

INTRODUCTION

Accounting has evolved, as in the case of medicine and law, in response to the social and economic needs of society. As business and society become more complex, accounting develops new concepts and techniques to meet the ever-increasing needs for financial information. Without such information, many complex economic developments and social programs may never have been undertaken.

In a market economy, information helps decision-makers make informed choices regarding the allocation of scarce resources under their control. When decision-makers are able to make well-informed decisions, resources are allocated in a way that better meets the needs and goals of those within the market.

Accounting is relevant in all walks of life, and it is absolutely essential in the world of business. Accounting is the system that measures business activities, processes that information into reports and communicates the results to decision-makers. Accounting quantifies business communication. For this reason, accounting is called the language of business. The task of learning accounting is very similar to the task of learning a new language; thus, the need for this book which teaches the Basics of Accounting in a very conceptual manner.

DEFINITIONS OF ACCOUNTING

Accounting is a service activity. Its function is to provide quantitative information, primarily financial in nature, about economic entities that is intended to be useful in making economic decisions.

Accounting is an information system that measures, processes and communicates financial information about an economic entity.

Accounting is the process of identifying, measuring and communicating economic information to permit informed judgments and decisions by users of the information.

Accounting is the art of recording, classifying and summarizing in a significant manner and in terms of money, transactions and events which are, in part at least, of a financial character, and interpreting the results thereof.

The Method of Venice

Luca Pacioli, a Franciscan friar and a celebrated mathematician, is generally associated with the introduction of double-entry bookkeeping. In 1494 he published his book, *Summa de Arithmetica, Geometria, Proportioni et proportionoalita* or "Everything about Arithmetic, Geometry, proportions and proportionality," which includes, *Particularis de Computis et Scripturis* or "Details of Calculation and Recording, " describing double-entry bookkeeping. His treatise reflected the practices of Venice at the time, which became known as the Method of Venice or the Italian method. Therefore, he did not invent double-entry bookkeeping, but rather described what were prevalent accounting practices of the day.

Although Pacioli made no claim to developing the art of bookkeeping, he has been regarded as the father of double-entry accounting. He stated that the purpose of bookkeeping was "to give the trader without delay information as to his assets and liabilities." Pacioli also advised the computation of a periodic profit and the closing of the books. He said, "It is always good to close the books each year, especially if you are in a partnership with others. Frequent accounting makes for long friendship. "

FUNDAMENTAL BUSINESS MODEL

For a business to be successful, it needs to develop a product or service that customers will pay for and thus create a revenue stream. It can be a new product or service that meets specific needs. It can also be a better product or service. Or, it can be a product or service that offers a better value proposition. A business requires investments to enable it to pay for the infrastructure, equipment and personnel. Only after a skillful combination of these elements can a business generate a revenue stream.

The business model is built on five activities

1. First, the investors provide the required capital for the business. The cash investment will then be held in a bank account.
2. The cash in the business can be:

- converted into another type of asset that will be used in the business (e. g. equipment) or sold (e.g. Inventory;)
- or spent on operating costs such as salaries, rentals and utilities.

3. The combination of business resources provides the basis for producing the products or services.

4. The sale of a product or service generates an asset called a receivable. This asset once collected will produce a cash inflow for the business.

5. If there's an existing debt from banks, the cash inflow from collections will be used to provide the debt providers with interest on their loans to the company. The rest of the cash can be sent back to the cycle by being converted into other assets or spent on operating costs (back to stage 2). In the normal course of business, this whole process will earn profits on which tax will have to be paid. Any profit after tax can continue to be reinvested in the cycle or paid out to the owners as a "return" on their investments.

FORMS OF BUSINESS ORGANIZATIONS

Any of the above types of activities may be performed by a business organization be it a sole proprietorship, a partnership or a corporation. A business generally assumes one of the three forms of organization. The accounting procedures depend on which form the organization takes.

Sole Proprietorship. This business organization has a single owner called the proprietor who generally is also the manager. Sole proprietorships tend to be small service-type (e. g. physicians, lawyers and accountants) businesses and retail establishments. The owner receives all profits, absorbs all losses and is solely responsible for all debts of the business. From the accounting viewpoint, the sole proprietorship is distinct from its proprietor. Thus, the accounting records of the sole proprietorship do not include the proprietor's financial records.

Partnership. A partnership is a business owned and operated by two or more persons who bind themselves to contribute money, Property, or industry to a common fund, with the intention of dividing the profits among themselves. Each partner is personally liable for any debt incurred by the partnership. Accounting considers the partnership as separate organization, distinct from the personal affairs of each partner.

Corporation. A corporation is a business owned by its stockholders. It is an artificial being created by operation of law, having the rights of succession and the powers, attributes and properties expressly authorized by law or incident to its existence. The stockholders are not personally liable for the corporation's debts. The corporation is a separate legal entity.

ACTIVITIES IN BUSINESS ORGANIZATIONS

Many types of decisions are made in business organizations. Accounting provides important information to make these decisions. The three types of organizational activities are as follows : financing, investing, and operating.

Financing Activities. Organizations require financial resources to obtain other resources used to produce goods and services. They compete for these resources in financial markets. Financing activities are the methods an organization uses to obtain financial resources from financial markets and how it manages these resources. Primary sources of financing for most businesses are owners and creditors, such as banks and suppliers. Repaying the creditors and paying a return to the owners are also financing activities.

Investing Activities. Managers use capital from financing activities to acquire other resources used in the transformation process-that is, to transform resources from one form to a different form, which is more valuable, to meet the needs of the people. Having the right mix of resources is essential to efficient and effective operations.

An **efficient** business is one that provides goods and services at low costs relative to their selling prices. An **effective** business is one that is successful in providing goods and services demanded by the customers.

Investing activities involve the selection and management including disposal and replacement of long-term resources that will be used to develop, produce, and sell goods and services. Investing activities include buying land, equipment, buildings and other resources that are needed in the operation of the business, and selling these resources when they are no longer needed.

Operating Activities. Operating activities involve the use of resources to design, produce, distribute, and market goods and services. Operating activities include research and development, design and engineering, purchasing, human resources, production, distribution, marketing and selling, and servicing. Organizations compete in supplier and labor markets for resources used in these activities. Also, they compete in product markets to sell the goods and services created by operating activities.

FUNDAMENTAL CONCEPTS

Several fundamental concepts underlie the accounting process. In recording business transactions, accountants should consider the following

Entity Concept. The most basic concept in accounting is the entity concept. An accounting entity is an organization or a section of an organization that stands apart from other organizations and individuals as a separate economic unit. Simply put, the transactions of different entities should not be accounted for together. Each entity should be evaluated separately.

Periodicity Concept. An entity's life can be meaningfully subdivided into equal time periods for reporting purposes. It will be aimless to wait for the actual last day of operations to perfectly measure the entity's profit. This conceptual allows the users to obtain timely information to serve as a basis on making decisions about future activities. For the purpose of reporting to outsiders, one year is the usual accounting period.

Stable Monetary Unit Concept. The Philippine peso is a reasonable unit of measure and that its purchasing power is relatively stable. It allows accountants to add and subtract peso amounts as though each peso has the same purchasing power as any other peso at any time. This is the basis for ignoring the effects of inflation in the accounting records.

BASIC PRINCIPLES

In order to generate information that is useful to the users of financial statements, accountants rely upon the following principles:

Objectivity Principle. Accounting records and statements are based on the most reliable data available so that they will be as accurate and as useful as possible. Reliable data are verifiable when they can be confirmed by independent observers. Ideally, accounting records are based on information that flows from activities documented by objective evidence. Without this principle, accounting records would be based on whims and opinions and is therefore subject to disputes.

Historical Cost. This principle states that acquired assets should be recorded at their actual cost and not at what management thinks they are worth as at reporting date.

Revenue Recognition Principle. Revenue is to be recognized in the accounting period when goods are delivered or services are rendered or performed.

Expense Recognition Principle. Expenses should be recognized in the accounting period in which goods and services are used up to produce revenue and not when the entity pays for those goods and services.

Adequate Disclosure. Requires that all relevant information that would affect the user's understanding and assessment of the accounting entity be disclosed in the financial statements.

Materiality. Financial reporting is only concerned with information that is significant enough to affect evolutions and decisions. Materiality depends on the size and nature of the item judged in the particular circumstances of its omission. In deciding whether an item or an aggregate of items is material, the nature and size of the item are evaluated together. Depending on the circumstances, either the nature or the size of the item could be the determining factor.

Consistency Principle. The firms should use the same accounting method from period to period to achieve comparability over time within a single enterprise. However, changes are permitted if justifiable and disclosed in the financial statements.

