prospective investors will start applying for the shares, through filling in application forms and paying application money (which should at least be 5% of a face or normal value a shares.)

If the application do not amount to the minimum subscription within 40 days of the issue of the prospective then the whole application money has to be refunded by the directors to the applicants within 8 days, otherwise they will liable to repay it with 5% interest as a penalty.

If the applications amount to the minimum subscription then the directors will start considering each application. They may allot the full number of shares applied for or less than that or none at all without giving any reason.

CLASSES OF SHARES:-

What is a share?

Shares are unit of uniform values into which the share capital of the company is divided.

What is share capital?

Share capital is the sum total of the nominal value of shares of a company.

(a) Ordinary shares or Equity shares;-

Do not give preferential rights in respect of fixed dividends and in regard to the repayment of capital in case of winding up.

(b) **Preferred ordinary shares**; Have a right to receive dividends after the preference shareholders have received their dividends.

(c) Deferred ordinary shares:-

Have a right to receive dividend after the preferred ordinary shares, have received their dividend.

(d) Preference shares:-

Give preferential rights in respect of a fixed dividend and in regard to the repayment of capital in case of winding up.

(e) Cumulative preference shares:-

In this case any arrears of dividend go on accumulating until paid up.

(f) Participating preference shares:-

Entitle their holders to receive not only a fixed rate of dividend but also share in the surplus profit after the other classes of shareholders have received their specified rate of dividend.

(g) Guaranteed preference shares;

Entitle their holders to receive a fixed rate of dividend quarantined by vendors or any third party. In case of a bad year (i.e no profit declared the guarantees have to pay the guaranteed dividend out of their personal recourses.).

(h) Deferred founder or management shares:-

Have a right to receive dividend after all other classes of shareholders have received their dividend.

Such shares do belong to promoters or founders of the company. When shares are offered to the public, the cost of such shares is usually payable by installments. The installments may be made of application allotment and calls.

A call is the amount of installments payable for each share following the installments payable on allotment.

When the company allots the shares, it signifies acceptance of the offer made by the applicants, when the prospective investment apply for the shares, this does not guarantee that they receive such shares money may be refunded to the unsuccessful applicant with a letter of regret. On allotment a binding contract will exist between the company and their shareholders.

ISSUE OF SHARES

Shares may be issued by a joint stock company for different consideration:-

(i) For consideration other than cash: In this case the company may purchase a running business and pay money / consideration to the vendors in the form of shares.

(ii) For cash: - In this case shares can be issued at (a) part (b) premium Discount.

(a) At par:-

In this case the shareholders are required to pay the nominal value of the shares.

(b)At premium

In this case the shareholders are required to pay more than the nominal value of the shares. That is shares are issued at a profit for example a share of Tsh. 100 being issued at Tshs. 110, Tshs, 10 is the premium.

(c) At discount:-

There are some restrictions on issuing shares at a discount but all the same the shares are issued at less than the nominal value. For example a share of 10 Tshs being issued at Tshs. 9, Tshs. 1 is the amount of discount.

Issue of shares at a premium:-

When the company issues shares above par, the excess termed as premium is held in a separate account called share premium A/c in accordance with the requirements of the company Act. The amount of share premium is called a capital gain and it is usually recorded in the balance sheet on the liabilities side under "Reserve and surplus".

The share premium can be used in the following ways:-

(i) To pay up the un issued shares for distribution to member as bonus shares.

(ii) To write off preliminary expenses in the formation of a company.

(iii) To write off expenses on issuing shares or debentures..

(iv). To write off commission paid or discount allowed on issuing shares and debentures.

(v). To provide for a premium payable on redemption usually the amount of share premium is payable for in a lump sum on allotment

ENTRIES:-

(a) On amount being due

DR. Application allotment A/c

CR. Share capital A/c

CR. Share premium A/c

(b) When the allotment money is received:-

Dr. Cash / Bank A/c

Cr. Application and allotment A/c

UNDER OR OVER SUBSCRIPTION FOR SHARE

Under – subscription for shares:-

It is a situation where by applications are received for a number shares less than that offered by the company for subscription.

In this case entries for application allotment and call will be made on the applications received.

And if the applications do not amount to minimum subscription the whole application money shall be returned to the applicants.

Over – subscription for shares:-

It is a situation where by applications are received for a number of shares more than that offered by the company for subscription. The excess application money is usually used in making goods the allotment money. And the excess application money can be utilized in the following way:-

(i) Some applications may be returned to the unsuccessful applications i.e. rejected and money being returned to the unsuccessful applications.

(2) Partial allotment may be made:-

This is the allotment of a smaller number of shares than that applied for example of 4000 shares being allotted 2000 shares where as a holder of 8000 being allotted 2600 shares.

3) Prorate allotment may be made:-

This means the allotment of share to an applicant or group of application on proportional basis.

Examples: Given shares applied = 16,000

Shares rejected = 1000

Shares issued = 10,000

PRORATE

Applied Issued / allotments.

16000 10,000

Less: (1000)

Net: 15,000: 10,000

Prorate 3: 2

This means for every 3 shares applied, 2 shares shall be allotted.

NB: A company cannot allot more than the shares issued.

CALLS IN ARREARS

Represents the extent that the shareholders have not paid the amount due on call made to them.

Dr. Calls in arrears A/c

Cr. Call A/c (appropriate)

Money alter allotment is called a call.

CALLS IN ADVANCE

Money may be received before call in due entries.

(j) Dr. Cash / Bank A/c

Cr. Call in advance A/c (Amount received in advance of calls).

(ii) Dr. Call in advance A/c

Cr. Call A/c (Appropriate) (When the call is made)

EXAMPLE:

Baja Company Ltd has an authorized capital of 100,000 Tshs divided into 20,000 ordinary shares of 50 sh. each the whole of the shares were issued at par. Payments being made as follows;-

Payable on applications 5 Tshs.

Payable on allotments 15 Tshs.

1st call 20 Tshs.

2nd call 10 Tshs.

Applications were received for 32,600. It was decided to refund application money on 2600 shares and to allot shares the basis of 2 for every 3 applied for. The excess application moneys sent by the successful applicants is not to be returned but it is to be held and so reduced the amount payable on allotment the calls were made and paid in full with the exception of one member holding 100 shares who paid neither the first and the second another who didn't pay second call on 20 shares. The member of the second call the first each on his 200 shares.

Required:

Prepare the relevant ledger A/c to record the above Ledger Account

DR BANK ACCOUNT CR

Application & allotment(5x32600)	163,000	Application & allotment(5x2500)	13000
Application & allotment	250,000		
first call	398000		
call in advance	2000	Balance c/d	996,800
second call	196800		
	1,009,800		1,009,800

DR APPLICATION & ALLOTMENT CR

Bank (refund)	13,000	bank (Application money)	163,000
ord.share capital (5+15)20000)	400,000	bank (Application money)	250,000
	413,000		413,000

DR ORDINARY SHARE CAPITAL CR

Balance c/d	1,000,000	Application & allotment 1st call 2nd call	400,000 400,000 200,000
	1,000,000		1,000,000

DR **1ST CALL ACCOUNT** **CR**

ordinary shares capital (20x20000)	400,000	Bank call in arrear (20 x 100)	398,000 2,000
	400,000		400,000

DR **2ND CALL AND FINAL CALL ACCOUNT** **CR**

Ordinary share capital(10x20000)	200,000	Bank call in advance call in arrear (10x(100+20)	196,800 2,000 1,200
	200,000		200,000

DR **CALL IN ARREAR ACCOUNT** **CR**

1st call	2000	Balance c/d	3,200
2nd call	1200		
	3200		3200

BALANCE SHEET (EXTRACT) AS AT

Authorized share capital		Fixed Assets			
Ordinary shares Tshs. 500	xxx		cost	Acc.deprec.	Net
		premises	xxx	xxx	xxx
Issued and paid up capital		machinery	xxx	xxx	xxx
20000 ord. share of Tshs. 50 each	1,000,000		xxx	xxx	xxx
Reserves & surplus		current assets			
share premium	xxx	stock			xxx
long-term liabilities		calls in arrear			3200
Debentures	xxx	bank balance			996800
current liabilities					
creditors	xx				
Dividend payable	xx				
corporation tax	xx				
	1,000,000				1,000,000

EXERCISE

1. Ujamaa & Co. Ltd, offered its ordinary shares for sale to the public as follows:-

January 3: Application invited for 10,000/= ordinary shares of Tshs. 100/= each. Applicants were asked to enclose application money of 29/= per share.

January 10: Applications received for 10,000/= ordinary shares.

February 17: Allotment money dully received.

March 5: First call of Tshs. 45/-per share made

March 22: First call duly received.

You are required to show:-

(a) Journal entries to record the above transactions.

(b) All relevant ledger A/c

(c) Assuming the company has made no transaction other than the ones listed above, the company on 22nd March, 1984.

Solution for exercise 1
JOURNAL ENTRIES

S/N	DETAILS	DR	CR
1	Bank	290,000	
	Application		290,000
2	Bank	260,000	

	Allotment		260,000
3	Bank	450,000	
	1st call		450,000
4	Application	290,000	
	O/share capital		290,000
5	Allotment	260,000	
	O/share capital		260,000
6	1st call	450,000	
	O/share capital		450,000

LEDGER

DR **BANK ACCOUNT**

		Balance c/d	
Application	290,000		
Allotment	260,000		
1st call	450,000		
	1,000,000		
Balance b/d	1,000,000		

APPLICATION A/C

DR			
31st JAN	O/share capital	290,000	Bank

ALLOTMENT A/C

DR			
28th FEB	O/share capital	260,000	Bank

1ST CALL A/C

DR			
MARCH	O/share capital	450,000	Bank

ORDINARY SHARE CAPITAL A/C

DR			
	Balance c/d	1,000,000	Application Allotment 1st call
		1,000,000	1

2. Nyamasama Co. Ltd offered 25,000 ordinary shares of Tshs. 50 each for public subscription as follows:-

Tshs. 10 on application

Tshs. 15 on allotment to include share premium

Tshs. 15 on 1st call

Tshs. 20 on 2nd call

Application were received for 38,000/= share. The promoters decided to:-

(i) Reject 8000 applications and to refund the money received against them.

(ii) Allot 5 shares for every 6 applied for by the remaining applicants.

Excess application money received from these applicants was transferred to an allotment money A/c

Allotment money was duly received. The first call was made and money promptly received from all but one shareholder who held 500 shares. The second call was paid by all shareholders except two, one who held 500 shares and who had earlier failed to pay the first call, and another who held 200 shares.

Required:-

(a) Show the relevant ledger A/c of the company.

(b) Show the company's opening balance sheet after all the above transactions have been made.

2. (a)

JOURNAL ENTRIES

DATE	DETAILS	DEBIT	CREDIT
10-Jan	Bank A/c	250,000	

	Allotment & application		250,000
17-Jan	Bank A/c	375,000	
	Allotment & application		300,000
15-Mar	First call A/c	450,000	
	Ordinary share capital		450,000
22-Mar	Bank	450,000	
	First call A/c		450,000

(b)

DR BANK ACCOUNT CR

DATE	DETAILS	AMOUNT	DATE	DETAILS	AMOUNT
10-Jan	Applic& allotment(10,000x25)	250,000			
6-Jan	Allotment & applic(30x 10,000)	300,000			
5-Mar	ordinary share(1st call)	450,000		Balance c/d	1,000,000
		1,000,000			1,000,000

DR APPLICATION & ALLOTMENT CR

	ordinary share	550,000		Bank(applied money) Bank(allot money)	250,000 300,000
		550,000			550,000

DR ORDINARY SHARE ACCOUNT CR

	Balance c/d	1,000,000		1st call Application & allotment	450,000 550,000
		1,000,000			1,000,000

DR 1ST CALL ACCOUNT CR

5-Mar	ordinary share(45 x10,000)	450,000		Bank	450,000
		450,000			450,000

BALANCE SHEET AS AT 31ST/ 3/1984

Authorized share capital		Current assets	
ordinary shares(10,000 x100)	1,000,000	Bank	1,000,000
	1,000,000		1,000,000

SOLUTION FOR EXERCISE 2

DR APPLICATION & ALLOTMENT CR

	Bank(refund)	80,000		Bank(applied money)	380,000
	ordinary share capital(10+5)x2500)	375,000		Bank(allot money)	325,000
	premium share(10x25,000)	250,000			
		705,000			705,000

DR ORDINARY SHARE ACCOUNT CR

	Balance c/d	1,250,000		1st call	375,000
				Application &allotment	375,000
				2nd call	500,000
		1,250,000			1,250,000
				Balance b/d	1,250,000

DR 1ST CALL ACCOUNT CR

				call in arrears(500 x 15)	7,500
	ordinary share(15 x 25,000)	375,000		Bank	367,500
		375,000			375,000

DR 2ND CALL ACCOUNT CR

	ordinary share(20 x 25,000)	500,000		call in arrear(20 x 700)	14,000
				Bank	486000
		500,000			500,000

DR **SHARE PREMIUM ACCOUNT** **CR**

	Balance c/d	250,000		Application & allotment	250,000
		250,000			250,000
				Balance b/d	250,000

DR **BANK A/C** **CR**

Application and Allotment	380,000	Application and Allotment	80
Application and Allotment	325,000	Balance c/d	,478
1st call	367,500		
2nd call	486,000		
	1,558,500		,558,
Balance b/d	1,478,500		

BALANCE SHEET AS AT

Authorized share capital			
ordinary share(25,000 x 50)	1,250,000	Current Assets	
		Bank	1,478,500

Current liabilities		call in arrear(14,000 + 7500)	21,500
share premium	250,000		
	1,500,000		1,500,000

ISSUE OF SHARES AT DISCOUNT

A company may issue shares at a discount (i.e. for a consideration less than the nominal value) subject to the following conditions as laid drawn by the company's act:-

(a) The issue must be authorized by an ordinary resolution.

(b) The resolution should state the maximum rate of discount.

(c) The issue must be sanctioned by the company's law board.

(d) At least one year should have elapsed since the date by which the company was allowed to commerce business.

(e) The issue should be made within two month after the date of the sanction of the company's law board.

(f) A prospectus relating to the issue of shares at a discount should give particulars about the discount allowed on the issue of shares and also of the amount of discount not yet written as at the date of prospectus.

NB: The entry is usually made on allotment:-

Dr. Application and Allotment A/c

Dr. Discount on issue of shares A/c

Cr. Share capital A/c

The amount of discount is a fictitious asset and so must be written off as an expenses as soon as possible.

Dr. Profit & Loss / Share premium A/c

Cr. Discount on issue A/c

FORFEITURE OF SHARES

When a call remains unpaid, and the time allowed for its payments has expired, then the company may FORFEIT shares together with the amount already received on such shares.

In order for the forfeiture of such shares to be valid, the following conditions must be satisfied:-

(a) The forfeiture must be authorized by the company's articles.

(b) The procedure of the forfeiture must be followed.

(c) There should be a default by a shareholder in payment of a valid call.

(d) A notice requiring a shareholder to pay a specified amount within a specified period of time must given (usually a fourteen day's notice).

Entries on forfeiture:-

(i) Calls in arrears on forfeited shares:-

Dr. Forfeited, shares A/c.

Cr. Calls in a arrears A/c.

(ii) Shares for forfeited due to calls in arrears:-

Dr. Share capital A/c with the called value.

Cr. Forfeited shares A/c.

(iii) Forfeited shares now being reissued

Dr . Forfeited shares reissued A/c

Cr. Share capital A/c

(iv) Cash received prior to forfeiture on the reused shares :-

Dr. Forfeited shares

Cr. Forfeited shares reissued

(v) Cash received on the reissued shares:-

Dr. Cash / Bank A/c

Cr. Forfeited share reissued A/c

(vi) Share premium (if any) on the reissued A/c:-

Dr. Forfeited shares issued A/c

Cr. Share premium A/c

Example:-

The authorized and issued share capital of cosy fire's Ltd was Tshs. 75000 divided into 75000 ordinary shares of Tshs. 1 each, fully paid 2 January 2007. The authorized capital was increased by a further 85,000 ordinary shares of Tshs. 1 each to Tshs. 160,000.

On the same date 40,000 ordinary shares of Tshs. 1 each were offered to the public at Tshs. 1.29 per share payable as to sh. 0.60 on application (including the premium), Tshs. 0.35 on allotment and sh. 0.30 an 6th April 2007.

The list was closed on 10 January 2007, and by that date applications for 65,000 shares had been received. Applications for 5000 shares received no allotment and cash paid in respect of such shares was returned.

All shares were allocated to the remaining applications on prorate to their original application the balance of the monies received on applications being applied to the amounts due on allotment.

The balances due on allotment were received on 31st January 2007 with the exception of one allote of 500 share and these were declared forfeited on 4 April 2007. These shares were reissued at fully paid on 2 May 2007 at Tshs. 10 per share. The call due on 6 April 2007 was duly paid by the other shareholder.

Required:-

(a) To record the above mentioned transaction in the appropriate ledger.

(b) To show how the balances on such accounts should appear in the company's balance sheet as at 31st May 2007.

Calculate of prorate:-

	Applied	Offered
	65000	40000
Refund	(5000)	_____
	60,000	40,000

Allotment money received

Due on allotment 0.35 x 40000 14,000

Less: excess capt. Money received: 0.6 x 20,000 12,000

2,000

Less: Due on all allotment; 0.35 x 500 = 175

Less: excess apply money 0.6 x 250 = 150 25

Allotment money received **1975**

3 ⟶ **2**

? ⟶ 500

$= \frac{1500}{2} = 750 - 500 = 250$

DR BANK ACCOUNT CR

DATE	DETAILS	AMOUNT	DATE	DETAILS	AMOUNT
1/1/2007	Balance b/d	75,000		Appl& allot(refund)	3000
1/10/2007	Application & allotment	39,000			
	Application & allotment	1975			
	First & final call	11850		Balance c/d	125,375
	forfeited Reissue	550			

		128,375			128,375
	Balance b/d	125,375			

DR APPLICATION & ALLOTMENT ACCOUNT CR

Bank(refund)	3000		Bank(appl.money)	39,000
ordinary share capital	28,000		call in arrear	25
share premium	10,000		Bank(allot&money)	1975
	41,000			41,000

DR ORDINARY SHARE CAPITAL ACCOUNT CR

	forfeited share(0.7x500)	350	1/1/2007	Balance b/d	75,000
				Application &allotment	28,000
				forfeited share reissue	500
	Balance c/d	115,000		First & final call	11850
		115,350			115,350

				Balance b/d	115,000

DR FIRST & FINAL CALL CR

	ordinary share capital	11850	Bank	11850
		11,850		11,850

DR SHARE PREMIUM ACCOUNT CR

	Balance c/d	10375 10375		application & allotment forfeited share	10,000 375

DR CALL IN ARREAR ACCOUNT CR

	application & allotment	25		forfeited share	25
		25			25

DR FORFEITED SHARE ACCOUNT CR

	call in arrear forfeited	25 325		ordinary share capital	350
		350			350

DR FORFEITED SHARE REISSUED ACCOUNT CR

	ordinary share capital share premium	500 375		forfeited share Bank	325 550
		875			875

First call (calculation)

40,000 - 500 = 3950

x 0.30

11850

BONUS ISSUE OR SCRIPT ISSUE:

The directors of a limited company may decide to issue. More shares to existing shareholders against the reserves or P&L A/C balance in this case, the shareholders are not supposed to make any payment.

Right issue:- May be defined as the raising of new capital by a company by giving existing shareholders the right to subscribe to new shares of debentures in proportion their current holdings.

EXERCISE

M. Limited has an authorized share capital of Tshs. 1,500,000 divided into 1,500,000 ordinary share of Tshs. 1 each. The issued share capital at 31st March 2007 was Tshs. 500,000 which was full paid and had been issued at par. On 1st April 2007, the directors, in accordance with the Company's articles decided to increase the share capital offering by a further 500,000 ordinary shares of Tshs 1 each at a price of Tshs. 1.60 Per share payable as follow:-

On application including the premium Tshs,. 0.85 Per share

On allotment Tshs. 0.25 Per share

On 1st final colon 3rd August 2007 Tshs. 0.50 Per share

On 13th April 2007, applications had been received for 750,000 shares and it was decided to allot the shares on the basis of four shares for every five shares for which applications had been received.

The balance of the money received on application was to applied to the amount due on allotment. The shares were allotted on 1st May 2007, the unsuccessful applications being repaid their cash on this date. The balance of the allotment money was received in fully by 15th May 2007.

With the exception of the member who failed to pay the call on the 5000 shares allotted he the reminder of call was paid in full within two weeks of the call being made.

The directors resolved to the forfeit these shares on 1st September 2007 after giving the required notice. The forfeited shares were reissued on 30th September 2007 to another member at Tshs. 0.90 Per share.