CORE COMPETENCIES FRAMEWORK FOR ACCOUNTANTS

In recent years, there has been a growing clamor for professional bodies and the academe to bridge the gap between the requirements of the workplace and the academic preparation of our professionals. A competency-based approach to the preparation of professionals offers a systematic and effective way of bridging this gap.

A competency-based approach to education is one where the competencies, and skill sets required of a newly admitted professional are identified through a formal process and are later validated by business and industry and subject matter experts. Such identified competencies (or learner outcomes) have predetermined performance measures for assessing skill acquisition.

The government has undertaken efforts to improve the entry-level qualification requirements for the Filipino CPAs by releasing the well-defined set of competencies, Core Competency Framework for Entry to the Philippine Accountancy profession. The core competencies for accountants identify the knowledge, skill, and professional values that new CPAs need to have in order to successfully face the challenges of today's changing environment and the future.

The strategic goal is to produce technically competent and ethical professional accountants ready to compete internationally. Hence, the higher education structure (which includes the curriculum and course syllabi) should develop the following minimum core competencies:

Knowledge

The CPA's knowledge must cover:

General Knowledge

Of emphasis here are gaining an understanding of the different cultures in the world and developing an international perspective. It is generally believed that the traits that will make our Filipino CPAs prominent in the global marketplace are:

- competency in the English language (the lingua franca of business),
- adaptability to Western business practices,
- level of trainability and
- good capabilities in dealing with foreign partners.

Organizational and Business Knowledge

In addition to the core knowledge in areas such as economics, quantitative methods and business statistics, organization behavior, marketing and operations management, the CPA must be conversant of international business and have an understanding of how the global business system works. He should also have an appreciation of the importance of ethics and corporate governance in business. The CPA must demonstrate competence in the following:

- administrative capability and efficiency
- decision modeling
- risk analysis and management
- measurement
- industry and sector perspective

Information Technology (IT) Knowledge

This includes not only being conversant with IT concepts for business systems but sound knowledge on internal control in computer-based systems, development standards and practices for business systems, management of the adoption, implementation and use of IT, evaluation of computer business systems, and managing the security of information.

Accounting Knowledge

This includes core knowledge related to accounting and related areas and must include proficiency in the International accounting and auditing standards, cost management and the latest concepts in management accounting, recent tax laws and business and commercial laws, It also includes

knowledge of corporate finance and the Philippine capital markets, professional ethics and environmental accounting and reporting. The CPA should demonstrate competence in the following:

- Basic Accounting and Preparation of Financial Statements, the Accounting Profession and International Accounting Standards
- Advanced Financial Accounting practices
- Advanced Financial Reporting principles
- Management Accounting - Basic Concepts
- Management Accounting - Information for planning, Decision-Making and Control
- Taxation, Business and Commercial Laws
- Auditing - Fundamentals
- Auditing - Advanced Concepts
- Business Finance and Financial Management

Skills

The skills to be developed include:

Intellectual

This set of skills includes the ability to carry out abstract logical thinking and understand critical thinking. It also includes creative thinking or the generation of new ideas visualization or "seeing things in the mind's eye"; and reasoning skills or the discovery of a rule or principle underlying the relationship between two, or more objects and applying it when solving a problem. The CPA must demonstrate the following skills:

- analysis
- problem solving
- strategic/critical thinking

Interpersonal

This involves developing the ability of CPAs to work in groups and being a team player. It includes the skills to participate as member of a team and contributing to group effort teaching others new skills; working to satisfy clients' expectations; negotiation skills and working with diversity or working well with men and women from diverse backgrounds. The CPA must demonstrate attributes such as:

- being a team player
- persuasion, confidence and diplomacy
- discreetness, open mind and patience
- capability for work and ability to respond well to pressure

Communication

This refers to active listening skills and the ability to communicate effectively one's points of view, both orally and in writing, at all organizational levels being able to justify one's position, deliver powerful presentations and to persuade and convince others. The CPA must demonstrate skills such as the ability to:

- verbally and/or in writing explain financial/statistical/administrative matters/policies/procedures/regulatory matters/audit results at a level appropriate to the audience.
- ask clear, concise and relevant questions to obtain desired information to perform a task.
- negotiate effectively.

Values

Values must concentrate on:

Professional Ethics

Since the objectives of the accountancy profession are to work in accordance with the highest standards of professionalism, to attain the higher level of performance and generally to meet the public interest, the need for CPAs to conform to the ethical standards of the profession become vital. These include integrity, objectivity and independence, professional competence and due care, confidentiality, and professional behavior.

Moral Values

Beyond ethical rules, there is a need for CPAs to be able to discern between what is morally right or wrong.

BRANCHES OF ACCOUNTING

The work that accountants undertake ranges far beyond that of simply summarizing information in order to calculate how much profit a business has made, how much it owes, and how much is owed to it. Although this work is still very important, accountants are involved in other types of work. Of course, other information specialists (such as market researchers and operations analysts) have also been drawn into the preparation of management information, and at one time, some observers expected accounting to be taken over by these newer and more scientifically-based disciplines. However, this has not happened. There are three main reasons:

1. Financial information supplied to external users still has a dominant influence on internal management information;
2. Other information specialists have been reluctant to become involved in detailed accounting matters ; and
3. Accountants have been quick to absorb new methods and techniques into their work.

The main branches of accounting and their brief descriptions are discussed as follows:

Auditing

Auditing is the accountancy profession's most significant service to the public. An external audit is the independent examination that ensures the fairness and reliability of the reports that management submits to users outside the business entity. The result of the examinations is embodied in the independent auditor's report. Once the required financial statements have been prepared by management, they have to be evaluated in order to ensure that they do not present a distorted picture.

External auditors are appointed from outside the organization. The external auditor's job is to protect the interests of the users of the financial statements. By contrast, internal auditors are employees of the company. They are appointed by, and answer to, the company's management though they work independently of the accounting and other departments. They ensure the accuracy of business records, uncover internal control problems and identify operational difficulties.

To differentiate further, internal auditors perform routine tasks and undertake detailed checking of the company's accounting procedures, whereas external auditors are likely to go in for much more selective testing. Nonetheless, they usually work very closely together, although the distinction made between them still remains important.

Bookkeeping

Bookkeeping is a mechanical task involving the collection of basic financial data. The data are first entered in the accounting records or the books of accounts, and then extracted, classified and summarized in the form of income statement, balance sheet and cash flows statement. This process normally takes place once a month. An income statement shows whether the business has made a profit or loss during the period, i. e. it measures how well the business has done. A balance sheet lists what the entity owns (its assets), and what it owes (its liabilities) as at the end of the period. The cash flows statement presents the cash inflows and outflows of the business during the period

The bookkeeping procedures usually end when the basic data have been entered in the books of accounts and the accuracy of each entry has been tested. At that stage, the accounting function takes over. Accounting tends to be used as a generic term covering almost anything to do with the collection and use of basic financial data. It should, however, be more properly applied to the use to which the data are put once they have been extracted from the books of accounts. Bookkeeping is a routine operation, while accounting requires the ability to examine a problem using both financial and non-financial data.

Cost Bookkeeping, Costing, and Cost Accounting

Cost bookkeeping is the process that involves the recording of cost data in books of accounts. It is, therefore, similar to bookkeeping except that data are recorded in very much greater detail. Cost accounting makes use of those data once they have been extracted from the cost books in providing information for managerial planning and control. Accountants are now discouraged from using the term 'costing' unless it is qualified in some way, i. e. By referring to some branch of costing (such as standard costing), but even so you will still find the term 'costing' in general use.

The difference between bookkeeping per se and cost bookkeeping is largely one of degree of detail. A cost accounting system contains a great deal more data, and thus once the data are summarized there is much more information available to the management of the company. Cost accounting deals with the collection, allocation, and control of the cost of producing specific goods and services. This accumulation and explanation of actual and prospective cost data is important to control current operations and to plan for the future. Cost accounting now forms one of the main sub-branches of management accounting.

Financial Accounting

Financial accounting is focused on the recording of business transactions and the periodic preparation of reports on financial position and results of operations. Financial accountants accord importance to generally accepted accounting principles. Financial accounting is the more specific term applied to the preparation and subsequent publication of highly summarized financial information. The information supplied is usually for the benefit of the owners of an entity, but it can also be used by management for planning and control purposes. It will also be of interest to other parties, e. g. Employees and creditors.

Financial Management

Financial management is a relatively new branch of accounting that has grown rapidly over the last 30 years. Financial managers are responsible for setting financial objectives, making plans based on those objectives, obtaining the finance needed to achieve the plans, and generally safeguarding all the financial resources of the entity. Financial managers are much more heavily involved in the management of the entity than is generally the case with either financial or management accountants. It should also be noted that the financial manager draws on a much wider range of disciplines (such as economics and mathematics) and relies more extensively on non-financial data than does the more traditional accountant.

Management Accounting

Management accounting incorporates cost accounting data and adapts them for specific decisions which management may be called upon to make. A management accounting system incorporates all types of financial and non-financial information from a wide range of sources.

Taxation

Tax accounting includes the preparation of tax returns and the consideration of the tax consequences of proposed business transactions or alternative courses of action. As typically known, accountants involved in tax work are responsible for computing the amount of tax payable by both business entities and individuals but their work is really more complex. Accountants with this specialization aim to comply with existing Tax statutes but are also in constant legal search for ways to minimize tax payments. It is not necessary for either companies or individuals to pay more tax than is lawfully due. If tax experts attempt to reduce their clients 'tax liabilities strictly in accordance with the law, this is known as 'tax avoidance'. Tax avoidance is a perfectly legitimate exercise but tax evasion (the non-declaration of sources of income on which tax might be due) is a very serious offense.

Government Accounting

It is concerned with the identification of the sources and uses of resources consistent with the provisions of city, municipal, provincial or national laws. The government collects and spends huge amount of public funds annually so it is necessary that there is proper custody and disposition of these funds.

Multiple Choice

1. Which of the following are true of partnerships?

1. The partners' individual exposure to debt is limited.
2. Financial statements for the partnership by law must be produced and made public.
3. A partnership is not a separate legal entity from the partners themselves.

a. 1 and 2 only

b. 2 only

c. 3 only

d. 1 and 3 only

2. Which accounting concept should be considered if the owner of a business takes goods from inventory for his personal use?

a. the substance over form concept

b. The accrual concept

c. The going concern concept

d. The business entity concept

3. Which accounting concept states that omitting or misstating this information could influence users of the financial statements?

a. The consistency concept

b. The accrual concept

c. The materiality concept

d. The going concern concept

4. Which of the following accounting concepts means that similar items should receive a similar accounting treatment?

a. Going concern

- b. Accrual
- c. Substance over form
- d. Consistency

5. Assets are usually valued under which basis?

- a. Replacement cost
- b. Historical cost
- c. Net realizable value

6. Which of the following best explain the feature of consistency of presentation?

- a. When preparing the accounts of a firm, one should normally account for similar items in the same way from one accounting period to the next.
- b. Firms in the same industry must account for similar items in the same way.
- c. Firms must comply with accounting standards and regulations.
- d. None of the above.

7. Which of the following statements about accounting concepts and the characteristics of financial reporting information is not correct?

- (i) Entities may exclude information that is relevant in financial statements because it is too difficult for the users to understand.
 - (ii) The historical cost concept means that only items capable of being measured in monetary terms can be recognized in the financial statements.
 - (iii) Consistency in use of the same accounting policies for the same or similar items from one period to the next is essential to enhance comparability among the entities.
- a. (i) and (ii)

- b. (i) and (iii)
- c. (ii) and (iii)
- d. All of the above

8. Which type of business organization is owned by its stockholders?

- a. corporation
- b. Partnership
- c. Proprietorship
- d. All the above are owned by stockholders

CHAPTER 2

OBJECTIVE OF GENERAL PURPOSE FINANCIAL REPORTING

Chapter 1 of the IFRS Framework states: The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to present and potential investors, lenders and other creditors, who use that information to make decisions about buying, selling or holding equity or debt instruments and providing or settling loans or other forms of credit.

The **primary users** need information about the resources and claims against the resources of the entity not only to assess an entity's prospects for future net cash inflows but also how effectively and efficiently management has discharged their responsibilities to use the entity's existing resources.

The IFRS Framework notes that general purpose financial reports cannot provide all the information that users may need to make economic decisions. They will need to consider pertinent information from other sources, for example, general economic conditions and expectations, political events and political climate, and industry and company outlooks.

Other Users and Their Information Needs

Decision-makers need information. The more important the decision is, the greater is the need for reliable information. Virtually all businesses and most individuals keep accounting records to aid them in making decisions. The users utilize financial statements in order to satisfy some of their different needs for information.

- **Employees** are interested in information about the stability and profitability of their employers. They are also interested in information which enables them to assess the ability of the enterprise to provide remuneration, retirement benefits and employment opportunities.
- **Customers** have an interest in information about the continuance of an enterprise, especially when they have a long-term involvement with, or are dependent on, the enterprise.
- **Government and their agencies** are interested in the allocation of resources and, therefore, the activities of the enterprises. They also require information in order to regulate the activities of the enterprises, determine taxation policies and as the basis for national income and similar statistics.
- **Public.** Enterprises affect members of the public in a variety of ways. For example, enterprises may make a substantial contribution to the local economy in many ways including the number of people they employ and their patronage of local surprises.

External users are individuals and others that have current or potential financial interest in the reporting entity but are not involved in the daily operations of the entity. The information needs of these users are diverse so that only the primary or the general-purpose financial statements are provided. These users may include owners, stockholders, creditors, potential investors, suppliers, customers, labor unions, government agencies, trade associations and the public. Their information needs is served by financial accounting.

Internal users include the board of directors, chief executive officers, chief financial -officers, vice presidents, business unit managers, plant managers and the supervisors. These employees have different specific goals that are designed to help the entity attain its overall strategies and mission. Management accountants design and use an information system that primarily helps in planning and control decisions.

QUALITATIVE CHARACTERISTICS OF USEFUL FINANCIAL INFORMATION

Chapter 3 of the IFRs Framework provides: The qualitative characteristics of useful financial reporting identify the types of information are likely to be most useful to users in making decisions about the reporting entity on the basis of information in its financial report. The qualitative characteristics apply equally to financial information in general purpose financial reports as well as to financial information provided in other ways.

Fundamental Qualitative Characteristics

Relevance and faithful representation are the fundamental qualitative characteristics of useful financial information. Information must be both relevant and faithfully represented if it is to be useful. Neither a faithful representation of an irrelevant phenomenon nor an unfaithful representation of a relevant phenomenon helps users make good decisions.

Relevance

Relevant financial information is capable of making a difference in the decisions made by users. Financial information is capable of making a difference in decisions if it has predictive value, confirmatory value, or both. The predictive value and confirmatory value of financial information are interrelated.

Relevant information influences the economic decisions of users by helping them evaluate past, present or future events, or confirming, or correcting, their past evaluations. Information about financial position and past performance is frequently used as the basis for predicting future financial position and performance and other matters in which users are directly interested. To have predictive value, information needs to be in the form of an explicit forecast.

Confirmatory and predictive roles are the principal ingredients of relevance and are interrelated. Financial information has a confirmatory role when it is used to confirm or correct the decision-makers earlier expectations. It is an analysis of the relationship between predictions and outcomes. The information is used to assess how well management has performed its function by comparing its achievements with expectations.

Faithful Representation

General purpose financial reports represent economic phenomena in words and numbers. To be useful, financial information must not only be relevant, it must also represent faithfully the phenomena it purports to represent. This fundamental characteristic seeks to maximize the underlying characteristics of completeness, neutrality and freedom from error.

Completeness. A complete depiction includes all information necessary for a user to understand the phenomenon being depicted, including all necessary descriptions and explanations. For example, a complete depiction of a group of assets would include, at a minimum, a description of the nature of the assets in the group, a numerical depiction of all of the assets in the group, and a description of what the numerical depiction represents (for example, original cost, adjusted cost or fair value).

Neutrality. Free from bias. A neutral depiction is not slanted, weighted, emphasized, de-emphasized or otherwise manipulated to increase the probability that financial information will be received favorably or unfavorably by users. Financial statements are not neutral if, by the selection or presentation of information, they influence the making of a decision or judgment in order to achieve a predetermined result or outcome.

Freedom from Error. No errors or omissions in the description of the phenomenon, and the process used to produce the reported information has been selected and applied accurate in all respects with no errors in the process. In this context, free from error does not mean perfectly accurate in all aspects.

Enhancing Qualitative Characteristics

Comparability, verifiability, timeliness and understandability are qualitative characteristics that enhance the usefulness of information that is relevant and faithfully represented.

Comparability

Information about a reporting entity is more useful if it can be compared with similar information about other entities and with similar information about the same entity for another period or another date. Comparability enables users to identify and understand similarities in, and differences among, items. Unlike the other qualitative characteristics, comparability does not relate to a single item. A comparison requires at least two items.