You are required to write up the ledger a/c necessary to record these transactions in the books of M. Ltd.

Premium = 1.60 - 1.0 = 0.6

Application = 0.85 - 0.6 = 0.25

Applied Issue

? 500.000

5 4

= 5 x 500,000 = 625,000 x 7

4

Net Applied Amount = 625,000

Allotment received:-

Due to allotment (0.25 x 500,000) = 125,000

Less: Expenses on Appl. (0.85 x 625 – 500,000) 106,250

Allotment money received **18750**

DR BANK ACCOUNT CR

1-Jan	Balance b/d	500,000		Application& allot(125000x0.85	106250
	Apply & allotment	637,500			
	1st call	247,500		Balance c/d	1,302,000

	Apply & allotment forfeited share reissue	18,750 4,500			
		1,408,250			1,408,250

DR APPLICATION AND ALLOTMENT ACCOUNT CR

	Bank(refund) ordinary share(0.5x500,000) share premium(0.6x500,000)	106,250 250,000 300,000		Bank(apply money) Bank(allotment money)	637,500 18750
		656,250			656,250

DR ORDINARY SHARE CAPITAL CR

	forfeited share(1x5000)	5000	1-Jan	Balance b/d	500,000
				1st call	250,000
	Balance c/d	1,000,000		Appl.and allotment	250,000

		1,005,000			1,005,000
				Balance b/d	1,000,000

DR FORFEITED SHARE ACCOUNT CR

	call in arrears	2500		ordinary share	5000
	forfeited issued	2500			
		5000			5000

DR FORFEITED SHARE REISSUE ACCOUNT CR

	ordinary share(1x5000)	5000		forfeited share	2500
	share premium	2000		Bank(0.90x5000)	4500
		7000			7000

DR 1ST CALL ACCOUNT CR

	ordinary share(500,000x0.5)	250,000		call in arrears(0.5x5000) Bank	2500 247,500
		250,000			250,000

DR SHARE PREMIUM ACCOUNT CR

	Balance c/d	302,000		Appl.and allotment forfeited share	300,000 2000
		302,000			302,000
				Balance b/d	302,000

DR CALL IN ARREARS ACCOUNT CR

	1st call	2500		forfeited share	2500
		2500			2500

Allotment re**c**eived

Due on allotment (0.25 x 500,000) = 125,000

Less; excess on application (0.85 x(625,000 – 500,000) (106250)

18750

BALANCE SHEET AS AT 30/9/2007 (Extract)

Authorized share capital			
ordinary share	1,500,000		
Issued paid up capital	1,000,000	Current assets	
		Bank	1,302,000
reserve & surplus			
share premium	302,000		
	1,302,000		1,302,000

REDEMPTION OF SHARE

Shares can be bought back from their holders direct on a specific data or range of dates.

METHODS OF REDEMPTION

Shares can be redeemed in two ways:-

(i) Out of distributable

e.g.- Credit balance on profit &loss A|c's

- General reserve

(ii) Out of fresh issue of share made for purpose of redemption

I: Redemption out of distributable profit

According to this method, an amount equal to the nominal value of the shares being redeemed is transferred from a reserve which could otherwise be distributed as cash dividend to a reserve account called capital Redemption Reserve Account.

Entry: Dr. Profit & loss appropriation A/c with the nominal value of the shares redeemed.

Cr. Capital Redemption Reserve A/c

The transfer to the capital Redemption Reserve A/c curtails the amount which could otherwise be distributed as cash dividend and so jeorpodice the company's liquidity.

II: Redemption out of fresh issue of shares:-

In this case shares can be redeemed out of issuing new share to the members. The issue should be made for the purpose of redemption. Now the amount to be transferred to the capital redemption reserve A/c shall be the difference between the nominal value of the shares now being redeemed and the proceeds from the fresh issue of shares.

Transfer to CR = Nominal value - cash collected out of fresh of shares redeemed issue.

Or = Nominal value of shares redeemed - Nominal value of cash collected out of fresh Issue.

PREMIUM PAYABLE ON REDEMPTION

If the company redeems shares above par (at premium) the premium payable on redemption, shall be appropriated from the distribution profit.

The share premium a/c can be utilized in paying the premium payable on redemption, if the share now being redeemed were originally issued at a premium and a new issue of shares is being made for the purpose.

Now the share premium A/c can be used to meet the premium on redemption only to the extent of the lesser of:-

(i) To credit balance of the share premium A/c after crediting the premium on fresh (new) issue.

(ii) The amount of the share premium received on the original issue pf the shares now being redeemed.

COMPANY ACCOUNT 1.2

CAPITAL REDEMPTION RESERVE

The balance on this A/c can be utilized in paying up the unissued shares of a company as fully paid Bonus shares.

ISSUE OF BONUS SHARES

The receive to provide for the Bonus shares may be used in the following order:-

(i)` Capital Redemption Reserve.

(ii) Share premium.

(iii) Other Reserves (e.g. profit /loss balance, general reserve).

ENTRIES REDEMPTION OF SHARES

A) **Declaration of redemption**

Dr. Redeemable preference share capital A/c

Cr. Preference share redemption A/c

B) **Premium payable on redemption**

Dr. Share premium A/c or P & L appropriation A/c

Cr. Preference share Redemption A/c

C) **Redemption of shares**

Dr. Preference share Redemption A/c

Cr. Cash / Bank/c

D) **Transfer of the nominal value of the shares being redeemed**

Dr. P&L appropriation. A/c

Cr. Capital Redemption Reserve A/c

Example:

Mpenetecho Co. Ltd had 800,000 % redeemable preference shares of Tshs.1 each in issue originally issue at a premium of act 40 per share. The company

new proposes to redeem 200,000 of these shares at Tshs. 1/60 per share financed partially by the issue of 160000 ordinary shares of sh. 1 per share at Tshs. 1/20. Prior to the issue of replacement shares the share premium A/c had a credit balance of Tshs. 242,000.

Show the amount of premium payable on redemption to be approached from;-

(a) Share premium A/c

(b) Distribute profit

Solution

Given: Premium on original issue = 0.40

Premium on fresh issue = 1 - 1.20 = 0.20

Premium on original issue = 0.4 x 200,000

= 80,000

Premium on redemption = 0.6 x 200,000

= 120,000

Premium on fresh issue = 0.2 x 160,000

= 32,000

REDEMPTION OF DEBENTURES

Strictly used, Debenture is a written acknowledgement of a debit, by a limited company providing terms and conditions as for its security, interest and repayment.

Or

It can loosely be defined as an account borrowed by a limited company.

An issue of debenture (i.e obtain of loan from the public) may be documented under seal, (with the added formality of being executed in Deed form).

SECURITY:-

The security may take the form of fixed assets which may be applied for the benefit of the debenture holders on a breach of the debenture deed. (E.g. failure to pay interest, involvement). That is why we have mortgage debentures and simple or married debentures.

Mortgage debentures are the debentures in which assets have been pledged.

Naked debentures are the debentures without security. The security may be described as fixed or floating.

Fixed charge:-

Granted on fixed assets which can be applied for the benefit of the debenture holders on a breach of the debentures deed. While the charge is operative, the security may neither be traded nor exchanged. On the breach of the debenture deed, the assets can then be applied for the benefit of the debentures holders.

Floating charge:-

Granted so as to apply to all assets, and while the charge is operative, the assets can either be traded or exchanged. On the breach of the debenture deed, the charge crystallizes and assets the priority of the debenture holders.

TRUSTEE

The Debenture Deed will appoint a trustee for the debenture holders whose work is to safe guard the interest of the debenture holders. On the breach of the Trust deed, the trustee will appoint a receiver who will seize the security (property) and apply if for the benefit of the debenture holders' arrangement for the repayment of the debenture issue.

REDEMPTION OF DEBENTURES

Debentures can be bought back (redeemed) using the following methods:-

(a) **Sinking fund method / Debenture Redemption fund method**.

Under this method a fixed sum calculated from the sinking fund tables is set aside and invested in outside securities which together with interest compounded annually and calculated using a fixed rate, a sufficient sum will them be available to redeem (repay & the debentures on their maturity.

(i) At the end of the first year:-

(a) Dr. P & L appropriation A/c with the annual appro.

Cr. Sinking fund A/c / Debenture redemption sum set aside.

(b) Dr. Sinking fund investment A/c / Debenture Redemption fund

Investment A/c.

Cr. Cash / Bank A/c with the equipment amount invested.

(ii) At the end of the second and subsequent years.

Dr. P. & L appropriation A/c with interest received on investment

Cr. Sinking Fund A/c

(b) Dr. Cash / Bank A/c with interest received on investment.

Cr. Sinking Fund A/c

(c)Dr. Sinking Fund investment A/c with both the fixed sum (+)

Cr. Cash / Bank A/c interest now being re invested.

(iii) At the end of the final year (the year of redemption:-

(a) Dr. P& L appropriation A/c with the fixed sum set a side

Cr. Sinking fund A/c investment

(b) Dr. Cash / Bank A/c with interest received on investment

Cr. Sinking fund A/c

NB: At the end of the final years, no further investment is made instead of security will be sold out.

Entries :-

(i) Dr. Cash / Bank A/c with cash received on sale of the

Cr. Sinking fund investment A/c investment.

(ii)Dr. Sinking Fund Investment A/c with profit on sale of the investment

Cr. Sinking fund A/c

NB: The balancing figure on the sinking fund A/c after the debentures have been redeemed, will be transferred to the general reserve.

Entry:-

Dr. Sinking fund A/c with transfer of the balance

Cr. Reserve A/c

EXERCISE

Debentures of Tshs. 30000 are issued on 1st Jan. 2003. Redemption is to take place on equal terms four years later. The company decided to set aside an equal amount to be invested at 5% which will provide Tshs. 30000 on maturity. Tables show that Tshs. 0.232012 invested annually will produce sh. 1 in 4 years time.

You're required to show:-

(a)Debenture redemption reserve A/c (sinking fund / Debentures redemption A/c)

(b)Debenture sinking fund investment A/c

(c)Debentures

(d) Profit and Loss extracts

DR SINKING FUND ACCOUNT CR

			1.1.2004	Balance b/d	6960
31.12.04	balance c/d	14,268	31.12.04	P & L Appr.	6960
			31.12.04	cash(interest)	348

		14268			14268
			1/1/2005	Balance b/d	14,268
			31.12.05	P & L Appr	6960
31.12.05	balance c/d	21941		cash(interest)	713
		21941			21941
			1/1/2006	Balance b/d	21941
31.12.06	Debenture Reserve	30,000	31.12.06	P & L Appr	6960
		8057	31.12.06	cash(interest)	1097
			31.12.06	Deb.sink.fund inv.	8059
		38057			38057

PURCHASE IN THE OPEN MARKET

At times a company can buy its own debentures in the open market. This practice should be allowed by the terms of issue.

This brings a financial sense if the market value is below the present value of the further interest payments plus the sum payable on redemption.

The debentures can be bought back for cancellation. The purchase of debentures in the open market can be ex-int or cum – int.

If it is ex – int, then this means it is without interest, and therefore interest has to be calculated and added to the purchase price.

And if it's cum – int, then this means it is with interest and therefore for recording purpose, the interest included should be deducted from the total price paid.

Entries:-

Purchases of debentures for cancellation

(i)Purchase of own debentures in the open market.

Dr. Investment in own debentures A/c

Cr. Cash / Bank A/c

(ii)Pre – acquisition interest included in the purchase price.

Dr. Debenture interest A/c

Cr. Investment in own debentures A/c

(iii)Cancellation of the debentures (Nominal value)

Dr. Redeemable debentures

Cr. Investment in own debentures A/c

(iv)Profit on cancellation of the debentures.

Dr. Investment in own debentures A/c

Cr. Sinking fund A/c / Debenture Redemption fund A/c

(v)The balance on the sinking fund A/c after all the debentures has been cancelled.

Dr. sinking fund A/c

Cr. Reserve A/c

Example:-

Super Mnyanyue Company had some years ago issued Tshs. 400,000 12% redeemable debentures. Under the terms of the trust deed the debentures would be redeemed or bought back on the open market at anytime. A sinking fund had been established for this purpose.

On 1st January 1998 the balance on debenture redemption fund was Tshs. 152400 and on debenture redemption fund investment Tshs. 112800.

The following transactions occurred during 1999:-

Jan. 14: Sinking fund investment bought Tshs. 38100.

May 16: Sinking fund investment income received Tshs. 8700

June 30: Debenture interest paid for half year Tshs. 24000

Sept. 15: Sinking fund investment sold (costing Tshs. 57000), Tshs. 61200

Sept. 30: Tshs. 60000/- debenture bought back on open moment at 97 and cancelled Tshs. 58200.

Oct. 16: Sinking fund income received Tshs. 5100.

Nov. 21: Sinking fund investment sold (cost Tshs. 43200) Tshs. 40,000.

Nov. 30: Tshs. 40000 debentures redeemed at 96 ci on open market and cancelled Tshs.

38400.

Dec.31: Debenture interest paid Tshs. 18000

Dec 31: Annual appropriation Tshs. 32000

Open, post and balance the appropriate accounts to record the above.

Solution:-

DR DEBENTURE REDEMPTION FUND ACCOUNT CR

21-Nov	Deb.Red fund inv.	3200		Balance b/d	152,400
31/12	General reserve	100,000	16-May	cash(income)	8700
				Deb.red.fund.inv profit on sale	4200
			16-Oct	cash(income)	5100
			30-Sep	invest.in own deb(profit)	
			30-Nov	inv.in own(profit)	3600
			31-Dec	P & L A ppr	32000
		209,600			209600

DR DEBENTURE REDEMPTION FUND INVESTMENT ACCOUNT CR

1-Jan	Balance b/d	112,800	16-Sep	cash	61,200
14-Jan	cash(purchase)	38,100	21-Nov	cash	40,000
16-Sep	Deb.red.fund profit on sale	4200	21-Nov	Deb.Red.fund	3200
				Balance c/d	50700
		155,100			155,100

DR 12%DEBENTURE INTEREST ACCOUNT CR

30-Jun	cash	24,000	31dec	P&l	45,800
30-Sep	investment in own	1800			
30-Nov	investment in own	2000			
31-Dec	cash	18,000			
		45,800			45,800

DR INVESTMENT IN OWN DEBENTURE ACCOUNT CR

30-Sep	cash	58200	30-Sep	12% Deb.interest	1800
30-Sep	Deb.Red fund(profit)	3600	30-Sep	Redeem deb	60,000
30-Nov	cash	38400	30-Nov	Deb.interest	2000
	Deb.Red fund(profit)	3600	30-Nov	Redeem deb	40,000
		103,800			103,800

Interest included = 3 month $60{,}000 \times \frac{12}{100} \times \frac{3}{12} = 1800$

Interest included = 5 month: $40{,}000 \times \frac{12}{100} \times \frac{5}{12} = 2000$

DR 12% REDEEMABLE DEBENTURE ACCOUNT CR

30-Sep	invest in own	60,000		Balance b/d	400,000
30-Nov	invest in own	40,000			
31-Dec	Bal.c/d	300,000			
		400,000			400,000

EXERCISE

1. Eight years ago Trafalgar Co. Ltd had issued Tshs. 300,000 12% Debentures. Interest was payable on both June 30th and Dec. 31st. Under the terms of the trust deed, the debentures could be redeemed on bought back on the married at any time after 1st Jan. 1999. A sinking fund had been established for this purpose.

On 1st Jan. 1994, the balance on debentures redemption fund Tshs 246,250 and on debenture redemption fund investment Tshs. 203,500.

The following transactions took place for the year 1994:-

Jan: Sinking fund investment bought for Tshs. 42,600

May 25: Sinking fund investment income received Tshs. 9230.

June 30: Debenture interest paid 800

Aug. 14: Sinking fund investment sold (cost Tshs. 71,200) for Tshs. 79600.

Aug. 31 Tshs. 100,000 debentures bought back on open market at 97 cum – int and cancelled.

Sept. 30: Tshs. 100,000 debentures bought back on open market at 96 cum-int and cancelled.

Oct. 24: Sinking fund investment income received Tshs. 8920.

Dec. 19: Sinking fund investment sold (cost Tshs. 82500) for Tshs. 81000

Dec. 31: Debenture interest paid

Dec 31: Annual appropriation Tshs. 44,000

Required:

Open post and balance the appropriate ledger accounts to record the above transactions.

DR DEBENTURES REDEMPTION ACCOUNT CR

19-Feb	Deb.red.fund.inve	1500		Balance b/d	246,250
31-Dec	General reserve	200,000	25-May	cash(income)	9230
			14-Aug	Deb.red.fund inve	8400
			24-Oct	cash(income)	8920

			30-Sep	investment in own Deb.	7000
			31-Aug	investment in own Deb.	5000
			31-Dec	P & L Appr	44,000
		328,800			328,800

DR DEBENTURES REDEMPTION FUND INVESTMENT ACCOUNT CR

	Balance b/d	203,500	14-Aug	cash(sale)	79,600
			19-Dec	cash(sale)	81,000
			19-Feb	Deb.red.fund(loss)	1500
			31-Dec	Balance c/d	92,400
		254,500			254,500
1-Jan	Balance b/d	92400			

DR 12% DEBENTURE INTEREST ACCOUNT CR

30-Jun	cash	18,000	31-Dec	P & L	29,000

8/31/9/31	invest.in.own.deb invest.in.own.deb cash	2000 3000 6000			
		29,000			29,000

DR INVESTMENT ON DEBENTURE ACCOUNT CR

31-Aug	cash	97,000	31-Aug	Redeemable deb.	100,000
30-Sep	cash	96,000	31-Aug	Debenture interest	2000
31-Aug	Deb,red,fund(profit)	5000	30-Sep	Redeemable debenture	100,000
30-Sep	Deb,red,fund(profit)	7000	Sep-31	Debenture interest	3000
		205,000			205,000

DR REDEEMABLE DEBENTURES ACCOUNT CR

31-Aug	invest.own.Deb	100,000		Balance b/d	300,000

30-Sep	invest.own.Deb	100,000			
31-Dec	Balance c/d	100,000			
		300,000			300,000

Interest 30/6: $300,000 \times \frac{12}{100} \times \frac{6}{12} = 18,000$

31/12: $100,000 \times \frac{12}{100} \times \frac{6}{12} = 6000$

2. Some years ago Mplc had issued 375,000 of 10% debenture. 2000/2010 at par. The term of the issue allow the company the right to purchase these debentures for collection at or below per with an option to redeem at a premium of 1 percent, on 30 Sept. 2006. The exercise this option the company must give three months notice which it dully did on 30 June 2003 indicating its intention to redeem all the debenture outstanding at 30th Sept. 2006.

MPLC had established a sinking fund designed o accumulate the sum of Tshs. 378750 by 30 September 2006 and had appropriated profits annually and invested these, together with the interest from such investments and profits made on any realizations from time to time.

A special No. 2 bank account was established specifically to deal with the receipts and payments relating to the debentures and the sinking fund.

By 30 June 2006 annual contributions amounting to Tshs. 1334,485 together with the interest on the sinking fund investment of 39480 had all

been invested except for 2475 which remained in the No. 2 account at the date.

The only investment sold, prior to 30th June 2006 had cost 144,915 and realized 147,243. This was used to re purchase debenture with a par value of 150,000.

Transactions accruing between 1 July and 30th Sept. 2006 were:

(i) Interest received on the sinking fund investment

7th July	1,756
13th Sep.	1,455

(ii) Proceeds from the sale of investments:-

2nd Aug.	73,215	(Book value was 69322)
25th Sept.	160,238	(remaining investment)

(iii) Redemption of all debentures on 30th Sept. with the exception of 15,000 held by B. Limited. The company had received notice of a gamishee order.

(iv) MPLC deposited with the W. Bank P/C the sum of 15,150 on 30th Sept. 2006. (You are required to ignore debenture interest and income tax).

Required:-

From the information given above to prepare the ledger accounts (Including the No. 2 bank A/c/o in the books of MPLC for the period 30th June to 30 Sept. 2006.