Consistency, although related to comparability, is not the same. Consistency refers to the use of the same methods for the same items, either from period to period within a reporting entity or in a single period across entities. Comparability is the goal consistency helps to achieve that goal. Comparability is not uniformity. For information to be comparable, like things must look alike and different things must look different.

Verifiability

Verifiability helps to assure users that information represents faithfully the economic phenomena it purports to represent. Verifiability means that different knowledge and independent observers could reach consensus, although not necessarily complete agreement, that a particular depiction is a faithful representation.

Timeliness

Timeliness means that information is available to decision-makers in time to be capable of influencing their decisions.

Understandability

Classifying, characterizing and presenting information clearly and concisely make it understandable. While some phenomena are inherently complex and cannot be made easy to understand, to exclude such information would make financial reports incomplete and potentially misleading. Financial reports

are prepared for users who have a reasonable knowledge of business and economic activities and who review and analyze the information with diligence.

Applying the Enhancing Qualitative Characteristics

Enhancing qualitative characteristics should be maximized to the extent necessary. However, enhancing qualitative characteristics (either individually or collectively) cannot render information useful if that information is irrelevant or not represented faithfully.

Cost Constraint on Useful Financial Reporting

Cost is a pervasive constraint on the information that can be provided by general purpose financial reporting. Reporting such information imposes costs and those costs should be justified by the benefits of reporting that information. The IASB assesses costs and benefits in relation to financial reporting generally, and not solely in relation to individual reporting entities. The IASB will consider whether different sizes of entities and other factors justify different reporting requirements in certain situations.

UNDERLYING ASSUMPTIONS

Going Concern

The financial statements are normally prepared on the assumption that an enterprise is a going concern and will continue in operation for the foreseeable future. Hence, It is assumed that the enterprise has neither the intention nor the need to liquidate or curtail materially the scale of its operations.

This assumption underlies the depreciation of assets over their useful lives. If an entity expects to liquidate in the near future, its assets are valued at their worth at liquidation rather than original cost.

ELEMENTS OF FINANCIAL STATEMENTS

Financial statements portray the financial effects of transactions and other events by grouping them into broad classes according to their economic characteristics. These broad classes are termed the elements of financial statements. The elements directly related to the measurement of financial position in the balance sheet are **assets**, **liabilities** and **equity**.

The elements directly related to the measurement of performance in the income statement are **income** and **expenses**. The statement of changes in financial position usually reflects income statement elements and changes in balance sheet elements.

Multiple Choice

1. Who issues International Financial Reporting Standards?

- a. The IFRS Advisory Committee
- b. The stock exchange
- c. The International Accounting Standards Board
- d. The government

2. Which groups of people are most likely to be interested in the financial statements of a sole trader?

- A. Shareholders of the entity
 - B. The business's bank manager
 - C. The tax authorities
 - D. Financial analysts
- a. A and B only
 - b. B and C only
 - c. B, C and D only
 - d. A, B and C only

3. Which of the following statements is/are true?

- A. The directors of an entity are ultimately responsible for the preparation of financial statements, even if the majority of the work on them is performed by the finance department.

B. If financial statements are audited, then the responsibility for those financial statements instead falls on the auditors instead of the directors.

C. There are generally no laws surrounding the duties of directors in managing the affairs of an entity.

a. A only

b. A and B only

c. A, B and C

d. A and C only

4. According to the IASB conceptual framework which of the following is not an objective of financial statements?

a. providing information regarding the financial position of a business

b. providing information regarding the performance of a business

c. Enabling users to assess the performance of management to aid decision making

d. Helping to assess the going concern status of a business

5. The IASB Conceptual framework identifies user groups. Which of the following is not an information need for the 'Investor' group?

a. Assessment of repayment ability of an entity

b. Measuring performance, risk and return

c. Taking decisions regarding holding investments

d. Taking buy/sell decisions

6. Which of the following correctly defines 'equity' according to the IASB's Conceptual Framework for Financial Reporting?

a. Equity is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefit.

- b. Equity is a resource controlled by an entity as a result of past events and from which future economic benefits are expected to flow to the entity.
- c. Equity is the residual interest in the assets of the entity after deducting all its liabilities.
- d. Equity is increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities.

7. Which of the following statements is/are true?

- A. The IFRS Interpretations Committee is a forum for the IASB to consult with the outside world.
 - B. The IFRS Foundation produces IFRSs. The IFRS Foundation is overseen by the IASB.
 - C. One of the objectives of the IFRS Foundation is to bring about convergence of national accounting standards and IFRSs.
- a. A and C only
 - b. B only
 - c. B and C only
 - d. C only

8. What is the role of the IASB?

- a. Oversee the standard setting and regulatory process
- b. Formulate international financial reporting standards
- c. Review defective accounts
- d. Control the accountancy profession

9. According to the IASB's Conceptual Framework for Financial Reporting, which two of the following are part of faithful representation?

- A. It is neutral
- B. It is relevant
- C. It is presented fairly
- D. It is free from material error
- a. A and B
- b. B and C
- c. A and D
- d. C and D

10. Listed below are some characteristics of financial information.

- A. Relevance
- B. Comparability
- C. Faithful representation
- D. Timeliness

Which of these are fundamental characteristics, according to the IASB's Conceptual Framework for Financial Reporting?

- a. A and B only
- b. B and D only
- c. C and D only
- d. A and C only

11. The IASB's Conceptual Framework for Financial Reporting gives four enhancing qualitative characteristics. What are these four characteristics?

- a. Consistency, understandability, faithful representation, substance over form
- b. Accrual basis, going concern concept, consistency, true and fair view
- c. Faithful representation, comparability, understandability, relevance
- d. Comparability, timeliness, understandability, verifiability

12. Which one of the following statements is true of the historical cost convention?

- a. It fails to take account of changing price levels over time
- b. It records only past transactions
- c. It values all assets at their cost to the business, without any adjustment for depreciation
- d. It has been replaced in accounting records by a system of current cost accounting

13. Which one of the following is the main aim of accounting?

- a. To maintain ledger accounts for every asset and liability
- b. To provide financial information to users of such information
- c. To produce a trial balance
- d. To record every financial transaction individually

14. Which accounting concept or convention which, in times of rising prices, tends to understate asset values and overstate profits?

- a. The going concern concept
- b. The prudence concept

- c. The realisation concept
- d. The historical cost convention

15. Which of the following is not an enhancing qualitative characteristic of good financial information?

- a. Verifiability
- b. Timeliness
- c. Comparability
- d. Profitability

16. Which of the following statements is correct?

- a. An entity is not a going concern if the management has the needs to liquidate the entity.
- b. An entity is not a going concern if the management intends to curtail significantly the scale of the entity's operations.
- c. Both A and B are correct.
- d. Neither A nor B is correct.

17. Which three of the following are not included in the fundamental qualitative characteristics of useful financial reporting information?

- A. Materiality
- B. Relevance
- C. Prudence
- D. Faithful representation
- E. Comparability

- a. A, B and D
- b. A, C and E
- c. B, D and E
- d. C, D and E

18. Some qualitative characteristics of useful financial reporting information are as follows

- A. Neutrality
- B. Materiality
- C. Free from error
- D. Completeness

According to the Conceptual Framework, which of these characteristics contribute to the faithful representation?

- a. A, B and C
- b. A, B and D
- c. A, C and D
- d. B, C and D

19. Which of the following items would be a violation of the materiality concept?

- a. An entity did not present separately a loss arising from the disposal of an asset for p5, 000 in its statement of comprehensive income. Profit before tax for the year was P1 million.
- b. An entity did not disclose a P500, 000 illegal bribe made by one of Its senior management to a government official in its financial statements.
- c. An entity expensed the purchase of plastic dust bins that have an expected useful life of two years.

d. None of the above statements violates the materiality concept.

20. Which four of the following are qualitative characteristics that enhance the usefulness of information that is relevant and faithfully represented?

A. Understandability

B. Timeliness

C. Substance over form

D. Comparability

E. Verifiability

a. A, B, C and D

b. A, B, D and E

c. A, C, D and E

d. B, C, D and E

CHAPTER 3

PARTS OF AN INFORMATION SYSTEM

An information system is a collection of people, procedures, software, hardware and data which works together to provide information essential to running an organization.

People. People are competent end users working to increase their productivity. End users use hardware and software to solve information-related or decision-making problems.

Procedures. Procedures are manuals and guidelines that instruct end users on how to use the software and hardware.