Showing the transfer:

Solution

Sinking fund investment	
Annual contribution	334485
Add; interest	39480
profit on sale of investment	2328
profit o purchases	2757
	379050
less; Debenture purchased	150,000
	229,050
Sinking fund investment	
Annual contribution	334485
Add; interest(39480 -2475)	37005
	37490
less; investment sold	144915
	226575
Debenture	
original value	375,000
less; Debenture purchased	150,000
	225,000

DR BANK ACCOUNT CR

Balance b/d	2475	W.Bank	15150
interest	1756	Deb.redeemable	212100
interest	1455		
Total inv.sold	233453	Balance c/d	11889
	239,139		239139

DR SINKING FUND ACCOUNT CR

Prem.on redemption	2250	Balance b/d	229,050
	236,889	interest on debenture	1756
		interest	1455
		profit on sale	3893
		profit on sale	2985
	239,139		239,139

DR SINKING FUND INVESTMENT ACCOUNT CR

Balance b/d	226575	sale of investment	73215
profit on sale	3893	sale of investment	160238
profit on sale	2985		
	233,453		233,453

DR DEBENTURE ACCOUNT CR

Debenture Redemption	225,000	Balance b/d	225,000
	225,000		225,000

DR DEBENTURE REDEMPTION ACCOUNT CR

Bank	212100	10% Debenture	225,000
Balance c/d	15150	Premium on redemption	2250
	227,250		227,250

(iii) **Annual drawings out of profit:-**

In this case, an amount equal to the nominal value of the debenture to be redeemed is debited to the P & L appropriation A/c and credited to the Debenture redemption reserve A/c, the balance of which will be transferred to the capital. Reserve A/c once all the debentures have been redeemed.

Accounting entries:-

(a) Annual appropriation of the nominal value of the debentures redeemed:-

Dr. P & L Appropriation a/c

Cr. Debenture redemption reserve A/c

(b) Director's approval of the redemption of the debenture (Nominal value):-

Dr. Redeemable debenture A/c

Cr. Debenture redemption A/c

(c) Premium payable on redemption:-

Dr. Share premium and or P&L appropriation

Cr. Debenture redemption A/c

(d) Redemption of the debentures:-

Dr. Debenture redemption A/c

Cr. Cash / Bank A/c

(e) Profit on the redemption:-

Dr. Debenture redemption A/c

Cr. P&L A/c

Example:-

Champwili P&L had issue Tshs. 200,000 8% Redeemable Debentures. Under the terms of issue, redemption was to be effected by equal annual drawings over 10 years on 31st December each year starting 1996.

Eight years offer on 1st Jan. 2004, balance on 8% redeemable Debenture and on debenture redemption reserve accounts were Tshs. 400,000 and Tshs. 160,000 respectively. A further redemption took place in 2004 at 96 and the final redemption in 2005

Open, post and balance the appropriate accounts for the years 2004 and 2005.

EXERCISE

1. Kapirimposhi P&L had issued 500,000 12% Redeemable debentures in 1990 on which interest was paid half yearly on 30th June and 31/12 under the terms of the issue they were to be redeemed by equal annual drawings over 10 years on 31/12 from the year 1996 onwards.

8 years later on 1st Jan. 2004 the balances on debenture redemption reserve and 12% redeemable debentures were Tshs. 400,000 and Tshs. 100,000 respectively. A further redemption was affected in 2004 at 95 ex- int and the final redemption, 2005 at par ex- int – pen, post and balances the appropriate accounts to record the above transactions for each of the years 2004 and 2005.

DR 12% REDEEMABLE DEBENTURE ACCOUNT CR

31.12.2004	Deb.Red.	50,000	1.1.2004	Balance b/d	100,000
31.12.2004	Balance c/d	50,000			

		100,000			100,000
31.12.2005	Deb.redemption	50,000	1.1.2005	Balance b/d	50,000
		50,000			50,000

DR DEBENTURE REDEMPTION RESERVE ACCOUNT CR

31.12.2004	Balance c/d	450,000	1.1.2004	Balance b/d	400,000
				P & L Appr.	50,000
		450,000			450,000
31.12.2005	Capital reserve	500,000	1.1.2005	Balance b/d	450,000
			31.12.2005	P & L Appr.	50,000
		500,000			500,000

DR DEBENTURE REDEMPTION ACCOUNT CR

31.12.2004	cash	47500	31.12.2004	12% Red.debenture	50,000
31.12.2004	P & L	2500			

		50,000			50,000
31.12.2004	cash	50,000	1.1.2005	12% Deb.red	50,000
		50,000			50,000

DR DEBENTURE INTEREST ACCOUNT CR

30.06.2004	cash	6000	31.12.2004	P & L	12,000
30.06.2004	cash	6000			
		12,000			12,000
1.12.2005	cash	3000	31.12.2005	P & L	6000
31.12.2005	cash	3000			
		6000			6000

(iv) Insurance Policy method:-

Instead of investing the sum in securities, the same is paid by way of an Insurance premium to an Insurance company which issues an endorsement policy of the amount equal to the sum payable on redemption and maturing on the date when the debentures become repayable.

The premium paid annually is debited to the debenture redemption fund policy A/c and credited to the cash / Bank A/c, and the premium is paid at the beginning of a period.

The same amount will be set aside out of profit & loss appropriation A/c through debiting profit and loss appropriation A/c and crediting debenture redemption fund A/c.

On the maturity of the policy:-

Dr. Cash / Bank A/c

Cr. Debenture Redemption fund policy A/c) with sum received on the maturity of the policy and any balance on the Insurance policy A/c shall be taken to the debenture Redemption fund (Deb. Red. Reserve) A/c

If a Cr. Balance - Dr. Deb. Fund policy A/c

Cr. Deb. Red. Fund A/c

If a De. Balance - Dr. Deb. Red. Fund A/c

Cr. Deb. Fund policy A/c

On the redemption of the debentures:-

Dr. Redeemable Debenture A/c / Debenture Redemption

Cr. Cash / Bank A/c

The credit balance on the deb. Redemption Fund A/c shall be transferred to a Reserve A/c.

Entry: Dr. Deb. Redemption Fund A/c

Cr. Reserve A/c

Example:-

A company has a debenture on issue of Tshs. 150,000 on 1st Jan. 1990. It decided to provide for the redemption of the debentures for Tshs. 1,500,000 for 3 years. The annual premium is Tshs. 47,500. Show the necessary ledger accounts to record the above using the Insurance policy method.

DR REDEEMABLE DEBENTURE CR

31.12.90	Balance c/d	150,000	1.1.90	cash	150,000
		150,000			150,000
31.12.91	Blance c/d	150,000	1.1.91	Balance b/d	150,000
		150,000			150,000
31.12.92	Deb.red.	150,000	1.1.92	Balance b/d	150,000
		150,000			150,000

DR DEBENTURE RED.FUND INSURANCE POLICY ACCOUNT CR

1.1.90	cash(in.prem)	47500	31.12.90	Balance c/d	47500
		47,500			47,500
1.1.91	Balance b/d	47500	31.12.91	Balance c/d	95,000
	cash(in.prem.)	47500			
		95,000			95,000

1.1.92	Balance b/d	95000	31.12.92	cash	150,000
1.1.92	cash(in.prem.)	47500			
	Deb.Red.fund	7500			
		150,000			150,000

DR DEBENTURE REDEMPTION FUND ACCOUNT CR

31.12.90	Balance c/d	47,500	31.12.90	P & L	47500
		47,500			47,500
31.12.91	Balance c/d	95,000	1.1.91	Balance b/d	47500
				P & L Appr.	47500
		95000			95000
			1.1.92	Balance b/d	95000
31.12.92	Deb.redemption	150,000	31.12.92	P & L Appr.	47500
			31.12.92	Deb.red.fund policy	7500
		150,000			150,000

DR DEBENTURE REDEMPTION ACCOUNT CR

	cash	150,000	31.12.92	Redeemable Deb.	150,000

		150,000			150,000

EXERCISE

1. A Ltd company issued Debentures of Tshs. 600,000 on 1st Jan. 1992 and decided to provide for the redemption by means of an Insurance policy for Tshs. 600,000. The annual premium was Tshs. 190000. Prepare the necessary ledger accounts assuming that the amount of policy was dully released and debentures were paid.

2. The following balances appeared in the books of a limited company on 31st Dec. 1997:-

	Dr.	Cr.
6% Debentures.		Tshs. 500,000
Debentures redemption Insurance policy.	Tshs. 460'000	
Debenture redemption fund		Tshs. 460'000

The policy amount was Tshs. 500,000 and the annual premium were received, and the debentures were redeemed.

-You are required to prepare the necessary ledger accounts in the books of the company.

OUT OF CAPITAL METHOD:-

Example:-

A Ltd co. had a debenture on issue of Tshs. 15000 on 1st Jan. 1990 at a discount of 5%, repayable at par by annual drawings of Tshs. 3000 for five years. Show the necessary ledger accounts for the first year to record the above.

Solution:-

Discount on debenture = 5/100 x 15000 = 750.

DR CASH ACCOUNT CR

	Deb.Appl.&Allot	14250		Deb.,redemption	3000

DR DEB.APPLICATION & ALLOTMENT CR

	Redeem Deb.	15,000		Bank	14250
				Disc on issue	750
		15,000			15,000

DR REDEEMABLE DEBENTURES ACCOUNT CR

1st year	Deb.Redemption	3000			15,000

31.12.90	Bal.c/d	12,000			
		15,000			15,000
				Balance b/d	12,000

DR DISCOUNT ON ISSUE DEBENTURE ACCOUNT CR

	Deb.Appl.&Allot	750	31.12.90	P & L	250
				Bal. c/d	500
		750			750

DR DEBENTURE REDEMPTION ACCOUNT CR

311.2.91	cash	3000		Reedemable Deb.	3000
		3000			3000

Discount on deb. Written off = 5/15 x 750 = 250.

COMPANY FINAL ACCOUNTS

They consist of the trading A/c and Profit and Loss A/c. The trading and profit and loss A/c of a company are similar to those of a sole proprietorship, except that in the profit and loss A/c of the company, the following items can be seen to have been debited to it, there are:-

(a) Debenture Interest

(b) Directors salaries or fees or emoluments

(c) Audit fees or charges

And to the credit side there can be shown a part from the gross profit made other gains such as Dividends received.

In this section / A/c the distribution of profit is shown. It is in this A/c that appropriation items such as corporation tax payable, proposed dividend interim dividend, reserve transfer etc are listed.

Corporation tax:-

It is a tax levied on a company's profit.

Dividend:-

The term dividend originates form a Latin word "Dividend" meaning to dividend. It is that part of the profit of a company which is distributed among its share holders.

TYPES OF DIVIDEND:-

(a) Interim Dividend

(b) Proposed Dividend

(a) **INTERIM DIVIDEND**

The word "Interim" originates from Latin meaning "in the meantime"

It is a dividend which is declared before the close of the company's financial period.

(b) **PROPOSED DIVIDEND**:-

This is only provided for and so not paid before the accounts are closed.It's shown itself among items on the Balance sheet as "proposed dividend or unpaid dividend"

To the credit side of the appropriation A/c is included such items as the Net profit made during the year and balance of profit it from the previous year.

DR APPROPRIATION ACCOUNT FOR THE YEAR ENDED 31STDEC1999 CR

Dividends, interim	xx	Balance b/d	xxx
proposed	xx	Net profit made during the year	xxx
written off expenses	xx		
corporation tax payable	xx		
Transfer to reserve e.g CRR	xx		
Bal. c/f (retained earnings unappropriated balance)	xx		
	xxxx		xxxx

Sales		xxxx
less; Return inwards		xxx
		xxxx
Deduct; cost of goods sold ; opening stock	xxx	

Add; purchases xxx		
carriage inwards xx		
less; Return outwards xxx	xxx	
Net purchases	xxx	
less; closing stock	xxx	xxx
Gross profit		xxxx
Add ; other gains e.g. dividend/interest received		xxx
		xxxx
Deduct ; Directors salaries xx		
Debenture interest xx		
Stationery xx		
Audit fees xx		xxx
Net profit made during the year before tax		xxxx
Deduct ; corporation tax		xx
Net profit after tax		xxx
Add ; Net profit b/f (previous year)		xx
		xxx
Deducts ; dividend interim xx		
proposed xx		
Transfer to general reserve x		xxx
Balance c/f Retained earnings/un appropriated balance		xxx

BALANCE SHEET AS AT 31/12/1999

Fixed Assets	cost	Depreciation	Net
Premises	xxx	-	xxx
Furniture & fittings	xx	x	xx
Machinery	xx	x	xx
Motor vehicle	xx	x	xx
	xxx	xx	xxx
Deduct; Net current Assets			
or Working capital			
Current Assets			
stock	xxx		
Debtors xx			
less; provision x	xx		
cash	x		
	xxx		
less; current liabilities			
sundry creditors xx			
proposed dividend xx			
corporate tax payable xx	xx		xx
Net assets			xxx
Financed by;			
Authorized share capital			

ordinary shares of each /=			xxx
Issued & paid up capital			
ordinary shares of /= each			xxx
Reserves & surplus			
P & L balance (retained earnings)			xxx
share premium			xx
ordinary share holder fund/Equity			xxx
Add; % Debentures			xx
capital employed			xxx

EXERCISE:-

Here is a trial balance of RF Ltd as at 31st June 2008.

	DEBIT	CREDIT
share capital - authorized & issued		50,000
stock as at 30th June 2007	38,295	
Debtors	26890	

creditors		12310
10% Debentures		20,000
Fixed replacement reserve		10,000
General reserve		6000
P & L A/c as at 30th June 2007		3964
Debenture interest	1000	
equipment at cost	35,000	
Motor vehicle at cost	28500	
Bank	3643	
cash	180	
sales		99500
purchases	66,350	
Returns Inwards	1150	
carriage inwards	240	
wages and salaries	10360	
Rent, Rates and insurance	5170	
Discount allowed	1246	
Directors remuneration	2500	
provision for depr.at 30th june2007		
equipment at cost		8400
Motors		10350
	220,524	220,524

Given the following information as at 30th June 2008, drawn up a set of financial statements for the year to that date.

(i) Stock 30th June 2008 Tshs. 4937.

(ii) The share capital consisted of 25000 ordinary shares of sh. Each and 25000 10 per cent preference shares was proposed to be paid as well as a dividend of 20 per cent on the ordinary shares.

(iii) Accrued rent Tshs. 700. Directors remuneration Tshs. 2500.

(iv) Debentures interest ½ years interest owing.

(v) Depreciation cost equipment 10 percent reserve, motors 20%.

(vi) Transfers to Reserve; General reserve Tshs. 2000. Fixed assets replacement reserve Tshs. 1,000.

(vii) Provide 50% as corporation tax payable.

PROFIT &TRADING & LOSS APPROPRIATION ACCOUNT & B/SHEET.

Sales		99500
less; Returns inwards		1150
Net sales		98350
Deduct; cost of goods sold		
opening stock	38295	
Add; purchases	66350	
	104,885	
less; closing stock	49,371	55,514
Deduct; wages and salaries 10360		

Rent (5170 + 700)	5870	
Debenture interest	1000	
Debenture owing	1000	
Discount allowed	1246	
Directors remuneration	5000	
Depr; Equipment(10/100 x 35000)	3500	
Motors(20/100 x 28500)	5700	33676
Net profit made before tax		9160
Deduct;corporation tax(50% x 9160)		4580
Net profit after tax		4580
Add; Net profit b/f(previous yr)		3964
		8544
Deduct; dividend interim	2500	
proposed (20/100 x 2500)	5000	
Transfer to reserve(1000+2000)	3000	10500
		1956

BALANCE SHEET AS AT30TH JUNE 2008

Fixed Assets	cost	Depreciation.	Net
Equipment	35,000	(8400+3500)	23100
	28500	(10350+5700)	12450

		63,500	27,750	35,550
Deduct; Net current Assets				
Current Assets				
stock	49371			
Debtors	26890			
Bank	3643			
cash	180			
80,084				
less; current liabilities				
sundry creditors	12310			
proposed dividend	2500			
Corporate tax payable	4580	19390		60694
				-25144
Financed by;				
Authorized share capital				
(50,000 - 25,000) ord.share of 1@				25,000
Reserve & surplus				
P & L Balance				1956
Add; 10% Debenture				20,000

Capital employed			21,956

HIRE PURCHASE ACCOUNTING

HIRE PURCHASE TRANSACTIONS.

As a system of trading, hire purchase is governed by the hire purchase act. Under this system the buyer agrees to pay for the goods by installments.

The property in goods remains with the seller and the buyer pays hire charges over a stipulated period of time at the end of which the pays a further amount called an option to purchase/ option fee which then gives him ownership. The buyer obtains possession for the goods and uses them, but ownership for the goods will pass from the seller to the buyer when the latter pays the final installment. If the buyer he fails to pay any installment, then seller will be entitled to take back the goods (repossess) and the buyer shall have no any claim over the installment he already paid.

ACCOUNTING PART

1. Buyers books.
2. Sellers books.

Hire- purchase transactions in the buyers books

Goods which are dealt with are usually fixed assets such as motorcars, refrigerators and etc.

The hire purchase price actually it consists of two elements:-

1. Cash “cost” price and
2. Hire purchase interest.

This acts as compensation to the seller for delay in receiving a full payment at once and also for covering up some attendant risks.

N.B

It is a normal accounting policy to treat hire purchase transactions as actual sales or purchase, because the intentions of the buyer 1st pay the whole amount through installments.

Methods of writing off the title purchase interest.

1. Straight line / fixed installment methods.
2. Sum of the digits method (or rule of 78 methods).
3. Actuarial method.

This interest should be written off to P & L A/C over the period of the hire purchase contract.

1. **Straight line method**

Under this method, the hire purchase interest written off on the straight line basis. Therefore the hire purchase interest per installment due = (Total hire purchase /Interest)/(Total number of interest).

1. **Some of the years' digits method**

This is an arithmetical method of apportioning the hire purchase interest in approximate proportion to the amount outstanding at any time.

Procedure

1. Number the installments e.g. 3 installments

   1

   2

   3

2. Assign the highest digit to the first installment and digit one to the last installment

Installment	digits
1	3

2 2

3 1

3. Sum up the digits 6

4. Apportion the H.P. interest e.g I H.P interest = Tshs 36000
   1. Apportion the H.P. interest e.g I H.P interest = Tshs 36000

      1st Year hire purchase interest =3/6 x 36000

      = 18000

      2nd year hire purchase interest = 2/6 x 36000

      = 12000

      3rd year hire purchase interest = 1/6 x 36000

5. =6000
6.

Buyer's books continue

1. **Actuarial method**

This is method of the writing off the hire purchase interest based on the reducing balance phenomenon.

This method can be used in the presence of the following items:-

Cash price, deposit, (not necessary) rate of interest, number of installments together with their respective amounts.

Working:-

cash price	xxx
less; Deposit	xx
Balance subject to H.P Interest	xxx
Add; Hire purchase interest;1st yr	xx
	xxx
Deduct; 1st yr installment paid	xxx
Balance subject to H.P Interest	xxx
Add; hire purchase interest;2nd yr	xx
	xxx
Deduct; 2nd yr installment paid	xxx
Balance subject to H.P Interest	xx
Add; hire purchase inter.3rd yr	xx
	xx
Deduct; 3rd and final instal. Paid	xx
	NIL

METHOD OF RECORDING.

There are two alternative methods of recording.

Method A

Accounting entries:

1. Dr fixed asset A/C

   Cr seller / vendor/ credit A/C

With the cash "cost price

2. Dr; H.P. interest expense A/C
   Cr; vendor A/C

With the proportion of the H.P interest when

Installment is due

3. Dr. Vendor A/C
   CR cash / bank A/C

With the deposit + installment paid

N.B

Balance on the vendor A/C represents the unpaid portion of the cash price, which should be included under current liabilities in the B/S.

METHOD B

1. Dr. Fixed assets A/C with the cash price
   Dr H.P interest suspense A/C with the total H.P interest
   Cr, vendors A/C with total H.P price.

2. Dr. H.P interest expense A/C
   Cr H.P interest suspense A/C

with the proportion of the H.P interest installment is due

3. Dr; Vendor A/C
Cr; cash / bank A/C } with the deposit + installment paid

N.B

The balance on the vendor A/C less the balance of hires purchase interest suspense A/ shall be included current liabilities in the balance sheet.

Example

On 1st Jan 1991, contractor's ltd bought a hydraulic crane from Hi – lift ltd on hire purchase. The terms o f H.P contract were initial deposit of Tshs 40000 was payable followed by 3 installments of Tshs 37978 on 1st Dec in each of the next three years from 1991 onwards. The cost of the crane for cash purchase would have Tshs. 120,000. Interest is charged on the balance out standing 31st Dec at the rate of 20% p.a. the final year of both company's end 31st Dec.

Required

1. What was amount of H.P. Interest included in the H.P price?
2. What amount of interest could allocated in each of three years if the sum of digits method were used.
3. Prepare the relevant ledger a/c contraction ltd ledger for each of the three year ended 31st Dec 1991, 1992, 1993 base on the assumption that contractors ltd charges depreciation on his fixed assets. Using a straight line method in addition 20% p.a interest rate is in uses.