Software. Software is another name for programs-instructions that tell the computer how to process data. There are basically two kinds of software

System Software. System software is background software that helps a computer manage its internal resources. An example is the operating system. Windows and Linux are popular operating systems.

Application Software. Application software performs useful work on general-purpose problems. The two types of applications software are basic applications and advanced applications.

Basic applications include:

- Browsers-navigate, explore, find information on the Internet.
- Word processor-prepare written documents.
- Spreadsheet-analyze and summarize numerical data.
- Database management system-organize and manage data and information.
- Presentation graphics-communicate a message or persuade other people.

Advanced applications include:

- Multimedia- integrates video, music, voice, and graphics to create interactive presentations.
- Web publishers- create interactive multi-media web pages.
- Graphics' programs-create professional publications, draw, edit, and modify images.
- Virtual reality-create realistic three-dimensional virtual or simulated environments.
- Artificial intelligence-simulated human thought processes and actions.
- Project managers-plan projects, schedule, people, and control resources.

Hardware. Hardware consists of input devices, the system unit, secondary storage, output devices, and communication devices.

Input Devices. Input devices translate data and programs that humans can understand into a form the computer can process. The more common are the keyboard, mouse, scanner, digital camera and microphone.

Secondary Storage. Secondary storage stores data and programs. Three most common storage media are:

- Flash drive
- Hard disk-non-removable; internal disk drive.
- Optical disk-removable; CD and DVD are common.

ELEMENTS OF FINANCIAL STATEMENTS

Financial Position

In simple terms, assets are valuable resources owned by the entity. Per Framework, asset is a resource controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise. The future economic benefits embodied in an asset may flow to the enterprise in a number of ways. The parts of the definition of an asset can be explained further:

- **"Controlled by the enterprise"** - control is the ability to obtain the economic benefits and to restrict the access of others (e. g. An entity being the sole user of its plant and equipment or by selling idle assets).
- **"Past events"** - The event must be past before an asset can arise. For example, equipment will only become an asset when there is the right to demand delivery or access to the asset's potential. Dependent on the terms of the contract, this may be on acceptance of the order or on delivery.
- **"Future economic benefits"** - These are evidenced by the prospective receipt of cash. This could be cash itself, an account receivable or any item which may be sold. Although, for example, a factory may not be sold (on a going concern basis) for it houses the manufacturing facility for the goods. When these goods are sold, the economic benefit resulting from the use of the factory is realized as cash.

For example, an asset may be:

- Used singly or in combination with other assets in the production of goods or services to be sold by the enterprise;
- Exchanged for other assets;
- Used to settle a liability; or
- Distributed to the owners of the enterprise.

Assets include cash, cash equivalents, notes receivable, accounts receivable, inventories, prepaid expenses, property, plant and equipment, investments, intangible assets and other assets.

Liabilities are obligations of the entity to outside parties who have furnished resources. Per Framework, liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits. The parts of the definition of a liability can be explained further:

- **"Obligations"** - These may be legal or not. For example, the year-end tax liability relates to the year's (i. e. past) events but in law this liability does not arise until it is assessed some time later.

- **"Transfer economic benefits"** - This could be a transfer of cash, or other property, the provision of a service or the refraining from activities which would otherwise be profitable.
- **"Past transactions or events"** - refer to discussion in assets.
- **"Complementary nature of assets and liabilities"** - As should be evident from the above, assets and liabilities are seen as mirror images of each other.

Settlement of a present obligation may occur in a number of ways, for example, by:

- Payment of cash;
- Transfer of other assets;
- Provision of services;
- Replacement of that obligation with another obligation; or
- Conversion of the obligation to equity.

Liabilities include notes payable, accounts payable, accrued liabilities, unearned revenues, mortgage payable, bonds payable and other debts of the enterprise.

Equity is the residual interest in the assets of the enterprise after deducting all its liabilities. Equity may pertain to any of the following depending on the form of business organization

- In a sole proprietorship, there is only one owner's equity account because there is only one owner.
- In a partnership, an owner's equity account exists for each partner.
- In a corporation, owners' equity or stockholders' equity consists of share capital, retained earnings and reserves representing appropriations of retained earnings among others.

Performance

Income is increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants.

The definition of income encompasses both revenue and gains. **Revenue** arises in the course of the ordinary activities of an enterprise and is referred to by a variety of different names including sales, fees, interest, dividends, royalties, and rent.

Gains represent other items that meet the definition of income and may, or may not, arise in the course of the ordinary activities of an enterprise. Gains represent increases in economic benefits and as such are no different in nature from revenue. Hence, they are not regarded as constituting a separate element.

Expenses are decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.

The definition of expenses encompasses losses as well as those expenses that arise in the course of the ordinary activities of the enterprise. There are various classes of expenses but they are generally classified as cost of services rendered or goods sold, distribution or selling expenses, administrative expenses or other operating expenses.

Losses represent other items that meet the definition of expense and may or may not, arise in the course of the ordinary activities of an enterprise. Losses represent decreases in economic benefits and as such are no different in nature from other expenses. Hence, they are not regarded as a separate element in this framework.

THE ACCOUNT

The basic summary device of accounting is the account. A separate account is maintained for each element that appears in the balance sheet (assets liabilities and equity) and in the income statement (income and expenses). Thus, an account may be defined as a detailed record of the increases, decreases and balance of each element that appears in an entity's financial statements. The simplest form of the account is known as the "T" account because of its similarity to the letter "T".

Account Title	
Left side	Right side
Debit	Credit

THE ACCOUNTING EQUATION

Financial statements tell us how a business is performing. They are the final products of the accounting process. But how do we arrive at the items and amounts that make up the financial statements? The most basic tool of accounting is the accounting equation. This equation presents the resources controlled by the enterprise, the present obligations of the enterprise and the residual interest in the assets. It states that assets must always equal liabilities and owner's equity. The basic accounting model is:

$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$$

Note that the assets are on the left side of the equation opposite the liabilities and owner's equity. This explains why increases and decreases in assets are recorded in the opposite manner ("mirror image"). As liabilities and owner's equity are recorded. The equation also explains why liabilities and owner's equity follow the same rules of debit and credit.

DEBITS AND CREDITS - THE DOUBLE-ENTRY SYSTEM

Accounting is based on a double-entry system which means that the dual effect of a business transaction is recorded. A debit side entry must have a corresponding credit side entry. For every transaction, there must be one or more accounts debited and one or more accounts credited. Each transaction affects at least two accounts. The total debits for a transaction must always equal the total credits.

An account is **debited** when an amount is entered on the **left** side of the account and **credited** when an amount is entered on the **right** side. The abbreviations for debit and credit are Dr. (from the Latin debere) and cr. (from the Latin credere), respectively.

The account type determines how increases or decreases in it are recorded. Increases in assets are recorded as debits (on the left side of the account) while decreases in assets are recorded as credits (on the right side). Conversely, increases in liabilities and owner's equity are recorded by credits and decreases are entered as debits.

The rules of debit and credit for income and expense accounts are based on the relationship of these accounts to owner's equity. Income increases owner's equity and expense decreases owner's equity. Hence, increases in income are recorded as credits and decreases as debits. Increases in expenses are recorded as debits and decreases as credits.

NORMAL BALANCE OF AN ACCOUNT

The normal balance of any account refers to the side of the account-debit or credit where increases are recorded. Asset, owner's withdrawal and expense accounts have credit balances. This result occurs because increases in an account are usually greater than or equal to decreases.

ACCOUNTING EVENTS AND TRANSACTIONS

An accounting event is an economic occurrence that causes 'changes in an enterprise's assets, liabilities, and/or equity. Events may be internal actions, such as the use of equipment for the production of goods or services it can also be an external event, such as the purchase of raw materials from a supplier.

A transaction is a particular kind of event that involves the transfer of something of value between two entities. Examples of transactions include acquiring assets from owner(s), borrowing funds from creditors, and purchasing or selling goods and services.

TYPES AND EFFECTS OF TRANSACTIONS

It will be beneficial in the long-term to be able to understand a classification approach that emphasizes the effects of accounting events rather than the recording procedures involved. This approach is quite pioneering. Although business entities engage in numerous transactions, all transactions can be classified into one of four types, namely

1. **Source of Assets (SA).** An asset account increases and a corresponding claims (liabilities or owner's equity) account increases. Examples: (1) purchase of supplies on account; (2) Sold goods on cash on delivery basis.
2. **Exchange of Assets (EA).** One asset account increases and another asset account decreases. Example: Acquired equipment for cash.
3. **Use of Assets (UA).** An asset account decreases and a corresponding claims
4. **Exchange of Claims (EC).** One claims (liabilities or owner's equity) account increases and another claims (liabilities or owner's equity) account decreases. Example: Received utilities bill but did not pay.

Every accountable event has a dual but self-balancing effect on the accounting equation. Recognizing these events will not in any manner affect the equality of the basic accounting model. The four types of transactions above may be further expanded into nine types of effects as follows

1. Increase in Assets-Increase in Liabilities (SA)
2. Increase in Assets-Increase in Owner's Equity (SA)
3. Increase in one Asset = Decrease in another Asset (EA)
4. Decrease in Assets-Decrease in Liabilities (UA)
5. Decrease in Assets-Decrease in Owner's Equity (UA)
6. Increase in Liabilities I Decrease in Owners' Equity (EC)
7. Increase in Owner's Equity-Decrease in Liabilities (EC),

8. Increase in one Liability-Decrease in another Liability (EC)

9. Increase in one Owner's Equity-Decrease in another Owner's Equity (EC)

TYPICAL ACCOUNT TITLES USED

STATEMENT OF FINANCIAL POSITION

Assets

Assets are should be classified only into two: current assets and non-current assets. Per revised Philippine Accounting Standards (PAS) No. 1, an entity shall classify assets as current when

- a. it expects to realize the asset, or intends to sell or consume it, in its normal operating cycle
- b. It holds the asset primarily for the purpose of trading
- c. it expects to realize the asset within twelve months after the reporting period ; or
- d. The asset is cash or a cash equivalent (as defined in PAS No. 7) unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets should be classified as non-current assets. Operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents. When the entity's normal operating cycle is not clearly identifiable, it is assumed to be twelve months.

Current Assets

Cash. Cash is any medium of exchange that a bank will accept for deposit at face value. It includes coins, currency, checks, money orders, bank deposits and drafts.

Cash Equivalents. Per PAS No. 7, these are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Notes Receivable. A note receivable is a written pledge that the customer will pay the business a fixed amount of money on a certain date.

Accounts Receivable. These are claims against customers arising from sale of services or goods on credit. This type of receivable offers less security than a promissory note.

Inventories. Per PAS No. 2, these are assets which are (a) held for sale in the ordinary course of business; (b) in the process of production for such sale; or (c) in the form of materials or supplies to be consumed in the production process or in the rendering of services.

Prepaid Expenses. These are expenses paid for by the business in advance. It is an asset because the business avoids having to pay cash in the future for a specific expense. These include insurance and rent. These prepaid items represent future economic benefits-assets-until the time these start to contribute to the earning process; these, then, become expenses.

Non-current Assets

Property, Plant and Equipment. Per PAS No. 16, these are tangible assets that are held by an enterprise for use in the production or supply of goods or services, or for rental to others, or for administrative purposes and which are expected to be used during more than one period. Included are such items as land, building, machinery and equipment, furniture and fixtures, motor vehicles and equipment.

Accumulated Depreciation. It is a contra account that contains the sum of the periodic depreciation charges. The balance in this account is deducted from the cost of the related asset-equipment or buildings-to obtain book value,

Intangible Assets. Per PAS No. 38, these are identifiable, nonmonetary assets without physical substance held for use in the production or supply of goods or services, for copyrights, licenses, franchises, trademarks, brand names, secret processes, subscription lists and non-competition agreements.

Liabilities

Per revised Philippine Accounting standards (PAS) No. 1, an entity shall classify a liability as current when:

- a. it expects to settle the liability in its normal operating cycle;
- b. it holds the liability primarily for the purpose of trading;
- c. the liability is due to be settled within twelve months after the reporting period; or
- d. the entity does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period.

All other liabilities should be classified as non-current liabilities.

Current Liabilities

Accounts Payable. This account represents the reverse relationship of the accounts receivable. By accepting the goods or services, the buyer agrees to pay for them in the near future.

Notes Payable. A note payable is like a note receivable but in a reverse sense. In the case of a note payable, the business entity is the maker of the note that is, the business entity is the party who promises to pay the other party a specified amount of money on a specified future date.

Accrued Liabilities. Amounts owed to others for unpaid expenses. This account includes salaries payable, utilities payable, interest payable and taxes payable.

Unearned Revenues. When the business entity receives payment before providing its customers with goods or services, the amounts received are recorded in the unearned revenue account (liability method). When the goods or services are provided to the customer, the unearned revenue is reduced and income is recognized.

Current Portion of Long-Term Debt. These are portions of mortgage notes, bonds and other long-term indebtedness which are to be paid within one year from the balance sheet date.

Non-current Liabilities

Mortgage Payable. This account records long-term debt of the business entity for which the business entity has pledged certain assets as security to the creditor. In the event that the debt payments are not made, the creditor can foreclose or cause the mortgaged asset to be sold to enable the entity to settle the claim.

Bonds Payable. Business organizations often obtain substantial sums of money from lenders to finance the acquisition of equipment and other needed assets. They obtain these funds by issuing bonds. The bond is a contract between the issuer and the lender specifying the terms of repayment and the interest to be charged.

Owner's Equity

Capital (from the Latin copitolis, meaning "property"). This account is used to record the original and additional investments of the owner of the business entity. It is or other assets that the owner may withdraw from the business ultimately reduce it. This account title bears the name of the owner.

Withdrawals. When the owner of a business entity withdraws cash or other assets, such are recorded in the drawing or withdrawal account rather than directly reducing the owner's equity account.

Income Summary. It is a temporary account used at the end of the accounting period to close income and expenses. This account shows the profit or loss for the period before closing to the capital account.

INCOME STATEMENT

Income

Service Income. Revenues earned by performing services for a customer or client for example, accounting services by a CPA firm, laundry services by a laundry shop.

Sales. Revenues earned as a result of sale of merchandise for example, sale of building materials by a **construction supplies firm**.

Expenses

Cost of Sale. The cost incurred to purchase or to produce the products sold to customers during the period; also called cost of goods sold.

Salaries or Wages Expense. Includes all payments as a result of an employer-employee relationship such as salaries or wages, 13th month pay, cost of living allowances and other related benefits.

Telecommunications, Electricity, Fuel and Water Expenses. Expenses related to use of telecommunications facilities, consumption of electricity, fuel and water.

Rent Expense. Expense for space, equipment or other asset rentals.

Supplies Expense. Expense of using supplies (e. g. office supplies) in the conduct of daily business.

Insurance Expense. Portion of premiums paid on insurance coverage (e. g. on motor vehicle, health, life, fire, typhoon or flood) which has expired.

Depreciation Expense. The portion of the cost of a tangible asset (e. g. Buildings and equipment) allocated or charged as expense during an accounting period.

Uncollectible Accounts Expense. The amount of receivables estimated to be doubtful of collection and charged as expense during an accounting period.

Interest Expense. An expense related to use of borrowed funds.

ACCOUNTING FOR BUSINESS TRANSACTIONS

Accountants observe many events that they identify and measure in financial terms. A **business transaction** is the occurrence of an event or a condition that affects financial position and can be reliably recorded.

Financial Transaction Worksheet

Every financial transaction can be analyzed or expressed in terms of its effects on the accounting equation. The financial transactions will be analyzed by means of a financial transaction worksheet which is a form used to analyze increases and decreases in the assets, liabilities or owner's equity of a business entity.

Illustration. Galicano Del Mundo decided to establish a sole proprietorship business and named it as Del Mundo Graphics Design. Del Mundo is a graphic designer who has extensive experience in drawing, layout, typography, lettering, diagramming and photography. He possesses the talent to visually communicate to a target audience with the right combination of words, images and ideas.

Del Mundo Graphics Design can do the layout and production design of newspapers, magazines, corporate reports, journals and other publications. The entity can create promotional displays; marketing brochures for services and products; packaging design for products; and distinctive logos for businesses. He also enters into agreements with clients for the progressive development and maintenance of their web sites. His initial revenue stream comes from web designing.

The owner, Galicano Del Mundo, makes the business decisions. The assets of the company belong to Del Mundo and all obligations of the business are his responsibility. Any income that the entity earns belongs solely to Del Mundo.

When a specific asset, liability or owner's equity item is created by a financial transaction, it is listed in the financial transaction worksheet using the appropriate accounts. The worksheet that follows shows the first transaction of the Del Mundo Graphics Design. The dates are enclosed in parentheses.

During March 2015, the first month of operations, various financial transactions took place. These transactions are described and analyzed as follows:

Mar. 1 Del Mundo started his new business by depositing P350, 000 in a bank account in the name of Del Mundo Graphics Design at BPI Poblacion Branch.