Solution

cash price	120,000
less; Deposit	40,000
Balance subject to H.P Interest	80,000
Add; H.p 1st yr 20/100 x 80,000	16,000
	96,000
Deduct; 1st yr installment paid	37978

Balance subject to H.P Interest	58022
Add; 2nd yr H.P interest 20/100 x 58022	11604
	69626
Deduct; 2nd yr installment paid	37978
Balance subject to H.P Interest	31648
Add; hire purchase inter.3rd yr 20/100 x 31648	6330
	37978
Deduct; 3rd and final instal. Paid	-37978
	NIL

a) Hire purchase = Total H.P price – cash price

= Deposit + 3 installments - cash price

= (40000 + 3 x 37978) - 120,000

= Tshs.33934

1. Calculate of the H.P. interest by the sum of the digit method.

Proportion of the H.P interest

1st year; 3/6 x 33934 = 16967

2nd year; 2/6 x 33934 = 11311

3rd year; 1/6 x 33934 = 5656

DR HI- LIFT COMPANY ACCOUNT CR

1/1/1991	Hi-lift company	120,000	31.12.1991	Bal. c/d	120,000

		120,000			120,000
1/1/1992	Bal. b/d	120,000	31.12.1992	Bal. c/d	120,000
		120,000			120,000
1/1/1993	Bal. b/d	120,000	31.12.1993	Bal. c/d	120,000
		120,000			120,000
1/1/1994	Bal. b/d	120,000			

DR HIRE PURCHASE INTEREST EXPENSE ACCOUNT CR

31/12/1991	Hi-lift coy	16,000	31.12.91	P & L	16,000
		16,000			16,000
31/12/1992	Hi-lift coy	11604	31.12.92	P & L	11604
		11604			11604
31/12/1993	Hi-lift coy	6330	31.12.93	P & L	6330
		6330			6330

DR PROVISION FOR DEPRECIATION ACCOUNT CR

31/12/91	Balance c/d	24,000	31.12.91	P & L	24,000
		24,000			24,000
31/12/92	Balance c/d	48,000	1/1/1992	Balance b/d	24,000
			31/12/1992	P & L	24,000
		48,000			48,000
31/12/93	Balance c/d	72,000	1/1/1993	Balance b/d	48,000
			31/12/1992	P & L	24,000
		72,000			72,000
		1/1/1994	Balance b/d		72,000

Example 2

A firm acquired two transport lames under hire purchase agreements, details of which are as follows:

Registration number	KQ710	KU600
Date of purchase	30TH May 1998	30th October 1998
Cash price	540000	720000
Deposit	93600	144000.
Interest (deemed to accrue) Every over the period of the Agreement)	76800	96000

Both agreements provided for the payment to be made in twenty four equal monthly installments commencing on the last day of the mount following purchase.

On 1st July 1999 vehicle KQ710 become a total loss in full settlement on 10th July 1999.

1. An insurance company paid Tshs 42000 under a comprehensive policy and
2. The hire purchase company accepted Tshs 190000 for the termination of the agreement.

   The firm prepared the accounts annually to 31st December, and provided depreciation on a straight line basis at a rate of 25% per annum for motor vehicle. With a full year depreciation in the year of purchase no depreciation being provided in the year of disposal.

   All installments were paid on the due dates.

Required:

Record these transactions in the following accounts, carrying down the balance as on 31 Dec 1999.

1. Motor vehicles
2. Provision for depreciation

3. Motor vehicles disposal
4. Hire purchase company
5. Hire purchase interest suspense A/C

Working;

	KQ710	KV600
Monthly 1 installment payable ; cash price	540,000	720,000
less: deposit	93600	144,000
	446,400	576,000
Add; H.P Interest	76800	96,000
	523,200	672,000
	24	24
monthly installment payable	21,800	28,000
	76,800	96,000
	24	24
Monthly H.P Interest payable	3200/=	4000/=

DR MOTOR VEHICLE ACCOUNT CR

30/4/98	H.P company	540,000	31/12/98	Balance c/d	126,000
30/9/98	H.P company	720,000			
		126,0000			126,0000
			1/7/1999	M.vehicle disposal	540,000
			31/12/99	Balance c/d	720,000
		126,0000			126,0000
1/1/2000	Balance b/d	720,000			

Total installment paid for 1998 for

KQ710	KV600
31/5 - 31/12/98 (7 months)	2 months
7 x 21800	2x28000
=152,600	= 56,000

152,600 + 56,000 = 208,600

DR HIRE PURCHASE COMPANY ACCOUNT CR

30/4/98	cash(deposit KU)	93600	30/4/98	Motor vehicle	540,000
	cash(deposit KU)	144000	30/4/98	H.P Interest	76800
	cash(KQ + KU)	208600	30/9/98	Motor vehicles	720,000

31/12/1998	Balance c/d	986,600	30/4/98	H.P Interest sus.	96,000
		1432800			1,432,800
10/7/1999	cash(KQ)	130800		Balance b/d	986,600
10/7/1999	cash	190,000			
10/7/1999	H.P interest susp.	49800			
31/12/99	cash(KU)	336,000			
31/12/99	Balance c/d	280,000			
		986,600			986,600

DR HIRE PURCHASE INTEREST SUSPENSE ACCOUNT CR

30/4/98	H.P company	76800	31/12/98	P & L	30400
30/4/98	H.P company	96,000	31/12/98	Balance c/d	142400
		172,800			172800
1/1/1999	Balance b/d	172,800	10/7/1999	H.P company(disc)	49800
			31/12/99	P & L(KQ)	4600
			31/12/99	P & L(KU)	48000
			31/12/99	Balance c/d	40000
		142,400			142,400
1/1/2000	Balance b/d	40,000			

DR M. VEHICLE ACCOUNT PROV.FOR DEPREC. ACCOUNT CR

	Balance c/d	315,000	31/12/98	P & L	315,000
		315,000			315,000
	Disposal	135,000	1/1/199	Balance b/d	315000

	Balance c/d	360,000	31/12/99	P & L	180,000
		495,000			495,000

DR MOTOR VEHICLE DISPOSAL ACCOUNT CR

1/7/1999	Motor vehicles	540,000	1/7/1999	M.V prov.for depr.	135,000
31/12/1999	P&L (piolt on disposal)	15000	1/7/1999	cash	420,000
		555,000			555,000

Total installment paid up to 1/7/1999

For (KQ) = 6 X 21800

= 130,800

For (KV) = 28000 X 12 = 336,000
24-(6+7)=11 Months

Installment due = 11 x 21800

= 239800

= 239800 – 190,000

= 49800

3. J. York was acquiring two cars under hire purchase agreements details of which are as follows.

Registration number JY 1 JY2

Date of purchase	31 June 20 x 6	30 Nov 20 x6
Cash price	£ 18,000	£ 24,000
Deposit	£ 3120	£ 4800
Interest (deemed to accrue every		
Over the period of the agreement)	£ 1920	£ 2400

Both agreements provided for payment to be made in 24 monthly installment commencing on the last day of the month following purchase.

On 1 September 20 x 7, vehicle Jy 1 becomes a total loss. In full settlement on

30 September 20 x7

1. An insurance co. paid 12500 under a comprehensive policy.
2. The hire purchase company accepted 6000 for the termination of the agreement.

   The firm prepared accounts annually to 31 Dec and provided depreciation on a straight line basis at a rate of 20 percent per Annam for motor, apportioned as from the date of purchase and up to the date of disposal.

All installments were paid on due dates

The balance on the hire purchase company account in respect of vehicle Jy 1 is to be written off

You are required to record these transactions in the following accounts, carrying down the balance as on 31 Dec 20 x 2

1. Motor vehicle
2. Depreciation

3. Hire purchase company
4. Assets disposal

Solution	**Jy 1**	**Jy2**
Cost price	18000	24000
Less: deposit	3,120	4800
	14880	19200
Add: H.P Interest	1920	2400
Total installment payable	16800	21600
	16800	21600
	24	24
Monthly installment paid	700	900
Total interest payable	1920	2400
	24	24
Monthly interest payable	= 80	= 100

DR MOTOR VEHICLE ACCOUNT CR

31.12.2006	H.P company	18,000	31.12.2006	Balance c/d	42,000
30.10.2006	H.P company	24,000			
		42,000			42,000
1.1.2007	Balance b/d	42,000	1/9/2007	M.V (Disposal)	18,000
			31.12.2007	Balance c/d	24,000
		42,000			42,000

Total installment paid for 2006 (4200 + 900) = 5100

JY1 30/6/2006 - 31/12/2006 JY2 31.11.2006 - 31.12.2006

6 x 700 = 4200 900 x 1 = 900

DR HIRE PURCHASE COMPANY (VENDOR) ACCOUNT CR

31.5.2006	cash(deposit)	3120	31.5.2006	Motor vehicle	18,000
30/10/2006	cash(deposit)	4800	30.10.2006	Motor vehicle	24,000
31.12.2006	cash(installment)	5100	31.5.2006	H.P interest suspense	1920
31.12.2006	Balance c/d	33,300	30.10.2006	H.P interest suspense.	2400
		46,320			46320

			1.1.2007	Balance b/d	33,300
20/9/2007	cash(for J1)	6000			
20/9/2007	cash(for J1)	5600			
20/9/2007	cash(instal. for J2)	10800			
20/9/2007	H.P interest	1000			
31.9.2007	Balance c/d	9900			
		33,300			33,300
			1.1.2008	Balance b/d	9900

Total installment paid up 1/9/2007

JY1 = 700 x 8 = 5600

JY2 = 900 x 12= 10800

Installment due = 24 – (6+8) = 10

= 700 x 10 = 7000

= 7000 – 6000

= 1000

DR MOTOR VEHICLE DEPRECIATION ACCOUNT CR

31.12.2006	Balance c/d	84,000	31/12/2006	P & L	84000
		84000			84000
1.08.2007	Disposal	5300	1.1.2007	Balance b/d	84000
31.12.2007	Balance c/d	78700			
		84000			84000
			1.1.2008	Balance b/d	78700

DR DISPOSAL ACCOUNT CR

31.5.2006	Motor vehicle	18,000		M/vehicle prov.	
				cash	12500
				P&L	5500
		18000			18000

DR HIRE PURCHASE INTEREST SUSPENSE ACCOUNT CR

31.5.2006	H.P company	1920	31.12.2006	P & L	580
30.10.2006	H.P company	2400	31.12.2006	Balance c/d	3740

		4320			4320
1.1.2007	Balance b/d	3740		H.P company (discount)	1000
			31.12.2007	P & L (JY1)	440
			31.12.2007	P & L (JY2)	1200
			31.12.2007	Balance c/d	1100
		3740			3740
1.1.2008	Balance b/d	1100			

Interest payable (Total)

JY1 = 80x 6 = 480

JY2 = 100 x 1 = 100

580

JY1 P& L

31/6 – 31/12 = 6 months

24 - 6 = 18

18 x 80 = 1440

IN SELLER'S BOOKS

Goods can be categorized into two major categories

1. Large items
2. Small items

Large items

These are the one which business buyers treat as fixed assets. In this case the amounts involved are substantial and transactions are relatively infrequent. Therefore the supplier is able to identify transactions surrounding each class of goods under hire purchase will ease. That is, the supplier can spread the gross profit and hire purchase interest over the hire purchase contract without much difficulty.

The hire purchase selling is made up of the following elements;

- Cost price plus gross profit giving the cash selling price.
- Cash selling price plus the hire purchase interest giving hire purchase selling price.
- H.P selling price = cost price + gross profit + hire purchase interest.

Accounting methods

Two alternative methods exist

METHOD A

Accounting entries

Dr H.P customer (debtor A/C)
Cr. H.P sales A/C

with cash selling price

Dr H.P. Customer A/C
Cr H.P interest received A/C

with proportion of H.P interest when the installment is due

Dr cash / bank A/C
Cr H.P customer A/C

With deposit + installments received

N.B

The balance on the H.P customer A/C at the end of the period, represents the cash sales price not yet due or received. Still at the end of the period, the following entries will be made.

Hr. H.P Trading A/C
General A/C

With cost of goods sold on hire purchase

Dr H.P. sales A/C
Dr H.P interest received A/C
Cr H.P Trading A/C

with transfer of balance on H.P sales and H.P interest received

DR H.P TRADING ACCOUNT CR

cost of goods sold	xxx	H.P sales(cash sale price)	xxx
prov.for unrealized profit	xxx	H.P interest received	xxx
Gross profit	xxx		
	xxxx		xxxx

The provision for unrealized profit is raised to suspend the appropriate portion of the gross profit included in the selling price.

Formula: prov for unrealized profit =

Or

%, margin x balance on cash not yet due

Entry

Dr; H.P trading A/C

CR; prov for unrealized profit A/C

This provision needs recalculations, and the difference between the opening and closing balance shall be transferred to the H.P Trading A/C

N.B

The balancing figure on the H.P trading A/C shall represent pure gross profit and H.P interest earned during the period.

And the balance on the H.P customer A/C (if any) at the end of the period, will be include under current assets in the balance sheet as H.P customer yet due.

Method B. (HIRE PURCHASE SUSPENSE ACCOUNT)

1. DR H.P customer (debtor) A/C with the total H.P selling price.

   Cr H.P sales A/C with cash selling price

   Cr H.P interest suspense A/C with the total H.P interest

Dr cash / bank A/C
CR H.P customer A/C
with deposit + installment received

Dr H.P. interest suspense A/C
Cr H.P interest received A/C
with release of the appropriate portion of H.P
interest when the installments due.

N.B At the end of the period, the balance on the H.P customers A/C will represent H.P debtors owing but not yet due & shall be included under current assets in the balance sheet.

Still at the end of the period the following entries will be made.

Dr: H.P sales A/C
Dr: H.P interest received A/C
Cr: H.P Trading

with transfer of balance on H.P sales + H.P interest received to H.P Trading

Dr H.P Trading A/C
CR General trading A/C

with cost of goods sold on hire purchase

Dr H.P Trading A/C
CR provision for unrealized profit A/C

with the creation of the provision for unrealized profit

N.B

The balancing figure on the H.P Trading A/C shall represent pure gross profit and H.P interest earned during the period.

Example:

Bulwell aggregates ltd wish to expand their transport fleet and have purchases three heavy Lorries with a list price of Tshs 18000 each Robert Bulwell has negotiated hire purchase finance to fund this expansion, and the company has entered in a hire purchase agreement with grariby Garages Pluc 1 Jan 2001. The agreement states that Bulwell aggregates will pay a deposit of Tshs 9000 on 1 January 2001 and two annual installments of Tshs 24000 each on 31 Dec 2001, 2002 and a final installment of Tshs 20391, on 31 Dec 2003.

Interest is to be calculated at 25% on the balance outstanding on 1 Jan each year and paid on 31 Dec each year.

The depreciation policy of Bulwell Aggregates ltd is to write off the vehicles over a four year period using the straight line method and assuming a scrap value of shs1333 for each.

Required

1. Account for the above transaction in the books of Grariby Garages PLC, and showing the entries in the hire purchase trading account for the years 2001, 2002, 2003. This is the only hire purchase transaction and under taken by this company.

Solution

cash price; 3 x 18000	54000	
less; deposit	9000	45,000

Add; 1st year H.P interest 25/100 x 45000	11250	56,250
Deduct; 1st year installment paid	24000	32,250
Add; 2nd year H.P interest 25/100 x 32,250	8063	40,313
Deduct; 2nd year installment paid	24000	16,313
Add; 3rd year H.P interest 25/100 x 16313	4078	20,391
Deduct; 3rd & final installment paid	20391	
NIL		

DR H.P DEBTORS ACCOUNT (Bullwell Aggr Ltd) CR

1/1/2001	H.P sales	54000	1.1.01	cash	9000
	H.P interest received	11250	31.12.01	cash	24000
			31.12.01	Balance c/d	32,250
		62250			62250
1.1.02	Balance b/d	32250	31.12.02	cash	24,000
	H.P interest received	8062	31.12.02	Balance c/d	16313
		40313			40313
1.1.03	Balance b/d	16313	31.12.03	Cash	20,391
	H.P interest received	4078			
		20391			20391

DR SALE S ACCOUNT CR

31.12.01	H.P Trading	54000	1/1/2001	H.P Debtors	54000

		54,000			54,000

DR H.P TRADING ACCOUNT FOR YEAR ENDED 31.12.01 CR

cost of goods	42,000	sales	54000
Provision for unrealized profit	7167	H.P interest received	11250
Gross profit	16083		
	65250		65250

DR H.P TRADING ACCOUNT FOR THE YEAR ENDED 31.12.02 CR

Gross profit	11605	H.P interest received	8063
		Provision for unrealized	3542
	11605		11605

DR H.P TRADING ACCOUNT FIR THE YEAR ENDED 31.12.03 CR

Gross profit	4078	H.P interest received	4078

DR PROVISION FOR UNREALIZED PROFIT ACCOUNT CR

31.12.01	Balance c/d	7167	31.12.01	H.P Trading	7167
		7167			7167
31.11.02	H.P Trading	3542	1.1.2002	Balance b/d	7167
31.12.02	Balance c/d	3625			
		7167			7167
			1.01.2003	Balance c/d	3625

DR HIRE PURCHASE INTEREST RECEIVED ACCOUNT CR

31.12.01	H.P Trading	11250	31.12.01	H.P Debtor	11250
		11250			11250
31.12.02	H.P Trading	8063	31.12.02	H.P Debtor	8063
		8063			8063
31.12.03	H.P Trading	4078	31.12.03	H.P Debtor	4078
		4078			4078

Calculation for provision for unrealized profit

For 2001; Prov. For unrealized profit=	cash sales not due x gross profit/ Total cash sales
(32250 x 12000)/54000 = 7167	
For 2002;	
(16313x12000)/54,000=3625	

EXERCISE

Songambele transport company ltd acquired 2 new 30 tone at calculated units on 1st Jan 1990 for Tshs 258300, the vehicles were supplied and financed by Uvuruge ltd and the terms of H.P contract required a deposit of Tshs 60000 on delivery, followed by 3 installments on 31st Dec 1990, 1991 and 1992 of Tshs 66000, 66000 and Tshs 66300.

Required

Prepaid their appropriate A/C in the books of Uvuruge ltd to record the above transaction for each of the tree years

Solution

Cash price	180,000
Less: deposit	60,000
	120,000
Add: 1st yr H.P interest (30/100 x 170000)	36,000
	156,000
Deduct: 1st H.P installment	66,000
	90,000
Add: 2nd yr H.P interest 930/100 x 90000)	127,000
	117,000

Deduct: 2nd yr installment 66,000

51,000

Add: 3rd H.P interest (30/100 x 51000) 15,300

66,300

Deduct: 3rd installment 66,300

NIL

DR SONGAMBELE (Debtors) ACCOUNT CR

1.1.90	H.P sales	180,000	31.12.90	cash(Deposit)	60,000
	H.P interest received	36,000	31.12.90	cash(Deposit)	66,000
			31.12.90	Balance c/d	90,000
		216,000			216,000
1.1.91	Balance b/d	90,000	31.12.91	cash(installment)	66,000
31.12.91	H.P interest received	27,000	31.12.91	Balance c/d	51,000
		117,000			117,000
1.1.92	Balance b/d	51,000	31.12.92	cash(installment)	66,300
	H.P interest received	15,300			
		66,300			66,300

DR SALES ACCOUNT CR

31.12.90	H.P Trading	180,000	1.1.90	Debtors	180,000
		180,000			180,000

DR H.P INTEREST RECEIVED ACCOUNT CR

31.12.90	H.P Trading	36,000	31.12.90	Debtors	36,000
31.12.91	H.P Trading	27,000	31.12.91	Debtors	27,000
31.12.92	H.P Trading	15,300	31.12.92	Debtors	15,300

DR PROVISION FOR UNREALIZED PROFIT A/C CR

31.12.90	Balance c/d	30,000	31.12.90	H.P Trading	30,000
		30,000			30,000
31.12.91	H.P Trading	13,000	1.1.91	Balance b/d	30,000
31.12.91	Balance c/d	17,000			
		30,000			30,000
31.12.92	H.P Trading	15,300	1.1.92	Balance b/d	17,000
31.12.92	Balance c/d	1,700			
		17,000			17,000
			1.1.93	Balance b/d	1,700

DR H.P TRADING ACCOUNT FOR THE YEAR ENDED CR

31.12.90	cost of goods	120,000	31.12.90	sales	180,000
	Provision for unrealized profit	30,000		H.P Interest	36,000
	Gross profit	66,000			

		216,000			216,000

DR H.P TRADING ACCOUNT FOR THE YEAR 1991 CR

	Gross profit	40,000		H.P interest	27,000
				Provision for unrealized profit	13,000
		40,000			40,000

DR H.P TRADING ACCOUNT FOR THE YEAR 1991 CR

	Gross profit	32,300		H.P Interest	15,300
				Provision for unrealized	17,000
		32300			32300

EXERCISE

Chaubuyu deals in motor vehicle. He sells motor vehicle on hire purchase basic. He sold two motor vehicles to Manumanu on 1st July 1998 for Tshs 80000. The cash price of these vehicles was Tshs 6500000. The payment was to be made as under deposit Tshs 200000. 24 monthly installment of Tshs 25000 each payable on lost day of every month. The company recognizes profit on Hire purchase sales in the year of sales but hire purchase interest apportioned on time basis. The financial year of Chaubuyu ends on 31 Dec each year.

Required

Record this transaction in the books of Chaubuyu carrying down the balances as on 31st Dec 1998.

1. Hire purchase sales Account.
2. Hire purchases Debtors Account.
3. Hire purchases interest suspense Account.

Solution

H.P interest = total H.P price - cash price

= 800000 - 650000

= 150000

Monthly H.P. interest received = 150000 x 6

24

= 37,500

DR H.P DEBTORS ACCOUNT CR

1.7.98	H.P sales	650,000	31.12.98	cash(deposit)	200,000
31/12/98	H.P interest rec.	150,000	31.12.98	(installment) cash	150,000
			31.12.98	Balance c/d	450,000
		800,000			800,000
1.1.99	Balance b/d	450,000			

DR H.P SALES ACCOUNT CR

31.12.98	H.P Trading	650,000	1.7.98	Debtors	650,000
		650,000			650,000

DR H.P INTEREST SUSPENSE ACCOUNT CR

31.12.98	H.P Trading	37500	31.12.98	Debtor	150,000
31.12.98	Balance c/d	112500			
		150,000			150,000
			1.1.99	Balance b/d	112,500

SELLER'S BOOK:

2. **Small items**

In this case the amounts involved (per item) are relatively small and the volume of such item is likely to be large.

Therefore no attempt is made to calculate the gross profit and H.P interest received for the separate crediting to the H.P Trading A/C. No calculations are made for each individual contract instead calculations are based on the total of all transactions of a particular accounting period involving a particular class of items under hire purchase, implying that pure gross profit and H.P interest are combined into one figure. This combined figure there is apportioned over the hire purchase period.

Method of recording / accounting

Alternative method is in use:

1. Stock on hire method
2. provision for unrealized profit method

1. **Stock on hire method**

This method is so called due to the fact that goods on hire purchases in the customer's hands are regarded as stock out on hire purchase contract at east.

Accounting entries

Dr H.P debtors A/C
Cr H.P sales A/C
with the H.P selling price

Dr H.P cash/ bank A/C
CR. H.P debtors A/C
with deposit and installments received

N.B

At the end of accounting period, the balance on the H.P debtors A/C represents sums owing (debtors owing) but not yet due.

Still at the end of the period, the following entries will be made:-

Dr H.P trading A/C
CR General trading A/C } with cost of goods sold on H.P

Dr ;H.P sales A/C
CR; H.P trading A/C } With the equivalent amount of deposit installments received

H.P sales A/C the balance will be equal and opposite to that on H.P Debtor A/C.

H.P TRADING ACCOUNT

Cost of goods sold	xx	Deposit+ installment	xx
	stock on hire	xx	
	xxx		xxx

The stock on hire (at cost) is calculated by using the following formula:

Stock on hire (at cost) =

The amount will then be credited to the H.P trading A/C and then carried down as a debit on the very A/C.

N.B

The balancing figure on H.P trading A/C represents pure gross forfeit and H.P interest earned during the period.

Example:

A business commenced selling electrical goods on H.P on 1st Jan 1990. During the 1st year goods cost was Tshs 15300 were sold for Tshs 26500. Deposit and installments received amounted to Tshs 13060. Prepares the appropriate ledger A/C using the stock on hire.

2. Provision for unrealized profit method In this case provision is raised against gross profit included in the hire purchases debtors not yet due to reduce them to cost.

Dr: H.P Debtors A/C
CR: H.P Trading A/C } with the H.P selling price

Dr: cash / bank A/C
Cr: H.P Trading A/C } With deposit and installments received

The balance on the H.P Debtors A/C at the end of the period represents sums owing on H.P contacts but not due still at the end of the period the following entries will be made.

Dr: H.P Trading A/C
Cr: general Trading A/C

with the cost of goods sold on hire purchase

Dr ; H.P sales A/C
CR: H.P trading A/C

with the transfer of balance on H.P sales A/C to H.P Trading

The provision for unrealized profit is raised against the profit and calculated by using the following formula.

$$Provision\ of\ unrealized\ profit = \frac{Cash\ sales\ not\ due x Gross\ profit}{Total\ cash\ sales}$$

This provision needs recalculations each period. The difference between the opening and closing balance shall be transferred to the hire purchases trading A/C.

Entry (on creating the prov.) = Dr H.P Trading A/C

CR; Provision for unrealized profit A/C

N.B

The balancing figure on the H.P trading A/C will then represent "pure gross profit plus hire purchase interest earned during the period".

Examples

A business commenced selling electrical goods on H.P on 1st Jan 1990. During the 1st year goods cost was Tshs 15300 were sold for Tshs 26500. Deposit and installments received amounted to Tshs 13060. Prepare the appropriate ledger A/C using the provision for unrealized profit method.

DR H.P DEBTORS ACCOUNT CR

H.P sales	26500	cash(deposit + installments	13060
		Balance c/d	13440
	26500		26500
Balance b/d	13440		

DR H.P SALES ACCOUNT CR

H.P Trading	26500	H.P Debtors	26500
	26500		26500

DR H.P TRADING ACCOUNT FOR THE YEAR ENDED CR

cost of goods	15300	H.P sales	26,500
Provision for unrealized Profit	5680		
Gross profit	5520		
	26,500		26,500

$$Unrealized\ profit = \frac{\text{Debtor owing but not due} x \text{Gross}}{Total\ H.P\ Sales}$$

$$= \frac{13440x\ 11200}{26500}$$

= 5680/=

EXERCISE

R.J commenced business on 1st Jan 2006. He sells refrigerators all of one standard type on hire purchase terms. The total amount including interest payable for each refrigeration is 1 Tshs 300. Customers are required to pay

an initial deposit of Tshs 60, followed by eight quarterly installments of Tshs 30 each. The cost of each refrigerator to RJ is Tshs 200.

The following trial balance was extracted from RJ books as on 31 Dec 2006.

TRIAL BALANCE AS AT 31 DEC 2006

Capital		100,000
Fixed assets	10,000	
Drawings	4000	
Bank overdraft		19,600
creditors		16,600
purchases	180,000	
cash collected from customers		76500
Bank interest	400	
wages and salaries	12800	
General expenses	5500	
	212,700	212,700

850 machines were sold on hire purchases terms during 2006. The annual accounts are prepared on the basis of taking credit for profit and loss Account for the year 2006 and balance sheet as on 31st Dec 2006.

Ignore depreciation of fixed assets.

Solution:

Deposit = 60 x 850 = 15000

Installment = 30 x 850 = 25500

76,500

Cost of goods = 200 x 850

= 170,000

Closing stock = 180000 = 900

200

900 -850= 50

50 x 200 = 10000

Selling price = 300 x 850

= 255000

DR HIRE PURCHASE DEBTOR ACCOUNT CR

H.P sales	255,000	cash(Deposit)	76500
		Balance c/d	178,500
	255,000		255,000
Balance b/d	178,500		

DR HIRE PURCHASE SALES ACCOUNT CR

H.P Trading	255,000	H.P Debtor	255,000
	255,000		255,000

DR HIRE PURCHASE TRADING A/C FOR THE YEAR ENDED CR

Purchases	180,000	H.P sales	255,000
less; closing stock	10,000		
cost of goods sold	170,000		
provision for unrealized Profit	59,500		
Gross profit c/d	25,500		
	255,000		255,000

DR PROFIT AND LOSS ACCOUNT

Bank rate	400	Gross profit b/d	25,500
Wages and salaries	12800		
General expenses	5500		
Net profit	6800		
	25,500		25,500

BALANCE SHEET AS AT 31ST DECEMBER 2006

capital	100,00		Fixed Assets		10,000
Add ; Net profit	6800				
less; Drawing	4000		Current Assets		
		102800	stock		10,000
Current liabilities			Debtors Less: Prov.	178,500 59,500	199,000
creditors		16,600			
Bank overdraft		19600			
		139,000			139,000

EXERCISE

P.Q. ltd commenced business on 1st Jan 1997. They sell TV sets, all of one standard type on hire purchase terms. The hire purchases price (including interest) is shs 20000 for each TV set. The customers are required to pay shs 5000 an initial deposit, followed by twelve monthly installments of shs 1250 each. The cost of each TV sets PQ ltd is shs 14000.

The following trial balance was extracted from PQ ltd on dec 1997

	DEBIT	CREDIT
Ordinary share capital		1,500,000
Fixed Assets	125,000	

Purchases	5,600,000	
cash collected from customers		4,500,000
wages and salaries	150,000	
General expenses	50,000	
Bank balance	255,000	
creditors		180,000
	6,180,000	6,180,000

400 TV sets were purchased during the year, but 260 tv sets were sold on hire purchase basis.

The annual accounts are prepared on the basis of taking credit for profit (including interest) in proportion to cash collected from customers.

Required:-

Prepare the hire purchase trading account and profit and loss A/C for year 1997 and a balance sheet as on 31st Dec 1997.

Solution:

Selling price = 20000 x 360

= 7,200,000

Closing stock = 14000 x (400 -360)

= 560,000

DR H.P DEBTORS ACCOUNT CR

H.P sales	7,200,000	cash collected	4,500,000

		Balance c/d	2,700,000
	7,200,000		7,200,000
Balance b/d	2,700,000		

DR H.P SALES ACCOUNT CR

H.P Trading	7,200,000	H.P Debtors	7,200,000
	7,200,000		7,200,000

DR H.P TRADING ACCOUNT AS AT 31ST DEC.1997 CR

		sales	7,200,000
purchases	5,600,000		
less closing stock	560,000		
cost of goods	5,040,000		
provision for unrealized profit	810,000		
Gross profit c/d	1,350,000		
	7,200,000		7,200,000

DR PROFIT AND LOSS ACCOUNT CR

wages and salaries	150,000	Gross profit b/d	1,350,000
General expenses	50,000		

Net profit	1,150,000		
	1,350,000		1,350,000

BALANCE SHEET AS AT 31ST DECEMBER 1997

capital	1,500,000		Fixed Assets		125,000
Add; Net profit	1,150,000	2,650,000	**Current Assets**		
			stock		560,000
current liabilities					
Creditors		180,000	Debtors Less: Prov	2,700,000 810,000	1,890,000
		2,830,000			2,830,000

REPOSSESSION

Sometimes the buyer of goods on hire may refuse to continue paying the installments. The seller may be permitted (having complied with some legal equipments) to repossess the goods. Both the deposit and installments received so far shall be retained by the seller.

Preferably, the transactions relating to the repossessed good are segregated from those transaction on hire purchases contract in the normal way hence the need to prepare repossession A/C in the seller books.

Entries

DR; Repossession A/c
CR; H.P Debtors A/c

with outstanding installments on reposed goods

DR; H.P interest suspense A/c
CR; Repossession A/c

with unearned interest on repossessed goods

DR; Repossession A/c
CR; Trade profit & loss A/c

with profit on repossession

- The reserve entry made for the loss.

Dr; H.P Sales A/C
Cr; H.P. Debtors A/C

with H.P selling price of the repossessed goods

Dr H.P Bank A/C
Cr; H.P. Debtors A/C

with deposit installed received on repossessed goods

1. The valuation figure on the repossessed stock shall be credited to the repossession A/C and then being carried down as a debit ball on that A/C.

Dr repossession A/C
Cr H.P. Trading A/C

with the cost of reposed goods

DR REPOSSESSION ACCOUNT CR

Cost	xx	Cash received	xx
		Stock	
	xxx		xxx

Example

Kitiorition commenced business on 1st April 1997. During the year ended 31st march 1998 purchases amounted to sh 10800 and ordinary sales to Tshs 12400. In addition the following sales were made under hire purchase agreements:-

Article	Cost	sale price	Deposit paid	Monthly instal.	no. of instal.paid in year
Radiogram	120	180	20	20 of Tshs.8	8
Television	160	240	24	12 of Tshs.18	2
Refrigerator	140	200	20	18of Tshs.10	4

Installments on the refrigerator could not be receipt and it was returned on 26 March and was unsold at 31 March. Stock in trade on 31st march excluding the returned refrigerator was valued at Tshs 1400.

You are required to;-

Prepare the H.P trading sales A/C, H.P. Debtors A/C Repossession A/C, H.P trading A/C and general trading A/C. Use stock on hire method.

Total cash collected; Radio = 20 + (8 x 8) =
84

$$Value\ of\ repossessed\ stock = \frac{\text{Outstand}}{\text{H. P Sal}}$$

$$= \frac{140x140}{200}$$

= 98

T .V = 24 + (2 x 18) = 60

Refrigerator. = 20 +(4 x 10) = 60

84+60+60 = 204

Outstanding Installment =(18-4) xTshs 10=140

DR H.P SALES ACCOUNT CR

H.P Trading(204 - 60)	144	H.P Debtors	
H.P sales	200		
Balance c/d	276		
	620		620

DR H.P DEBTORS ACCOUNT CR

H.P sales	620	cash	204
Repossession	60	H.P sales	200
		Balance c/d	276
	680		680
Balance c/d	276		

DR REPOSSESSION ACCOUNT CR

H.P Trading	140	H.P Debtors	60
H.P Trading(P & L)	18	stock c/d	98

	158		158
stock b/d	98		

DR H.P TRADING ACCOUNT CR

General Trading(cost)	420	Repossession	140
Gross profit	66	H.P sales(cash collect)	144
		Profit on repossession	18
		stock on hire	184
	486		486

DR GENERAL TRADING ACCOUNT CR

purchase	10800	sales	12400
		H.P Trading	420
Gross profit	3420	closing stock	1400
	14,220		14,220

Exercise

Zamaradi ltd began business on 1st Jan 1995 for the year ended 31st Dec 1999 purchase of cars amounted to sh 16200. Cash sales of ware shs 200000, hire purchase sales were:-

Type of car	cost price	sale price	Deposit rec.	Month instal.	instal.paid in year
Torgue	3000	4000	400	12 of Tshs.300	7
Helie	2000	2800	400	15 of Tshs.160	4
Planet	2500	3500	500	20 of Tshs.150	8
TOTAL	7500	10300			

The hire purchase of the planet returned the car on 20 Dec 1995 as he was unable to pay further installments.

Stock of car excluding repossessed car at 31st Dec 1995 were valued at Tshs 20000

Required to show:

1. The hire purchase trading A/C
2. The general trading A/C for the year ended 31 Dec 95

Solution

Value of repossess stock = 1800 x 2500 = 1,286

3600

Cash collected

Torgue = 400 + 7 x 300 = 2,500

Helie = 400 + 160 x 4 = 1,040

Planet = 500 + 150 x 8 = 1700

= 5240

Stock on hire

Tongue = 1600 x 3000 = 1125

4000

Helie = x 2000 = 1257

2800 2382

DR H.P TRADING ACCOUNT CR

cost of goods	7500	cash collected	5240
	stock on repossess	1286	
	stock on hire	2382	
	8908		8908

DR GENERAL TRADING ACCOUNT CR

purchases	162,000	sales	200,000
		H.P Trading	7500
		closing stock	20,000
	227,500		227,500

EXERCISE

H. ltd deal in refrigerators. They sell refrigerators on cash basis and hire purchase basis. During the year ending 31st Dec 1998 they made the following transaction.

Purchases 500,000

Ordinary sale	550,000
H.P Sale	150,000
Cash received from H.P sales	81,000
Cost of goods sold on Hire purchase	100000

One refrigerators was repossessed due to non – payment of installments. The outstanding of installment of this refrigerator amounted to Tshs 3000 H.P. sale of this refrigerators was Tshs 7000 and cost Tshs 6000. Cash received against the refrigerator and H.P sale are included in the above figures. The company follows the stock system. There was no closing stock except repossessed refrigerator.

Required:

Prepare the following accounts for the year ending 31st Dec

1. H.P Trading A/C
2. General trading A/C
3. Memorandum H.P. Debtors A/C

N.B: Stock system means using stock on hire purchase.

Solution

Stock repossession =

= 3000 x 6000

9000

= 2000

Stock on hire (cost = 66000 x (100,000 - 6000)

150,000 - 9000

= 66000 x 94000

141,000 = 44000

DR H.P TRADING ACCOUNT CR

cost of goods	100,000	cash collected	81,000
Gross profit	27,000	stock on repossession	2000
		stock on hire	44,000
	127,000		127,000

DR GENERAL TRADING ACCOUNT CR

purchases	500,000	sales	550,000
Gross profit	150,000	H.P Trading	100,000
	650,000		650,000

DR MEMORANDUM H.P DEBTORS ACCOUNT CR

H.P sales	150,000	cash collected	81,000
		Outstanding install.	3000
		Balance c/d	66,000
	150,000		150,000

EXERCISE.

On 1st Jan 1998 Mamujee acquired furniture on the hire purchase system from Babewana ltd, agreeing to pay four semiannual installments of Tshs 1600 each commencing on 30th June 1998. The cash price of the items was Tshs 6020 and interest of 5% per annum was chargeable.

On 30th Sept 1998, Mamujee expressed his inability to continue and Babewana ltd seized the property. Ti was agreed that Mamujee would pay

the due proportion of the installment up to the date of seizure, and also a further sum of shs 400 towards depreciation. At the time of repossession, Babewana ltd valued the furniture at sh 3000

The company after incurring Tshs 400 towards repairs of the furniture sold the items for Tshs 3600 on 1st October 1998.

Prepare the ledger accounts in the books of the vendor and the purchases presuming that the purchases charges depreciation at 10% per annum.

Solution:

Workings

Cash price	6020	
Add: ½ yr H.P interest 5/100 x 6020 x ½		151
	6171	
Deduct: ½ yr installment	1600	
	4571	
Add: ¼ yr H.P interest 5/100 x 4571 x ¼	57	
	4628	
Deduct install. + Dr (800 + 400)	1200	
	3428	

VENDOR'S BOOKS.

DR MAMUJEE ACCOUNT CR

1.1.98	H.P sales	6020	30.6.98	cash	1600
30.6.98	H.P interest rec.	151	30.9.98	Cash (Dep + instal.)	1200
30.9.98	H.P interest rec.	57	30.9.98	loss on repossession to P&L	428
			30.9.98	Repossession	3000
		6228			6228

DR H.P SALES CR

	H.P Trading	6020	1.1.98	Mamujee	6020

DR H.P INTEREST RECEIVED ACCOUNT CR

30.09.1998	P&L	208	30.6.98	Mamujee	151
			30.9.98	Mamujee	57
		208			208

DR REPOSSESSION ACCOUNT CR

30.9.98	Mamujee	3000	15.10.98	cash(sale proceeds)	3600
	cash(repair)	400			
	profit on sale to P & L	200			
		3600			3600

P & L ACCOUNT

Mamujee	428	profit on sale	200
		H.P interest received	208
	428		428

Purchases book's; Mamujee

DR FURNITURE ACCOUNT CR

1.1.98	Babewana ltd	6020	30.9.98	Depr(6020x10/100x9/12)	452
			30.9.98	Babewana	5568
		6020			6020

DR BABEWANA LTD ACCOUNT CR

30.6.98	cash	1600	1.1.98	furniture	6020
30.9.98	cash	1200	30.6.98	H.P interest	151
30.9.98	furniture	5568	30.9.98	H.P interest	57
				Loss on repossession(p&L)	2140
		8368			8368

DR H.P INTEREST EXPENSE ACCOUNT CR

30.6.98	Babewana ltd	151		P & L	208
30.9.98	Babewana ltd	57			
		208			208

Cash price not given;-

In this case the cash price and H.P interest will be calculated by working backward.

Example

Kasum industries ltd acquired plant, delivered on Jan 1st 1995 on the following hire purchase terms.

1. An initial payment of shs 40000 payable on or before delivery and.
2. For half year payment of shs 30000 each commencing from June 30th 1995. In arriving at these term, the plant manufacturers computer interest at 6% per annum resume industries ltd provides depreciation at the rate of 8% on cost.

You're required to show:-

The A/C in the books of tea Kasum industries ltd for the year ended 31st Dec 1995 and 31st Dec 1996 necessary to record the above transaction.