Del Mundo Graphics Design

Financial Transaction Worksheet

Month of March 2015

Assets	=	Liabilities	+	Owner's Equity
Cash	=			Del Mundo Capital
(1) <u>P350,000</u>	=			<u>P350, 000</u>

The financial transaction is analyzed as follows:

- An entity separate and distinct from Del Mundo's personal, financial affairs is created.
- An economic resource-cash of P350,000 is invested in the business entity. The source of this asset is the contribution made by the owner, which represents owner's equity. The owner's equity account is Del Mundo, Capital.
- The dual nature of the transaction is that cash is invested and owner's equity created. The effects on the accounting equation areas. Follows:
increase in asset cash from zero to P350,000 and increase in owner's equity from zero to P350,000
- At this Point, the entity has no liabilities, and assets equal owners' equity.

Mar. 5 Computer equipment costing P145,000 is acquired on cash basis. The effect of the transaction on the basic equation is:

Assets	=	Liabilities	+	Owner's Equity
Cash + Computer Equipment	=			Del Mundo Capital
Bal. P350,000	=			P350, 000
(5) <u>(145,000)</u> <u>145,000</u>	=			_____
Bal. <u>P205,000</u> + <u>145,000</u>	=			<u>P350, 000</u>
	=			<u>P350, 000</u>

This transaction did not change the composition of the assets- it decreases one asset-cash and increased asset-computer equipment by P145, 000. Note that the sums of the balances on both sides of the equation are equal. This equality must always exist.

Use of T-Accounts

Analyzing and recording transactions using the accounting equation useful in conveying a basic understanding of how transactions affect the business. However, it is not an efficient approach once the number of accounts involved increases. Double-entry system provides a formal system of classification and recording business transactions.

Illustration. The rules of debit and credit will be applied to the Del Mundo Graphics Design illustration for comparison. Three transactions will be added to the example. Before being recorded, a transaction must be analyzed to determine which accounts must be increased or decreased. After this has been determined, the rules of debit and credit are applied to effect the appropriate increases and decreases to the accounts.

Mar. 1 Del Mundo started his new business by depositing P350, 000 in a bank account in the name of Del Mundo Graphics Design at BPI Poblacion Branch.

Assets (Increase)		=	Owner's Equity (Increase)	
Cash			Del Mundo, Capital	
Debit (+)	Credit (-)		Debit (+)	Credit (-)
3-1 350,000				3-1 350,000

This transaction increased both the asset-cash and owner's equity. According to the rules of debit and credit, an increase in asset is recorded as debit while an Increase in owner's equity is recorded as credit ; thus, the entry is to debit cash and to credit Del Mundo, Capital. The transaction dates are placed on the left side of the amounts for reference.

Mar. 2 Computer equipment is acquired by issuing a P50,000 note payable to Maribeth Buenviaje Office Systems. The note is due in six months.

Assets (Increase)		=	Owner's Equity (Increase)	
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Computer Equipment		Notes Payable	
Debit (+)	Credit (-)	Debit (+)	Credit (-)
3-2 50,000			3-2 50,000

The transaction increased by p50, 000 the asset-computer equipment and the liability-notes payable. Computer equipment must be debited and notes payable must be credited.

True or False

1. Expenses represent the cash paid for goods sold or services rendered in the process of generating revenue.
2. Payment of a liability will not affect total assets but will cause total liabilities to decrease.
3. In a partnership, an owner's equity account exists for each partner.
4. Owner's equity is the excess of an entity's capital over its liabilities.
5. Not all financial transactions can be analyzed in terms of the basic accounting model.
6. Accounts that appear on the left side of the accounting equation usually have credit balances.
7. An accounting information system is the combination of personnel, records and procedures that a business uses to meet its need for financial information.
8. According to the balance sheet equation, the assets of a business entity must always equal the liabilities and owner's equity.
9. The basic summary device of accounting is the accounting equation.
10. Asset is a resource controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise.
11. Expenses cause decreases in owner's equity and are recorded by credits.

12. Income is increases in economic benefits during the accounting period that increases equity which may have resulted from the sale of goods or rendering of services by the business.

13. Income increases owner's equity and is recorded by a debit.

14. For every transaction, there is at least one account affected.

15. A debit entry always decreases the balance of an account.

16. A cash acquisition of a laptop computer will cause total assets to increase.

Fill in the Blanks

Rules of Debit and Credit

The account type determines how increases or decreases in it are recorded. Determine whether the word debit or credit is appropriate for each statement.

1. Asset accounts normally have balances. An increase in asset is recorded as _____ a while a decrease in asset is recorded as a _____.

2. Liability accounts normally have _____ balances. An increase in liability is recorded by a _____ and a decrease is entered as a _____.

3. The owner's capital account normally has a _____ balance. This account increases on the _____ side and decreases on the _____ side.

4. Income accounts normally have _____ balances. These accounts increase on the _____ side and decrease on the _____ side.

5. Expense accounts normally have _____ balances. These accounts increase on the _____ side and decrease on the _____ side.

Fill In the Blanks

- a. The four phases of accounting are _____, _____, _____ and _____.
- b. Increases in the capital account are _____.
- c. Increases in income accounts are _____.
- d. Increases in expense accounts are _____.
- e. The difference between assets and liabilities is _____.
- f. Financial events that occur in a business are termed _____.
- g. An investment (by the owner) in the business increases _____ and _____.
- h. To acquire something "on account" is to create a _____.
- i. The transaction description "paid on account" means a reduction of the asset _____ and reduction of the liability _____.
- j. Income increases net assets and also _____.
- k. A withdrawal of cash for owner's personal use reduces cash and _____.
- l. The left side of the account is known as the _____, whereas the right side is the _____.
- m. Increases in asset accounts are _____.
- n. Increases in liability accounts are _____.

Problem #1

Accounting Events

Which of the following events would be recognized in the accounting records of Rogelio Ceradoy HR Consultants on the date indicated?

Feb. 15	Ceradoy HR Consultants offers to purchase a piece of land for P1, 400, 000. There is a high likelihood that the offer will be accepted.
Mar. 2	Ceradoy HR Consultants receives notice that its rentals for an office space will increase from P50, 000 to P60, 000 per month effective April.
Apr. 29	Ceradoy HR Consultants receives its electricity bill for the month of April. The bill is due on May 9.
July 10	Ceradoy HR Consultants places an order for an office equipment costing P108, 000.
Aug. 6	The office equipment ordered on July 10 is delivered. Payment is not due until Sept. 1.

Problem #2

Transaction Effects on the Basic Accounting Model

During the month of May, Galicano Del Mundo Review had the following transactions:

A L OE

- a. Paid salaries for May, P54, 000.
- b. Acquired equipment on credit, P90,000.
- c. Purchased supplies in cash, P3,000.
- d. Additional investment by owner, P120,000.
- e. Received payment for services rendered, P18, 000.
- f. Made partial payment on equipment
acquired on credit, P30,000.
- g. Billed customers for services performed, P48,000.

h. Withdrew cash for personal use, P45,000.

i. Received payment from customers already
billed, P9,000.

j. Received bills for utilities to be paid next
month, P2, 100.

Required:

For each transaction, indicate whether the assets (A), liabilities (L) or owner's equity (OE) increased (+), decreased (-), or did not change (o) by placing the appropriate sign in the appropriate column.

Problem #3

Transaction Effects on the Basle Accounting Model

The following are some transactions of Virginia Yacapin Services:

a. Received cash as additional Investment.

b. Purchased supplies on account.

c. Charged customers for services made on account.

d. Rendered services to cash customers.

e. Paid cash for rent on building.

- f. Collected on account receivable in full.
- g. Paid cash for supplies.
- h. Returned supplies purchased on account.
- i. Paid cash to settle accounts.
- j. Paid cash to owner for personal use.

Required:

For each transaction, indicate whether the assets (A), liabilities (L) or owner's equity the appropriate column. (OE) Increased (+), decreased (-) or did not change (0) by placing the appropriate sign in the appropriate column.

Problem #

Effects of Transactions

The following selected transactions were completed by Roberto Orcajada Delivery Service during July 2015:

- ____ 1. Cash received from delivery services, P92,700.
- ____ 2. Paid creditors on account, P20,000.
- ____ 3. Received cash from owner as additional investment, P600,000.
- ____ 4. Paid advertising expense, P5,000.
- ____ 5. Billed customers for delivery services on account, P55,200.
- ____ 6. Purchased supplies for cash, P6, 000.