Year ended	Amount due at the end of year	instal. Paid	Total Amount due	H.p interest	Amount due beginning of the year
31/12/96	-	60,000	60,000	$\frac{60,000 \times \frac{6}{106}}{3396}$	(60,000-3396)=56604
31/12/95	56604	60,000	116604	$\frac{116,604 \times \frac{6}{106}}{6600}$	116,604-6,600=110,004
		40,000			110004
					150004

Cash price	150004
Less: deposit	40000
	110004
Add H.P interest 100 x 11004	6600
	116604
Deduct: installment	60000
	56604
Add: H.P interest 6/100 x 56604	3396

60000

Deduct: installment 60000

NIL

DR **PLANT ACCOUNT** CR

1.1.95	H.P company	150004	31.12.95	Balance c/d	150004
1.1.96	Balance b/d	150004	31.12.96	Balance c/d	150004
1.1.97	Balance b/d	150004			

DR **H.P COMPANY ACCOUNT** **CR**

31.12.95	cash(Deposit)	40,000	31.12.95	Plant	150004
31.12.95	cash(installment)	60,000	31.12.95	H.P interest	6600
31.12.95	Balance c/d	56604			
		156,604			156,604
31.12.96	cash(installment)	60,000	1.1.96	Balance b/d	56,604
			31.12.96	H.P interest	3396
		60,000			60,000

DR **H.P INTEREST ACCOUNT** **CR**

31.12.96	H.P company	6600	31.12.95	P & L	6600

31.12.96	H.P company	3396	31.12.96	P & L	3396

EXERCISE

1. Chaumbea co. Forward the piano to Bonge la Mshamba on system, the cost being shs 1000 and shs 2000 selling price. Payable in fifty monthly in stalemates of shs 40 each commencing from 31st aug. The sale take place on 1st aug 1991 the installment are regular paid. Accounts are drawn up on 31st Dec . on 1st October 1991 a similar sale is made to Mapua the cost price being shs 780, selling price shs 1040 payable in weekly installments of shs 20 commencing from the installment are paid regular. Show ledger a/c to the books of Chaumbea.

1. H.P Sales A/C
2. H.p memorandum A/C
3. H.p. trading A/C

2) Damson ltd had purchases the machinery on hire purchase system from Hindu Mandali machinery tld. The terms are that they would pay shs 20000 down on 1st Jan 1993 and five annually installments of shs 11000 each commencing from 31st Jan 1994. They charged depreciation of machinery rate of 15% pe annum at diminishing balance system.

Hindu Mandal machinery ltd had charged interest a rate ate of 10%. Show the machinery A/C, and Hindu Mandal machinery ltd A/C to record the above transaction in books of **Damson.** Still the installment are paid off, Damson accounting year ends on 31st Dec.

YEAR ENDED	AMOUNT DUE AT THE END OF THE YEAR	INSTALLMENT	AMOUNT DUE AT THE END OF YEAR	H.P INTEREST	THE AMOUNT DUE AT THE BEGINNING
31.12.97	-	11,000	11,000	$11000 \times \frac{10}{110} = 1000$	10,000
31.12.96	10,000	11,000	21,000	$21000 \times \frac{10}{110} = 1909$	19091
31.12.95	19091	11,000	30091	$30091 \times \frac{10}{110} = 2736$	27355
31.12.94	27355	11000	38355	$38355 \times \frac{10}{110} = 3487$	34868
31.12.93	34868	11000	45868	$45868 \times \frac{10}{110} = 4170$	41698
		20000			61,698

Cash price	61698
Less: deposit	20000
	41698
Add: H.P. Interest 10/100 x 41698	4169.8
	45867.8
Deduct: installment	11000
	34867.8
Add: H.P. interest 10/100 x 34867.8	3486.78

38354.58

Deduct; 2nd year installment 11000

27354.58

Working

31/8/91 provision for unrealized profit x 1,260 = 1,060

Cash collected = 5 x 40 = 200

1/10/91 ---31/12/91 (14 weeks)

Cash collected = 14 x 20 = 280

200 + 280 = 480

DR H.P MEMORANDUM DEBTORS ACCOUNT CR

H.P sales	3,040	cash collected	480
		Balance c/d	2,560
	3,040		3,040

DR H.P TRADING ACCOUNT CR

cost of goods	1780	H.P sales	3040
prov.for unrealized profit	1061		
Gross profit	199		
	3040		3040

EXERCISE

On 1st Jan 1994 five trucks were purchase by Bonyoa on hire purchase terms. The cash price of each truck is shs 110,000. The payment was to be made has follows

10% of the cash price down

25% of the cash price at the end of each of the four installment half year

The payment due on 31st dec 1994 would not be made; the vendor allows Bonyoa to keep three trucks on the condition that the value of the other two tracks would be adjusted against the amount due the trucks being value at cost less 25% depreciation. This vendors or spend 1200 on parallel over haul the trucks and sell them for190, 000. Bonyoa charges repreciation ion at 15% p.a on original cost. And closing his books on 30 June each year.

You're required to open necessary ledger in the books of both parties.

Solution:

Cash price for 5 tracks = 110,000 x 5 = 550,000

Down payment = 10/100 x 550,000 = 55,000

Installment paid = 25/100 x 55,000

= 220,000 – 55,000 = 165,000/=

Total H.P. Interest installment + deposit) - cash price

= [(137,500 x 4) + 55000)]- 550000

= 55,000

H.P. interest

Sum of the digit method

1 4 = 4/10 x 55,000 = 22,000

2 3 = 3/10 x 55,000 = 16,500

3 2 = 2/10 x 55,000 = 11,000

4 1/10 = 1/10 x 55,000 = 5,500

DR REPOSSESSION ACCOUNT CR

H.P Debtor	165,000	sales	190,000
overhauling	12,000		
profit on sales (P &L)	13,000		
	190,000		190,000

DR H.P DEBTORS ACCOUNT CR

H.P sales	550,000	cash(Deposit)	55,000
H.p interest	22,000	cash(installment)	137500
H.p interest	16,500	Repossession	165,000
		Balance c/d	231,000
	588,500		588,500

Buyer's book

DR TRUCK'S ACCOUNT CR

1.1.94	Cash(Deposit)	550,000	30.6.94	Depreciation	41250
			30.6.94	Balance c/d	508750

		550,000			550,000
31.12.94	Balance b/d	508750	31.12.94	Depreciation	41250
			31.12.94	Repossession	165,000
			31.12.94	P & L	22,000
			31.12.94	Balance c/d	280,500
		508750			508,750
1.01.1995	Balance c/d	250,500			

DR H.P COMPANY ACCOUNTS CR

30.6.94	Cash(Deposit)	55,000	30.6.94	Truck	550,000
30.6.94	Cash Installment	137500	30.6.94	H.P interest	22,000
	Balance c/d	379,500			
		572,000			572,000
	Repossession	165,000	31.12.94	Balance c/d	379,500
			31.12.94	H.P interest	16500
	Balance c/d	231,000			
		396,000			396,000

DR H.P DEBTORS ACCOUNT CR

1.1.94	H.P sales	550,000	1.1.94	cash(Deposit)	55,000
30.6	H.P interest	22,000	30.6	cash(installment)	137,500
			30.6	Balance c/d	379500
		572,000			572,000
1.7.1994	Balance b/d	379,500	31.12.1994	Goods repossessed	165,000
31.12.1994	H.P interest	16,500			231,000
		396,000			396,000
1.1.95	Balance b/d	231,000			

COST ACCOUNTING

COST ACCOUNTING

- concept
- Objectives and importance of cost accounting
- Differences btw cost accounting and financial accounting
- Cost classification
- Breakeven point (B.E.P)
- Cost for manufacturing enterprise

Simple cash budget

- Concept of cash budget
- Importance of preparing cash budget
- Compute and prepare a simple cash budget for a business

CONCEPT OF COST

This refers to the value of economic resources used as the result of production of any commodity

For example;

100'000/= spent for producing 100 units of mobile phones. That amount of money used is known as cost.

Cost accounting

- It is concerned with the ascertainment and allocation of cost
- In order to produce products or provide any services, some amount of money are spent by an organization. This amount is regarded as cost
- This cost must be recorded properly and charged to the relevant jobs/ activities
- This cost are presented to management for decision making and evaluating a performance of an organization
- The main objective of cost accounting are to establish budget and standard cost and to analyze the differences between budgeted and actual performance.

Objectives of cost accounting

i.) Cost ascertainment

-The cost of producing products/ providing services must be ascertain accurately. This cost consist of raw materials, labor

-The cost must be kept at minimum possible level

-The detailed information about cost help the management to make some decisions and to evaluate the performance of an organization.

ii.) Disclosure of wastes

-The cost incurred for the production of any commodity can be determined in advance in view of the past experience.

That is; cost accounting is an important aid to disclose waste

iii.) Decision making

-Cost accounting provides necessary information to the management for making decision

iv.) Cost control

-When we talk about cost control we mean material cost, labor cost and other must be obtained at desirable levels. Cost accounting principles are used to eliminate unnecessary cost.

v.)Planning

-The management prepare plans for the expansion of business activities.

-The installation of new machine and plant is needed to increase t he production capacity of manufacturing concern in view of greater demand of its products. Thus the past experience and cost data are used to prepare.

vi.)Measurement of efficiency

-Cost data are used to measure the efficiency of a company

-if there are various department/division of business enterprises then it is important to determine the relative performance of this department.

vii.)Setting selling price

-It is more advisable that a business concern should ascertain its cost and then add its profit into cost of sales to obtain selling price.

-The cost data are also helpful to set a selling price.

COST CLASSIFICATION

Cost may be classified under three categories;

i.) Fixed and variable cost

ii.) Direct and indirect cost

iii.) Cost classification by function

FIXED AND VARIABLE COST. (FIXED COST)

FIXED COST:

Is the cost which remains the same at various level of output. This cost does not change with the change in output i.e. Remain the same even at Zero level of output

-This cost incurred mostly in periodic basis

e.g.; - Rent of premises and salaries of permanent employees

VARIABLE COST

Is the cost which changes with the level of production or output.

When production increases, variable cost also increases

Example of variable cost is raw materials, direct wages and other related.

DIRECT AND INDIRECT COST.

DIRECT COST

Is that cost which can be identified on the production of some 'specific' products. Example of direct cost is raw material and labor cost. Since they

can be charged and identified to the production of some specific outputs, this is why we say raw materials and labour cost are good examples of direct cost.
Cost associated directly with the production of goods/outputs.

INDIRECT COST.

Is the cost which cannot be identified to the production of some specific products or outputs. Examples of this are; water charges, interest rate, indirect

Materials, communication charges etc.

Cost classification by function

Cost may be classified by its functions or activities such as that or consist of production cost, administration cost and selling and distribution cost

-Production cost consists of raw materials, labor, rent of factories etc.

-Administration cost involves office cost such as office rent, postage, telephone, electricity etc

-Selling and distribution cost; this consist of cost which are incurred to promote the selling of goods and delivery these goods to the customers E.g. Advertisement, salesmen commission, depreciation of delivery van, carriage outward, carriage inward.

ANALYSIS OF COST

The cost (total) incurred by the manufacturing firm may be analyzed by cost accountant as under such that;

-Direct raw materials (D.R.M)	xx
-Direct labor/Direct wages	xx
-Direct any other cost	xx
Total direct cost = prime cost	xx

Add;

Production overhead (manufacturing overhead)

- Indirect wages xx
- Indirect factory wages xx xx

Manufacturing/production cost xxx

In case of profit or loss

COST STATEMENT FOR THE YEAR ENDED

Total Direct Cost		
Raw materials (R.M)		xx
Direct labor (D.L)		xx
Prime cost of production		xxx
Add ; Manufacturing over head		
Factory rent	xx	
Power	xx	
Supervision expenses	xx	xxx
Production cost of goods produced		xxx
Add ;Administration cost and distribution		
Office rent	xx	
Depreciation office	xx	
Promotion	xx	
Advertisement	xx	
Carriage outward	xx	xxx
Cost of goods sold		xxx
Add ; Profit margin		xx
Total sales		xxx

Selling price â”€ total costs = profit/loss on production

-Direct raw materials involves cost of raw materials, opening stock of raw materials, closing stock of raw materials, carriage inwards of raw materials etc.

ILLUSTRATION 1

Prepare a cost statement from the following information;

Raw material	300,000
Direct labor	80,000
Factory rent	15,000
Supervision salary	20,000
Administration expenses	40,000
Selling and distribution expenses	15,000

NOTE; Profit margin is 50% on cost, calculate selling price.

COST STATEMENT FOR THE YEAR ENDED

Total Direct Cost		
Raw material		300,
Direct labor		80,
PRIME COST		380,
Total M.O.H (Total Manufacturing overhead)		
Factory rent	15,000	
Supervision salary	20,000	35,
Production cost of goods produced		415,
Administration expenses	40,000	

Selling and distribution	15,000	55,0
Cost of goods sold		470,
Add 50% margin		235,
Selling price		705,

Since profit = cost x 50%

= 470,000 x 50%

= 235,000

Cost of goods sold =	470,000
Add; profit margin =	235,000
Selling price	705,000

ILLUSTRATION 2

From the following information prepare a cost statement

R.M	80,000
D.L	35,000
Factory rent	5,000
Power	3,000
Indirect wages	2,000
Administration expenses	4,000
Selling and distribution expenses	3,000

Profit is 25% on sales

COST STATEMENT FOR THE YEAR ENDED

materials	80,000	
Direct labor	35,000	
PRIME COST		
MOH / FOH		
Factory rent	5,000	
Power	3,000	
Indirect wages	2,000	
Production cost of goods produced		
Distribution expenses	4,000	
Selling &distribution expenses	3,000	
Cost of goods sold		1
Add; profit margin		
Total sales		1

NOTE; 1.WIP- Is the cost of those items which remain incomplete at the end of the specific period

2. These are semi-finished goods

3. WIP may be valued at prime cost or factory cost

ILLUSTRATION 3

From the following information prepare a cost statement

Stock on 1st. 1 2006 R.M	45,000
W.I.P	22,000
Stock on 31st.12.2006 R.M	65,000
W.I.P	19,000
Purchases of R.M	670,000

Carriage inward	25,000
Returns of R.M	15,000
Direct wages	280,000
Factory rent	60,000
Factory power	48,000
Depreciation of plant	15,000
Supervision salary (factory)	55,000
Office salaries	70,000
Office expenses	12,000
Depreciation of office equipment	5,000
Salesman salaries	68,000
Delivery van expenses	27,000
Depreciation of delivery van	18,000
Advertisement	12,000

NOTE

i.) If there is office salary and supervisor's salary here normally supervisor's salary is for factory

ii.) If the question is silent then the amount of W.I.P is very little compare to R.M

or purchase of R.M then it means it is in the final stage so should be finalized in the factory overhead level

iii.) But another time you may be informed if W.I.P is in prime level (early stage) or factory overhead level (final stage)

SOLUTION FOR ILLUSTRATION 3

COST STATEMENT FOR THE YEAR ENDED 31.12.2006

Opening stock of (R.M)	
Add : Purchases of (R.M)	670,000
Add: Carriage inwards	25,000
	695,000
Less: Returns outward (R.M)	15,000
Cost of R.M available for use	
Less : Closing stock of (R.M)	
Cost of R.M used/consumed	
Add : Direct wages	
Prime cost	
Add :Manufacturing over head (M.O.H)	
Factory Rent	60,000
Factory power	48,000
Supervision salary	55,000
Depreciation of plant	15,000
Add : W.I.P (opening)	
Less : W.I.P (closing)	
PRODUCTION COST	

ILLUSTRATION 4.

ABC manufacturing co provides the following information for the month of October 2011

1st October 2011.

Raw materials	40,000
W.I.P	12,000

Finished goods	20,000
Stock on 31st October 2012	
Raw materials	35,000
Work in progress	17,000
Finished goods	23,000
Purchases of raw materials	250,000
Factory wages	80,000
Salaries of supervisors	30,000
Factory rent	10,000
Factory power	5,000
Sundry factory expenses	15,000
Office salary	13,000
Sundry office expenses	7,000
Salesmen salary	18,000
Sundry selling expenses	6,000
Sales	500,000

Required;

1. Prepare a production cost statement
2. Prepare a profit/loss statemen

I) COST STATEMENT FOR 30th SEPT 2012

Opening stock of (R.M)	
Add : purchases of (R.M)	

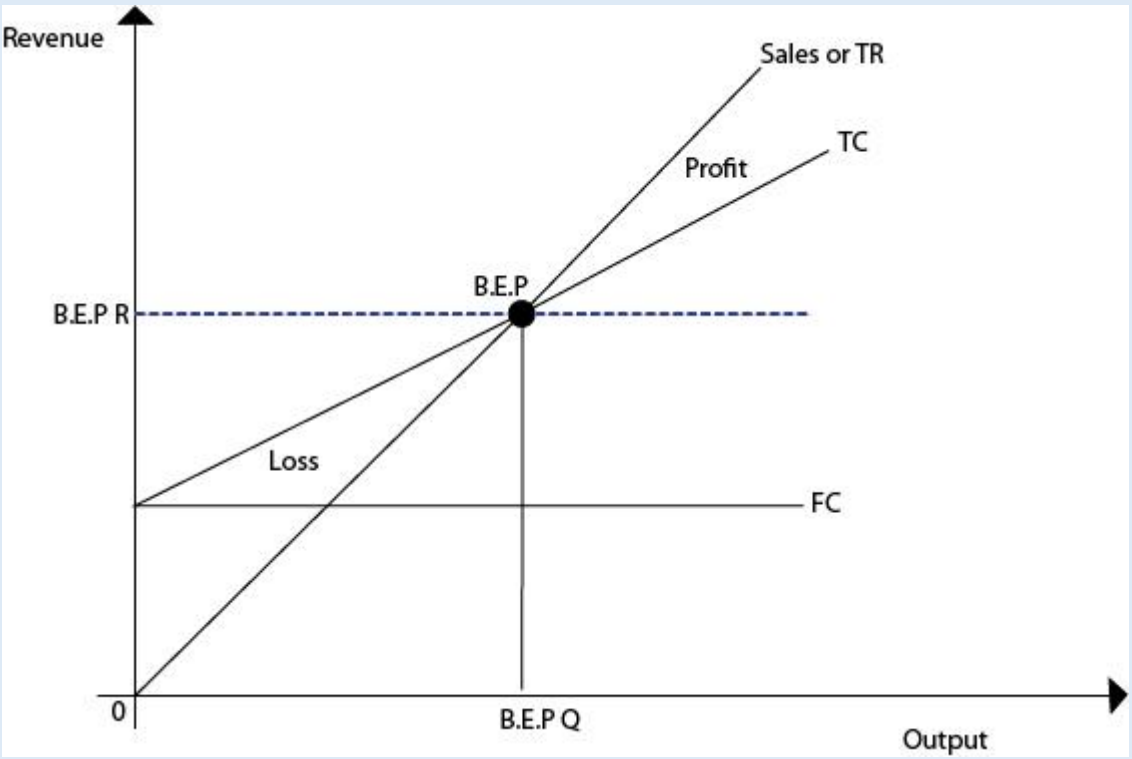
cost of R.M available for use	
less : Closing stock of (R.M)	
Cost of R.M used	
Add : Factory wages	
PRIME COST	
Add : Manufacturing overhead (M.O.H)	
Supervisor's salary	30,000
Factory rent	10,000
Factory power	5,000
sundry factory expenses	15,000
Add: W.I.P(01.10.2011)	
Less: W.I.P(31.09.2012)	
PRODUCTION COST	

II) PROFIT/LOSS STATEMENT FOR 30th SEPT 2012

Sales	
Less: Cost of good sold	
Opening stock of finished goods	20,000
Add: Production cost	390,000
	410,000
Less: closing stock finished goods	23,000
Gross profit	
Less: Administration cost/expenses	
Office salary	13,000
Sundry office expenses	7,000
Selling and distribution cost/expenses	
Salesmen salary	18,000
Sundry selling expenses	6,000
Net profit	

BREAK EVEN POINT (B.E.P)

This is level of activity at which total sales revenue is equal to total cost (TR = TC). This means that profit = 0 which means there will be no profit and no loss.



ASSUMPTION OF B.E.P CHART

Selling price and variable cost per unit remain the same at various levels of output

1. Fixed cost remain constant at all levels of activity within the given range
2. It is possible to distinguish between the cost and sales of a single product only
3. This chart shows the relationship between the cost and sales of a single product only
4. The techniques of production remain unchanged.

ILLUSTRATION

- You are required to prepare from the following information;

1. a break even chart
2. contribution /sales graph or profit volume graph
3. show the margin of safety in this chart if actual level of output is 20'000 units

Selling price per unit is 100/=

Variable cost per unit is 50/=

Fixed cost is 600'000/=

BREAK EVEN CHART

LEVEL OF OUTPUT PER UNIT	FIXED COST	VARIABLE COST Tshs 50 per unit	T.COST	SALE 100 p unit
5000	600,000	250,000	850,000	500,00
10,000	600,000	500,000	1,100,000	1,000,
15,000	600,000	750,000	1,350,000	1,500,
20,000	600,000	1,000,000	1,600,000	2,000,

MARGIN OF SAFETY

Margin = profit

- Margin of safety ; This represents the difference between the actual level of activity and the breakeven level of activity e.g If 80% is actual level of activity and Break even is 30%, calculate marginal safety

=Margin of safety= Actual sales-BED sales

=Margin of safety = 80% - 30%

Margin of safety = 50%

ANGLE OF INCIDENCE;

This shows at the breakeven point between the sales curve and total cost curve.

- This angle indicates the rate of increase in profit after the Breakeven point
- If this angle is wider, then profit will be increased at a higher rate after the breakeven point

CALCULATION OF BREAK EVEN POINT

ILLUSTRATION 1

State the formula to calculate breakeven point in terms of unit to be produced and sold.

We are going to use the following abbreviations;

S.P = Selling price

C.P = Cost price

P = Profit

C.M = Contribution margin & contribution margin per unit = CM/U

S.P = C.P +P

C.P = F.C + V.C

Contribution margin = S.P – V.C

B.E.P In terms of unit produced = (F.C)/(Contribution margin per unit)

$$= \frac{\text{Fixed cost}}{\text{Contribution margin}}$$

B.E.P in terms of sales value= (F.C)/(CM/C) x (S.P)/U

Contribution margin per unit = (S.P)/U - (V.C)/U

Sometimes; variable cost = material + labour

Contribution margin ratio =(C.M)/(S.P) or (F.C)/(1-V.C/SP)

ILLUSTRATION 2

Star manufactures a product called plate, in his own factory. Fixed cost per month is 45'000, each unit of plate cost 8/= by way of material and 17/= by way of direct labor. The selling price per unit is 40/=. How many units must he manufactures and sale per month in order to Break even

SOLUTION;

GIVEN DATA

Fixed cost = 45'000

Selling price/unit = 40/=

Unit of plate by way of material = 8/=

Unit of plate by way of direct labor = 17/=

Contribution margin = selling price – variable cost

Variable cost = material + labor

Variable cost = 8 + 17

Variable cost = 25

Contribution margin = 40 – 25

15

$$B.E.P = \frac{\text{Fixed cost}}{\text{Contribution margin}}$$

$$= \frac{45,000}{15}$$

=15

STATEMENT OF PROFIT / LOSS

Sales	(3000 x 40/=)	120,000
Less; variable cost		
Unit of plate by way of material (8 x 3000)=	24,000	
Unit of plate by way of direct labor(17 x 3000)=	51,000	
Fixed cost		45,000
		(120,000)
B.E.P (Break Even Point)		0

The above presentation verify that sales of 120,000, profit will be '0'.

ILLUSTRATION 3

Basic facts as from the above problem assume that the company wishes to make a profit of 6000 per month. Calculate the number of units that she

must produce and sale to attain this profit also calculate the amount of sales revenue that can generate this profit.

Solution;

(Fixed cost+desired profit)/(contribution margin unit)

Sales revenue = Quantity to be produced x SP/U

Let DM/U = 8

DL/U = 17

F.C = 45,000

Desired profit = 6000

Contribution margin = 15

SP/U = 40/=

Quantity to be produced = F.C + D.F/CM/U→(Fixed cost+Desired profit) /Contribution margin per unit

(45,000 + 6000)/ 15

(51,000/15) = 3400

Quantity to be produced = 3400

Sales revenue = Quantity to be produced x SP/U

= 3400 X 40

= 136,000

STATEMENT OF PROFIT/LOSS

Sales		
less ; variable cost		
unit of plate by way of material (8 x 3400)	27,200	

unit of plate by way of direct labour (17x3400)	57,800
Fixed cost	45,000
PROFIT	

ILLUSTRATION 4.

P.LTD manufactures a standard product called Pipi. The following is a summary of their cost incurred in
2008.

Fixed factory cost	24,000
Fixed administration cost	10,800
Direct labour	48,000
Depreciation of plant (variable cost)	8,000

In 2008, a total of 40'000 units of pipi were produced/ manufactured at a standard price of 5.20£ per unit.

The company has been approached by manufacturer/producer to supply annually 5000 units of pipi at 4.50£ per unit, At present the whole of P.LTD's Plant capacity is being used, so to produce the additional 5000 units, the company will need to acquire plants at a cost of 20'000£ that will have a useful life of 10 years and no residual value. Additional production will also increase the factory cost by 5% and selling distribution cost by 10%.

Required:

Would you recommend that P.LTD should accept the order?

Solution:

STATEMENT OF PROFIT OR LOSS BEFORE ACCEPTING ORDER

Sales (40'000 x 5.20)	
Less; variable cost	
Material	54,000
Direct labor	4,000
Depreciation of plant	8,000
FIXED COST	
Fixed factory cost	24,000
Fixed administration cost	10,800
Fixed selling and distribution cost	3,200
PROFIT BEFORE ACCEPTING ORDER	

STATEMENT OF PROFIT/LOSS AFTER ACCEPTING THE ORDER

Sales revenue (40,000 x 5.2)	208,000
(5000 x 4.5)	22,500
less ; TOTAL COST	
Material (45,000 x 1.35)	60750
Direct labour (45,000 x 1.2)	54,000
Depreciation of plant ; old plant ; 8000	
new plant; 2000	10,000
Fixed factory cost (24,000 x 5%)+24,000	25,200
Fixed admin. Cost	10,800
Fixed selling and distribution cost (32000 x 10%)	3,200
PROFIT MADE BY BOTH NEW AND OLD ORDER	

Recommendations:

P Ltd should accept the order since it's results to additional profit of Tshs. 6,550 (66,550-60,000)

WORKINGS

RAW MATERIALS

Material before order = 54,000

Units produced before order = 40,000

54,000/40,000 =1.35 units

= (Units produced before order + Additional units for order)

= (40,000 + 5000)

= 45,000

DIRECT LABOUR

Direct labor before order = 48,000

Units produced before order = 40,000

= 48,000/40,000 = 1.2 units

(Units produced before order + Additional units for order)

= 40,000 + 5,000

= 45,000

CASH BUDGET

CONCEPT;

BUDGET

A budget is a plan of action expressed in quantitative terms ''OR" is a financial and quantitative statement prepared and approved prior to a defined period of time, it may include income, expenditure and the employment of capital.

-Budget may be prepared for the business as a whole for the departments, for functions such as;

- Sales and production
- Financial and resource items such as; cash, capital, expenditures, purchases, man power etc.
- Examples of budget are;

Sales budget

Production budget

Purchases budget

Production cost budget

Selling and distribution cost budget

Cash budget

Budgeted profit and loss a/c and balance sheet

Benefits of budget

i.) These are a way of compiled planning, that is, in the presence of s budgets, a firm has clear guidelines and the financial and human resources can be utilized to achieve some specific targets or objectives.

ii.) The budget helps to improve communication and co-ordination among the management and employees.

iii.) These are used to determine and evaluate performance of the business enterprise.

iv.) The budgets help to clarify the authority and responsibility of departmental managers and other staff members.

CASH BUDGET

What is it?

Cash budget is prepared to show the expected cash receipts and payments in next few months or one year period.

The main functions of cash budget are to such that;

i.) Ensure that cash is available for revenue expenditure.

ii.) To indicate when, where and how much cash will be needed and whether , this is permanent or temporary

iii.) Preserve liquidity throughout the year

iv.) Reveal surplus cash for investment or expansion of facilities

v.) Guide management on financing capital expenditure internally or externally

The cash budget is affected by the following;

i.) Expansion or construction of the investment in fixed assets

ii.) Increase or decrease in stocks and debtors

iii.) Rate of inflation anticipated

iv.) Policy decisions like credit controls, dividends and taxation

-The cash budget is not affected by the following;

i.) Provision for bad and doubtful debts

ii.) Provision for depreciation

→ Anything that cannot involve movement of money does not affect the cash budget.

Illustration 1

The following information was extracted from the books of Box Ltd. A company which started trading one year ago;

MONTH/YEAR	SALES	PURCHASES
April, 2008	150,000	100,000
May	160,000	110,000
June	160,000	90,000
July	170,000	90,000
August	200,000	80,000
September	200,000	130,000
October	180,000	140,000
November	180,000	60,000
December	200,000	60,000

ADDITIONAL INFORMATION;

A. Cash in hand at the end of may, 2008 will be 180'000

B. 60% of the sales proceeds are received in the current month, 30% in the following month and the balance is received two months after sale

C. Suppliers are paid one month after delivery of goods

D. Corporation tax for 2007 amounting to 20'000 will be paid on 30th September 2008

E. Contractors retation money amounted to 50'000 will be paid on 30th June 2008

F. The shareholders at their last extra ordinary general meeting, increased the share capital by 70'000 and the first call of 40'000 will be received in October 2008

G. In October 2008, the company is due to receive 20'000/= as compensation for a civil suit

H. The monthly administration expenses amounted to 33'000 include; factory depreciation charge for 4'000 and preliminary expenses of 3'000

I. Office equipment worth 13'000 will be paid for in November, 2008

a. Required; prepare a cash budget for the period from 1st June to 31st December.

CASH BUDGET

DETAILS	JUNE	JULY	AUGUST	SEPT	OCT
Balance in cash	180,000	153,000	203,000	274,000	345,000
Sales collection; Receipts	159,000	166,000	187,000	197,000	188,000
First call	-	-	-	-	40,000
Civil suit compensation	-	-	-	-	20,000
Total receipts	339,000	319,000	390,000	471,000	593,000
PAYMENTS					
Payment to creditors	110,000	90,000	90,000	80,000	130,000
Office equipments					
Retention monies	50,000	-	-	-	-
Administration expenses	26,000	26,000	26,000	26,000	26,000
Payment of tax				20,000	
	186,000	116,000	116,000	126,000	156,000
Balance at the end of the month	153,000	203,000	274,000	345,000	437,000

WORKINGS;

Receipts

Sales * June 60% x 160,000 = 96,000

30% x 160,000 = 48,000

10% x 150,000 = 15,000

159,000

Jul 60% x 170,000 = 102,000

30% x 160,000 = 48,000

10% x 160,000 = 16,000

166,000

August 60% x 200,000 = 120,000

30% x 170,000 = 51,000

10% x 160,000 = 16,000

187,000

September 60% x 200,000 = 120,000

30% x 200,000 = 60,000

10% x 170,000 = 17,000

197,000

October 60% x 180,000 = 108,000

30% x 200,000 = 60,000

10% x 200,000 = 20,000

188,000

November 60% X 180,000 = 100,000

30% X 180,000 = 54,000

10% X 200,000 = 20,000

188,000

December 60% x 200,000 = 120,000

30% x 180,000 = 54,000

10% x 180,000 = 18,000

192,000

ILLUSTRATION

Draw a cash budget for S&S Co. Ltd showing the balance at the end of each month from the following information for the six month ended 31 December 2012

a) Opening cash (including bank) balance Tshs 600

b) Sales at Tshs 20 per unit

2012

March	April	May	June	July	August	September	October	November	December
130	100	120	145	200	150	175	200	195	200

Debtors pay their accounts three months after that inn which sales are made.

c) Production in units

2012

March	April	May	June	July	August	September	October	November	December
120	135	150	160	175	185	190	170	155	125

d) Direct labour costs of Tshs. 8 per unit are payable in the month of production

e) Raw materials used in production costs Tshs 5 per unit of this 80% are paid in the m nth of production.

f) Variable expenses are Tshs. 2 per unit paid on half in the same month as production and half in the month following production.

g) Will receive a legacy of Tshs 1250 in December 2012 .

h) Fixed expenses of Tshs 200 per month payable each month.

i) Drawing is to be Tshs 150 per month

j) Machinery costing Tshs 1000 to be paid for in October 2012.

SOLUTION ILLUSTRATION

Workings

PAYMENTS SCHEDULE

	July	**August**
Raw materials	160(July) x 4Tshs = 640	175 (Aug) x Tshs 4=700

150 (June) x1Tshs = 150 160 (July) x Tshs 1= 160

Direct labour 160 xTshs 8 = 1280 175 x Tshs 8 =1400

Variable (150 x Tshs 1) +(160 x Tshs 1) = 310 (175 xTshs 1) +(160 x1Tshs)=335

Fixed expenses = 200 =200

Drawings =150 =150

2730

2945

September **October**

Raw materials 185(Sept) x 4Tshs = 740 190 (Oct) x Tshs 4=760

175(Aug) x1Tshs = 175 185 (Sept) x Tshs 1= 185

Direct labour 175 xTshs 8 = 1480 190 x Tshs 8 =1520

Variable (185 x Tshs 1) +(175 x Tshs 1) = 360 (190 xTshs 1) +(185x1Tshs)=375

Fixed expenses = 200 =200

Drawings =150 =150

Machinery
=1000

3105
4190

November **December**

Raw materials 170(Nov) x 4Tshs = 680 155 (Dec) x Tshs 4=620

190(October) x1Tshs = 190 170 (Nov) x Tshs 1= 170

Direct labour 170 xTshs 8 = 1360 155 x Tshs 8 =1240

Variable (170 x Tshs 1) +(190 x Tshs 1) = 360 (155 xTshs 1)+(170x1Tshs)=325

Fixed expenses = 200 =200

Drawings =150 = 150

2940
2705

Receipt Schedule

	July	**August**	**September**	**October**	**November**	**December**
Sales units	100	160	145	200	150	175
Selling price (Tsh)	20	20	20	20	20	20
Collections	2000	3200	2900	4000	3000	3500

Legacy	-	-	-	-	-	1250
Total Receipt	2000	3200	2900	4000	3000	4750

S&S Co. Ltd CASH BUDGET

Details	July	August	September	October	November	December
Balance b/d (Opening cash)	600 2000	(130) 3200	125 2900	(80) 4000	(270) 3000	(210) 4750
	2600	3070	3025	3920	2730	4540
Less payments	2730	2945	3105	4190	2940	2705
Balance c/d (closing cash)	(130)	125	(80)	(270)	(210)	1835

NOTE: All figures with brackets are negative amount means on all months with negative cash there is bank overdraft.

COMPUTERIZED ACCOUNTING

The word computer come from the word compute which means to calculate.

- The initial objective of inventing computer was to create a fast calculating machine.
- However now-days more than 80% of work done by computer is non-mathematical nature. In real sense computer may be defined as a device that processes information or data. Data can be at various applicants when computer is used for recruiting personnel or the marks obtained by various subjects when the computer is used to prepare results or numbers of different types in case of application of computer for scientific research problems.
- Data may come in various shapes and sizes depending upon the type of computer application. A computer can store, process and retrieves data as and when desired for this reasons computers are also known as data 'PROCESSOR'. Data processor can gather data from various incoming sources merge (process of mixing) them all sort (arranging in some sequence-ascending or descending) them in desired other and print them in the desired format.

FEATURES OF A COMPUTER

HIGH SPEED OF OPERATION

The special feature of a computer is its high speed. Computers work at a meaning electronics speeds. These speeds are measurable in millions of a second. A computer can make millions of calculations without errors within few minutes.

ECONOMY

Every effort should be made to keep the cost to minimum level. The use of computer saves money for it user and ensures production of the quality goods at the least possible costs.

DELIGENCE

Computers are particularly desirable for the repetitive type of work because computer will continue to provide correct information continuously where as human beings are bound to make more and more errors as they get tired by doing the repetitive work hour after hour.

STORAGE OF DATA

A computer has memory like human beings. Unlike a human memory computer has a very large and accurate memory. The storage unit in the computer is called the memory volume of information. It can recall from its storage unit any bit of information which has been stored as and when need arises without much loss of time.

DECISION MAKING

Computers can make decisions on the basis of pre-defined criteria and can be used to solve the problems relating to different fields. A computer is able to take logical decisions and is capable of performing any job which can be split into a number of logical decisions.

ENSURES FLEXIBILITY

A computer can make modification in the stored program if it is desired. Thus, it ensures flexibility.

CONTROL

A mechanized system with the help of computer provides up to date information to the management with the help of which sound managerial decision can be made.

SCIENTIFIC RESEARCH

Man has limited memory and has been greatly limited by his inability to inter-relate sufficient volume of data to formulate and prove his hypothesis. The mechanical data processing unit with the help of computers has helped this direction without much difficult because millions of calculations are done within few minutes. Hence mechanized data processing has given a big boost to scientific research.

COMPONENTS OF COMPUTER

The basic components of a computer are as follows;

1. Input unit
2. Memory or storage unit
3. Arithmetic and logic unit
4. Output unit
5. Control unit

BASIC ORGANIZATION OF COMPUTER SYSTEM

The various functions performed by that unit are as follows;

1. **INPUT UNIT**;

This is unit transfer the information from outside to the memory or storage unit by any of the following methods.

-Punched cards which are passed through a punched card reader

-Punched paper tape, which is passed through a punched card reader.

-Magnetic tape or disc which is passed through a magnetic tape or dis- reader.

-Magnetic tape works like a domestic tape recorder. These are two reels and a mechanism for reading and writing data like domestic tape recorder, data recorded on the tape may be retained permanently or may be erased by recording other data over it. The tape is usually in width and of varying length and is made of plastic materials magnetic tapes work faster than punched cards and, like the punched cards are used not only as an input device but also are used for storage and for recording output, corrections can also be easily made on magnetic tape. Another additional advantage is that data can be inserted in this input unit which is not possible in punched paper tape or punched card after the tape or card has been punched.

MEMORY OR STORAGE UNIT

A series of figures are stored in the unit and are released at electronic speed for calculations. This unit retains temporarily results of sub-calculation till further processing. These units also serve the purpose of a store for final result of calculation before passing them to the output unit. The cost of a computer and the size of problem which it can handle depend upon its internal storage capacity.

ARITHMETIC AND LOGIC UNIT

Required calculations and logical operations are done in this unit by taking the necessary information from the memory unit the arithmetic units has the ability of performing all the ordinary operations of addition, subtraction, multiplication and division at very high speed. The logic unit is used to make decision where the instructions given to the computer require a decision may be of ‘yes’ or ‘no’ type.

OUTPUT UNIT

This unit turns out the end product i.e result, report or the final information to be obtained from the computer e.g economic order quantity of inventory variances etc. This unit transfer the final information to an outside document like printed

papers, punched card or magnetic tape.

CONTROL UNIT

This unit is also called program controller and is the most complex unit. It is a controller unit because each unit of the computer works under the supervision of this unit. Once the figures are fed into the input unit, the control unit takes complete charge and handles the figures as instructed by the computer program.

The main component of the computer is the CENTRAL UNIT (CPU). It is also known as central computer. The central processing unit contains the following units;

1. **CONTROL UNITS**
2. **ARITHMETIC AND LOGIC UNIT**.

HARDWARE

Is the physical computer itself containing a machine, keyboard, mouse, printer and related equipment used in an electronic data processing system.

SOFTWARE

Are all other materials utilized in selecting installing system and operation the electronic data processing system (except the operating personnel) SOFTWARE includes not only the computer programs (the sequence of instructions given to the computer) but everything about the electronic data processing system which helps the computer machine and its equipment to perform their functions. Software is an integral part of hardware one cannot function with the other.

DATA PROCESSING

Data refer to a number of figures or statistics about any phenomenon. In other words data are that describe units. In accounting data are usually expressed in monetary units, which are in rupees and paise. Data may also include non monetary units such as number of produced and sold, quantity of material used, number of workers employed etc. Data collected not be very useful for a specified purpose, where as processed data become useful for a specified purpose.

Raw data refer to input which after being processed is transformed into output known as information which become useful for a specific purpose.

DEVELOPMENT IN COMPUTERIZED ACCOUNT

The use of computer in commercial application has brought revolutionary changes in the industrial environment. Computerization has made its presence felt in every area of commercial application.

Most business except very smallest now use computers to handle accounting data.

ADVANTAGE OF COMPUTERIZED ACCOUNTING SYSTEM

i. Elimination of substantial manual work/efforts involved in posting entries in various books of accounts.

ii. Quick availability of any information on hand regarding debtors, creditors, funds position, etc

iii. Saving of substantial time applied in updating the books of accounts.

iv. Easy availability of information as per statutory or any other requirement.

v. Saving a storage space required for keeping voluminous data.

vi. Easy preparation of final accounts and also the reconciliation of those accounts.

By using computer the company will be saving in costs as the computer is able to do work of many clerks automatically hence employing great number of workers is reduced; Hence reduce the operational costs of the concerned company.

ACCOUNTING PACKAGING AND SOFTWARE

Software package is a set of pre-designed programmes since basic commercial activity remain the same. There are many software packages available in computers. Some commonly used are;

I. PERSONAL COMPUTER

a) Spread sheet

b) Data base

c) Word processor

(A) Spread sheet

A software designed to facilitate the creation and revision of Mathematical models, analysis and reports. Usually for business application

Spread sheet is a computerized matrix or gird made up of 254 rows and 63 columns. Any item in spread sheet may be changed at any time and new results will instantly and automatically shown. Also can be used to seek goals such as specific profit figures, etc

Spread sheet tend to be written by accountants for their own use, rather than by computer programmers.

BENEFITS OF SPREAD SHEET

a) It saves time by performing any calculations across the rows and columns within seconds.

b) It is a very simple tool to learn.

c) It provides greater flexibility for playing with numbers.

d) Eliminates the work of recalculations and re preparations of statement by automatically modifying the spread sheet for any changes.

(B)Data Base

Is any organized collection of information, A computer programme or group of programmes whose purpose is to organize, store, retrieve and allow the entry and updating of data base is called Data base Management System.

For computerized environment Data Base consists of related information. The basic objective of creating a Data Base is that once the information is available in the system in an organized form, it should be accessible to many users for multiple uses. Example;

i. Pay roll

ii. Mailing list

(C) Word Processor

Tools designed to simplify writing tasks. It is a powerful tool for;

- Document presentation
- Formatting document
- Saving the edited version of document

A word processor is a combination of computer hardware (the physical machine) and software.

The word processor benefit the user in the following manner;

- Eliminate the need to retyping entire page.
- Major changes can be incorporated as well without retyping.

(B) SOFTWARE PACKAGES FOR ACCOUNTING

There are number of ready made software packages that are available in the market. Since the application in the area of accounting are standard, then packages are also of standard and provide quite similar features.

The following are some standard application in the area of accounting which will be covered by one other pages. Accounting areas according to application may be broadly divided into;

i. General ledger

ii. Accounts payable

iii. Accounts receivable

(I) General ledger

This system helps in managing financial accounting. It generally serves the operational need of an accounting system also the statutory and management information requirements of an organization.

The report generated by the system include;

a) Day books

b) Journal

c) Subsidiary ledger

(II) ACCOUNTS PAYABLE

The accounts payable helps in monitoring suppliers bills, payment and outstanding. Accounts payable also assist in managing the payment and planning for cash requirements.

Accounts payable generates about the following reports;

- Bill register
- Payment register
- Credit/ Debit note
- List of outstanding

The packages can be used as they are or modified by the originating agency as per the users requirements. Standard packaging have immensely facilitated computerization of commercial application on;

- Trial balance
- Balance sheet
- Profit and loss statement
- Budget variance
- Funds flow statement
- Ratio analysis

(III) ACCOUNTS RECEIVABLE

The Accounts Receivable System (AIR) helps in reducing money collection periods and minimizes bad debts. AIR details with customer invoice, receipts and outstanding. With the use of AIR one can inquire regarding customers details, balances, outstanding and transactions.

AIR may generate the following reports;

- Invoice register
- Receipts register
- Credit/debit/notes register
- Customer journal
- Customers ledger
- Customers statement of accounts
- Receipts due to statement
- Interest receivable on overdue invoices
- A user designed Ageing report of receivables
- Customers directory

AUDITING

Meaning of Auditing

An Audit – may be defined as an examination by an Auditor of the final accounts i.e. trading account, profit and loss account and Balance sheet of a business enterprise.

→Also it involves the checking of supporting documents from which these accounts are prepared.

→The main purpose of an Audit is to ascertain whether or not these accounts present a True and fair view of the financial position of a Business.

IAG3 Has defined Audit as under ;- Audit is an Independent examination of an expression of an opinion on, the financial statements of an entity, by an appointed Auditor in pursuance of that appointment and in compliance with any relevant statutory or other provision including in particular Tanzania statements of standard Accounting practice .(TSSAP'S.) Together with relevant Auditing standards and Guidelines.

Auditor; The word Auditor comes from Latin word 'Audire' which means to hear.

Is the one whom the Receipts and payments of an establishment were read and he was supposed to hear 'or is an Independent person who is appointed by business enterprises to audit its accounts. The auditor may be an individual or a firm.

The Auditor's Duty is to form an opinion and report on the financial statements of a business enterprise for a specific period.

Auditing; Is the process of examination of financial statement's covering the transactions over a period of an organization on a certain date in order that the auditor may issue a report on them.

→It means Auditing is the Application of Auditing principles.

TYPES OF AUDITING

The following are the types of Auditing;

Statutory Auditing

Are those which are conducted under the provisions of the law of the country, According to companies Act of Tanzania all limited companies are required to get their accounts Audited, Similarly, co-operative societies Banks, Insurance companies and financial institutions are also required to

get their accounts audited according to the provisions of respective Acts.

Private Audit

Private or voluntary Audit is that audit which is not legally required. Examples of private audit are audits of sole trader, partnership business and Management audit of a limited company.

Internal Audit

Internal Audit is conducted by the internal auditor who is an employee of an organization.

→ the main purpose of internal audit is to find out whether the internal control system is working successfully or not.

→The report of internal audit is used only by the management for the improvement of internal control system. The internal auditor carries out checking work throughout the year

→Although, he is an employee of the organization but he is given some form of Independence in order to perform his duties more efficiently.

External Audit

External Audit is carried out by an Independent Auditor who is not an employee of the organization

→Internal auditor is appointed by the owners of a business. In case of a e the limited company, the share-holders appoint an external auditor.

→The main purpose of an external auditor is to submit an audit report on the financial position of business enterprises.

The Report is accepted by the share holders and other concerned parties like Bank managers, creditors.

Procedural Audit;

1. Is an examination and Review of the internal procedures and records of an organization. The main purpose of this audit is to ascertain whether the internal procedures are reliable or not.

→The procedural audit is conducted in order to improve the efficiency of internal control system and to ensure the implementation of the procedures/laid down by the management

→Also the procedural Audit is very expensive but can be applied where the owners suspect the duplication of internal policies followed by the directors.

Management Audit

Management Audit is conducted to investigate the management aspects of a business

→The main purpose of this Audit is to prepare of report on the effectiveness of the management from the point of view of the profitability and efficient running of the business.

→This Audit can reveal strengths and weakness of the management.

Standard Audit

This is a type of audit which is conducted to ascertain whether the client accounting system complies with the required levels of standards set by the professional bodies

1. Tanzania statement of standard Accounting practices (SSAP'S)U.K
2. International Accounting standards (IAS)
3. General Accepted Accounting principle (GAAP's)

Continuous Audit/Detailed Audit

Is an Audit which involves regular intervals of say one or three months

→The Auditor visits his clients at regular or irregular interval during the financial year and checks each and every transactions

Balance sheet Audit

Verification of the values of Assets, liabilities, the balance of reserves and provisions and the amount of profit earned or loss incurred by a firm during a year.

→This audit requires the auditor to report only on the balance sheet. In this case, he cannot ascertain whether the accounts supporting the balance sheet are kept or not.

→This type of Audit is more popular in USA and CANADA and is not common in UK and other countries including East Africa countries.

→ With Development of Industries and establishment of large companies, this type of Audit will be more widely used in the future.

Vouching Audit

Vouching Audit is that Audit where the auditor checks each and every transaction right from the origin in the books of prime entry till they are posted and the final accounts are prepared from the amount posted.

→This Audit requires lot of work.

→This system has become unpopular in large organizations where the numbers of transactions are into millions and where a good internal control system is in use. These days, the auditor relies on the examination of some of the transactions scientifically selected at Random. In UK, Kenya and other East African countries vouching audit is common approach.

Government Audit

Is the audit conduct in government Authorities, ministries departments by the controlled Auditor General(CAG) according to the Exchequer and Audit ordinance or act.

Note; It is the audit required by the government and it is conducted by controller and Auditor general (CAG) as per Audit act and Exchequer ordinance.

Financial Audit

Is the audit conducted to verify the accuracy of financial statements only and creating an opinion whether or not the financial statements portray the fair and true view of the firm's financial position & operation results. Note

it is mostly conducted by External Auditor who is Independent in his opinion.

Final Audit;

1. Is the Audit conducted and carried out at the end of the financial year and normally after the preparation of financial statements

ADVANTAGES OF FINAL AUDIT

1. Reduce chances of changing figures in the books of final Account
2. It is less expensive and suitable for small business
3. It is convenient to the client staff
4. The work of auditing becomes chemical easy.

DISADVANTAGES OF FINAL AUDIT

1. Not suitable (Advisable) to large entities
2. Delays in Auditors report due to short period (time of Auditing)
3. Large possibilities of errors and frauds even after audit process

INTERIM AUDIT

Is the audit conducted and carried out before the end of the year normally between the accounting periods.

NOTE; If it is undertaken to cover certain in dates within the financial year(trading period) e.g. quarterly &s of half yearly. Mainly for determining amount of profit to enable the company to declare an interim dividend to be distributed to shareholders.

ADVANTAGES INTERIM AUDIT

1. It makes easier the audit work at the end of the financial year
2. Easy to determine errors and frauds
3. Final audit can be completed very soon.

DISADVANTAGES OF INTERIM AUDIT

1. Figures may be altered after and it works.
2. Inconvenient to the client staff.

3. Additional work.

Partial Audit

Is the audit conducted only for specific or particular purpose on the instructions of the owner (client).

O.) **Complete Audit**

This is the Audit conducted and carried out by examining every transactions of the firm through checking of all vouchers, documents, financial statements, letters and minutes in details. This Audit is suitable for the firms with very weak internal control systems.

Note; These various types of Audit can be classified according to;-

1. **Form of organization**

   Under this class, various types of audit are;-

1. Audit of accounts of a sole proprietor
2. Audit of partnership accounts
3. Audit of accounts of limited companies
4. Audit of Government accounts
5. Other institutions

Nature of work

Various types of audit are, but according to the

1. Private audit
2. Statutory audit
3. Internal audit
4. External audit

Time factor

Audit may be conducted at different intervals of time. These are;

1. Final Audit
2. Interim Audit
3. Continuous Audit

Method of approach

According to method of approach, various types of audit are;

1. Procedural audit
2. Management audit
3. Standard audit
4. Balance sheet audit
5. Vouching audit

OBJECTIVES OF AUDITING

These objectives of an Audit may be classified as under;-

1. Primary objectives
2. Secondary or subsidiary objectives

PRIMARY OBJECTIVES

The primary objective of an Audit is to enable the auditor to determine the accuracy of financial statements or accounts.

The auditor forms his opinion through an audit whether or not the final account show a True and a fair view of the financial position of a business.

If the Auditor is of the opinion that profit and loss account and the balance sheet give a true and fair view of financial position of business enterprises then any reading and using primary objective of auditing are contained in the company act. These are known as statutory objectives. These include;

1. The auditor has an obligation to prove the true and fair view or other wise of the company's financial state of affairs
2. He should confirm the proper books of accounts are being kept or not.
3. The auditor is required to communicate his findings to the shareholders of the company in form of a report together with his opinion.

SECONDARY OBJECTIVES

These secondary or subsidiary objectives of auditing are;-

1. To detect errors and fraud

   Errors and frauds can be ascertained and detected by the management through the established internal control system.

2. To prevent errors and fraud i.e. through internal control system
3. To assist the clients to improve their accounting system
4. To find out whether the internal control system is working properly or not.

It must be emphasized that it is not the auditor duty to discover frauds but if he comes across them during the audit he should point out these frauds to the concerns persons. He should also point out the errors.

FUNCTIONS OF AUDITING

1. **Studying the Accounting system**

   It is the basic function of Auditing in order to determine the nature, timing and extent of the audit procedures. Auditor should know the accounting systems.

2. **Internal control system**

   It is the process which determines that management policies are carried out according to the accounting system. This system is very useful to safeguard the interest of enterprises. The Auditor determines the effectiveness of this system.

3. **Vouching**

   This is to determine the accuracy of the accounting of the assets of the business. The auditor can check the existence of asset.

4. **Legal requirement;**

   It is the function of auditing that statement is prepared under the legal requirement and various laws like company with Income tax ordinance which are introduced by the Government.

5. **Liabilities verification**

The liabilities can be verified from the books of accounts. The auditor can write letter to a creditor for the verification of liabilities. The auditor receives the certificate from management.

6. **Capital and revenue**

   Auditing should make difference between capital and revenue items. The capital items are compared to note the financial position of the business. The revenue item is compared to determine the Income. The years Income and expenses related to many can divide in correct and coming years.

7. **Valuation of liabilities**

   Through Auditing the value of liabilities and auditor can apply the accounting principles to assess the value of liabilities. The Auditor critically examines and takes help from the expert

8. **Valuation of assets**

   The management gives the value of assets and Auditor can apply the accounting principle to assess the value of assets. The Auditor critically examines and takes help from the experts.

INTERNAL CONTROL

The whole system of controls, financial and otherwise established by the management in order to carry on the business of the enterprise in an orderly and efficient manner, safeguard the assets and secure as far as possible the completeness and occurrence of the records.

The individual components of an internal control system are known as 'controls' or Internal control various types of Internal control are;

1. Control on purchases and creditors
2. Control on stock and work in progress.
3. Control on cash receipts and payments
4. Control on wages payments
5. Control on sales and debtors
6. Other controls

DETAILED INTERNAL CONTROL OBJECTIVES

An attempt is made here to systematize the various internal control objectives independent of the type of the client's business. The Internal controls over the accounting system should be designed to ensure that the following seven objectives are achieved

1. **Validity** – The internal control system should be designed to ensure that recorded transactions are valid. The system should not permit the inclusion of fictitious or nonexistent transactions in the records.
2. **Authorization** – The system should be designed to ensure that recorded transactions are authorized. An unauthorized transaction is a fraudulent one and leads to resources wastage.
3. **Completeness** – The set procedures must ensure that existing transactions are recorded to prevent omission from the records.
4. **Valuation** – An adequate internal control system most include procedures to avoid errors in arriving at values of the transaction amounts in the recording process
5. **Classification** – The laid procedures must ensure that proper classification of accounts is made if the financial statements are to be properly stated
6. **Timing** – Procedures in the internal control system should ensure that transactions are recorded at proper time's i.e. not before or delayed as this may lead to mis – statement.
7. **Posting and summarization** – The internal control system procedures have to be designed should ensure that transaction properly recorded and included in the subsidiary records these are follows;

1. To promote operational efficiency – The control within an organization are meant to prevent unnecessary duplication of effort and waste in all aspects of the business and to discourage inefficient use of other resources.
2. To encourage adherence to prescribe policies – Management Institutes procedures and rules in order to meet goals of the entity. The internal control system is meant to provide assurance that the policies are as followed by the clients' personnel.
3. To safeguard the Assets – This relates to physical as well as non-physical assets which can be stolen, misused, accidentally destroyed unless they are protected by adequate control

4. To provide reliable data – Management must have accurate and reliable information as the basis for its future decisions and also for carrying out its operation.

INTERNAL AUDIT

Internal audit – as an independent appraisal function established by the management of an organization for the review of the internal control system as a service to the management.

The main objective of Internal Audit is as under;

1. To safeguard the company's Fixed assets
2. To assist the management as far as possible to run the business efficiently and in orderly manner.
3. To act as a consulting department to other departments
4. To detect and prevent errors and frauds perpetrated by the client staff.
5. To help in the maintenance of a strong internal control system employed by the client.
6. To help the client to reduce the audit fee of the internal auditor.

EXTERNAL AUDIT

Is the audit conducted within the organization by an independent appointed auditor from outside the organization who is recognized by NBAA. External auditor is appointed by the owner of the firm and not the management of the firm in case of limited company the share holders appointed the internal auditor.

The main objective (primary objective) of external audit is to determine the accuracy of financial statements or accounts and form a true and fair view of the financial position and operation result of the business.

Other objective under external audit is as follows;

1. To confirm whether or not the proper books of accounts are kept
2. Detection of errors and frauds
3. Present findings to the owner in a report together with his opinion (auditing opinion)

4. Assist its client to improve their accounting system i.e. vouching and internal control system.
5. Finding out the weakness or strength of internal control system.

IMPORTANCE/SIGNIFICANCE OF INTERNAL AND EXTERNAL AUDIT.

1. It helps to determine the effectiveness of internal control system
2. It cuts down the work of external auditor and as a result the audit cost of external auditor reduces
3. It helps to prevent frauds
4. It facilitates the maintenance of proper accounting records and preparation of financial statement s in time.
5. It helps to review of the implementation of corporate policies, plans and procedures.
6. It helps to examine of financial and operating information for management detailed of transactions and balances.
7. Special investigations

SIMILARITIES BETWEEN INTERNAL AND EXTERNAL AUDIT

1. Both ensure the operation of an effective system of Internal control system
2. Both use almost similar techniques to conduct audit
3. Both safeguard the assets of the company
4. Both follow the professional ethics in the conduct of Audit.

DIFFERENCES BETWEEN INTERNAL AND EXTERNAL AUDIT

INTERNAL AUDIT	EXTERNAL AUDIT
Is conducted by the internal auditor who is an employee of an organization	Is an audit which carried out by an independent auditor who is not an employee of the organization
The main objective is to find out whether the internal control system is working successfully or not.	The main objective is to determine the accuracy of financial statement or accounts and form an independent opinion or whether or not financial statements show true

	and fair view of all financial position and operation.

AUDITOR'S WORKING PAPER

Nature and definition

Introduction – The efficiency of the Audit work is enhanced through the careful compilation and maintenance of audit work performed documentation of audit work is done through preparation of Audit working papers. Working papers

Meaning;

Working papers – are the records kept by auditor of procedures applied, tests performed, evidence (information) gathered and the pertinent conclusions reached in the audit engagement

→Audit working papers should be prepared as the audit proceeds so that the details and problems are not omitted.

→Each audit working paper should be properly identified with information such as client's name, period covered, description of contents, initials of the person who prepared it, date and an index code.

FORMS/TYPES OF AUDITOR'S WORKING PAPER

Audit working papers are classified into two categories and each category assembled in a separate file. This division into the two types is a matter of convenience to the auditor and there is no guideline on it. These are as follows;

1. Permanent Audit.} For the same client
2. Current Audit file.}

A.PERMANENT AUDIT FILE

A permanent Audit file is essential to the auditor in a continuous nature and which will be of value to each successive audit

→The file acts as a constant source of reference and helps avoid asking the client the same questions every time the auditor commences the annual audit. The permanent audit file typically contains the following;

- Memoranda and Articles of association and other appropriate statutory or legal regulations
- Copies of evidencing important agreements entered by the client e.g. leases, debenture deeds and other major contracts
- Brief description of the type of business
- Details of physical location of a business e.g. Factories, offices, shops etc.
- Details of the client's accounting system and internal audit procedures
- An organization chart of the client's staff.
- Name and address of client's Advisers, including bankers, stock brokers and management statement showing important accounting matters such as history and reserves, adopted basis of accounting e.g. stock valuation department
- Lists of accounting records and responsible officials

Note; Permanent Audit files should be updated at appropriate

B. CURRENT AUDIT FILE

The current audit file is used to hold all the working papers applicable to the year under audit. It should normally contain the following;

1. A copy of the statement on which the auditors are reporting authenticated by the directors signatures
2. An index covering all working papers unless they are cross-referenced to the relevant items in the accounts.
3. Audit program
4. An internal control questionnaire and other records including flow chart if designed to record and ascertain the adequacy of the internal control system
5. A schedule for each item on the balance sheet including comparative figures, showing its makeup, existence ownership
6. A schedule supporting each item in the statutory profit and loss account including comparative figures.
7. Checklist concerning compliance with statutory disclosure provisions

8. Record of queries and their manner of disposal including notes for future attention if necessary
9. A schedule of the important statistic or working ratios, comparative figures included where appropriate.
10. A record or extract of minutes of meetings of the directors and shareholders. These should be cross- retraced where relevant to the other working papers
11. Copies of letters to clients setting out any material weaknesses or matters with which the auditors are dissatisfied regarding the accounts or control procedures.
12. Letter representation

    Note; matters not of permanent importance, but which will require attention during the subsequent year's audit should be listed with references to the relevant working paper and a note transferred to the next current file while opened.

AUDIT REPORT AND OPINION

Audit report: Is a report prepared by an independent auditor to the management after examining the company's financial statements. It includes the auditors opinion regarding the true and fair view of the company's financial statement representation.

Audit opinion: This is the view given as a recommendation by an auditor after auditing the company's financial statement.

TYPES OF AUDIT OPINION

1.Unqualified opinion

This is given when the auditor is satisfied with the presentation of the company's financial statement, i.e the company's financial statement shows the true and fair view. The company's financial statement is prepared with the compliance of international accounting standards.

2.Qualified opinion

Given when an auditor fail to give out his or her opinion regarding the true and fair view of company's financial statement. Some of the items in the financial statement are not presented in the way in which they are supposed to be presented.

3. Disclaimer opinion
Given when there is the limitation of scope i.e If the management limit an auditor to audit some of the documents or to do physical stock of the company's assets as a part of audit sampling.

1.