____7. Paid rent for July, P20,000.

____8. Received cash from customers on account, P25,440.

____9. Determined that the cost of supplies on hand was P1,440 so P4,560 of supplies were used during the month.

____10. Owner withdrew cash for personal use, P20,000.

Indicate the effects of each transaction on the space provided:

- a. Increase an asset, decrease another asset.
- b. Increase an asset, increase a liability.
- c. Increase an asset, increase owner's equity.
- d. Decrease an asset, decrease a liability.
- e. Decrease an asset, decrease owner's equity.

Problem #

Recording Transactions in a Financial Transaction Worksheet

Nelson Daganta formed the Liceo Signages on Oct. 1, 2015. He deposited P250,000 in GE Money Bank under the name of the new business entity. During the month of October 2015, the following transactions occurred:

- | | |
|--------|---|
| Oct. 2 | Acquired a service vehicle in the amount of pigs, 000 on account. |
| 3 | Acquired supplies for cash, P57,000. |
| 9 | Received P87,500 cash for signs painted. |

- | | |
|----|---|
| 10 | Paid the month's rent, P25,000. |
| 11 | Painted signs for Cagayan Mobile on account, P170,000. |
| 12 | Paid P55,000 on account from Oct. 2. |
| 16 | Withdrew p25,000 for personal use. |
| 23 | Collected P35,000 from Cagayan Mobile. |
| 27 | Paid salaries of P57, 000 for the month. |
| 30 | Paaid BayanTel P7,500 for communication services for the month. |
| 31 | Paid a bill from AdAsia for P5, 500 of advertising for the month. |

Required:

Establish the following accounts in a financial transaction worksheet: Cash; Accounts Receivable supplies; service vehicle; Accounts payable; and Daganta, capital. Record in the worksheet the transactions listed above.

Problem #

Recording Transactions in a Financial Transaction Worksheet

Ruth Russell started Russell Industrial Spray Service on Apr. 1, 2015. During Apra, Russell completed the following transactions:

- a. Invested cash in the business, P60,000.
- b. Bought a service vehicle from CDO Motors for P112 500, paying P22,500 in cash, with the remainder due in thirty days.
- c. Bought spray equipment on account from Misamis Farm Supplies, P18,000.
- d, Paid rent for the month, P5,600.

- e. Paid cash for insurance on service vehicle for the year, P5,760.
- f. Received cash for spray services done on a building, P21,750.
- g. Bought supplies for cash, P5,730.
- h. Billed customers on account for services performed, P4,440.
- i. Paid cash for utilities, P960.
- j. Received bill for gasoline used by the service vehicle during the month, P3,270.
- k. Receipts from cash customers, P16, 420.
- l. Russell withdrew cash for personal use, P10,500.
- m. Paid salaries to employees, P20,400.

Required:

Record the transactions for the month of April 2015 using a financial transaction worksheet. Use the following accounts: Cash; Accounts Receivable; Supplies; Prepaid Insurance; Spray Equipment; Service Vehicle; Accounts Payable; and Russell, Capital. If the owner's equity account is affected by a transaction, identify it as revenue, expense, investment or withdrawal.

Problem #

Recording Transactions in a Financial Transaction Worksheet

Engracio Lucinada, Attorney-at-Law, opened his office on Sept. 1, 2015. The following transactions were completed during the month:

- a. Deposited P210, 000 in the bank in the name of the business.

- b. Bought office equipment on account from Daraga Corp., P147,000.
- c. Invested his personal law library into the business, P57,000.
- d. Paid office rent for the month, P7,600.
- e. Bought office supplies for cash, P8,850.
- f. Paid the premium for a one-year fire insurance policy on the equipment and the library, P1,860.
- g. Received professional fees for services rendered, P24,600.
- h. Received and paid bill for the use of a landline, P2,280.
- i. Paid salaries of two part-time legal researchers, P9,600.
- j. Paid car rental expense, P2 880.
- k. Received professional fees for services rendered, P21,200.
- l. Paid Daraga Corp. a portion of the amount owed for the acquisition of the office equipment recorded earlier, P15,000.
- m. Lucinada withdrew cash for personal use, P20, 750.

Required:

Record the transactions for the month of September 2015 using a financial transaction worksheet. Use the following accounts: Cash; Accounts Receivable; Office Supplies; Prepaid Insurance; Office Equipment Professional Library; Accounts payable; and Lucinada, capital. If the owner's equity account is affected by a transaction, identify it as revenue, expense, investment or withdrawal.

Problem #

Recording Transactions in a Financial Transaction Worksheet

On June 1, 2015, Christine Charity Resultay, Optometrist, established the Resultay Eye Clinic. Transactions completed during the month are as follows:

- a. Resultay deposited P200,000 in a bank account in the name of the business.
- b. Paid office rent for the month, P8,400.
- c. Bought supplies for cash, P7,750.
- d. Bought office equipment on account from Dagupan Equipment, P91,800.
- e. Bought a computer from Del Rosario Office Outfitters, P18,400, paying P6,000 in cash and the balance on account.
- f. Performed professional services for cash, P24,210.
- g. Paid accounts to Del Rosario Office Outfitters, P9,000.
- h. Received and paid the bill for utilities, P2,430.
- i. Paid salaries of the part-time assistants, P9,900.
- j. Performed professional services for cash, P25,150.
- k. Resultay withdrew cash for personal use, P12,500.

Required:

Record the transactions for the month of June 2015 using a financial transaction worksheet. Use the following accounts: Cash; Accounts Receivable; Office Equipment; Accounts payable; and Resultay, Capital. If the owner's equity account is affected by a transaction, identify it as revenue, expense, investment or withdrawal.

Problem #

Recording Transactions in a Financial Transaction Worksheet

In June 2015, Ma. Victoria Mones established the business, Luzon Realty. Transactions completed during the month follow:

- a. Deposited P120,000 in a bank account for the business.
- b. Paid office rent for the month, P7,000.
- c. Bought supplies consisting of stationery, folders and other office supplies
- d. Bought office equipment consisting of personal computer, desktop calculator, shredder and a check writer on account from Fair and Square Emporium, P62,000.
- e. Received bill from the Filipino Times for advertising, P3,820.
- f. Paid P9,000 to Fair and Square Emporium as part payment on purchase of office equipment recorded previously.
- g. Earned sales commissions, receiving cash, P31,600.
- h. Received and paid bill for utilities, P1,480.
- i. Paid bill for advertising recorded previously, P3,820.
- j. Paid car rental expenses used in tripping, P2,560.
- k. Mones withdrew cash for personal use, P10,300.

Required

Record the transactions for the month of June 2015 using a financial transaction worksheet. Use the following accounts: Cash; Accounts Receivable; Office Supplies; office Equipment; Accounts payable; and Mones, Capital. If the owner's equity account is affected by a transaction, identify it as revenue, expense, investment or withdrawal.

Problem #

Recording Transactions in T-Accounts

Remedios Palaganas is an experienced events planner. The transactions and accounts for the business are as follows:

- a. Invested P100,000 in cash to start her own business.
- b. Paid P5,000 for one month's rent.
- c. Bought office furniture for p15,000 in cash.
- d. Received delivery of laptop computer, P54,000. Paid 50% down, balance due in 30 days.
- e. Performed services for P12,000 in cash.
- f. Performed services for P10, 800 on credit.
- g. Acquired a fax machine for P7,500; paid P3, 000 in cash, balance due in 10 days.
- h. Received P5, 400 from clients on account.
- i. Paid P10, 000 for salaries.
- j. Settled in full the P4,500 balance for the fax machine.
- k. Received P7,000 in cash for services performed.
- l. Performed services for P12, 000 on credit.
- m. Paid P1, 350 for the monthly telephone bill.
- n. Paid P2,400 for the electric and water bills.

- o. Collected P2,000 from clients on account.
- p. Palaganas withdrew P7,000 in cash for personal expenses.

Required:

1. With the aid of T-accounts, record the transactions listed above. Use the following accounts: Cash; Accounts Receivable; Office Furniture; Office Equipment; Accounts payable; palaganas, capital; Palaganas, Withdrawals; Consulting Revenues; Salaries Expense; Rent Expense; Utilities Expense; and Miscellaneous Expense.
2. Determine the balances of the T-accounts.

Problem #

Recording Transactions in T-Accounts

The accounts and transactions of Evelyn Tria, Systems Consultant, are shown below:

- a. Invested P150,000 in cash to start the business.
- b. Paid P7,500 for one month's rent.
- c. Bought office furniture for P26 000 in cash.
- d. Performed services for P10, 500 in cash.
- e. Performed services for P12,750 on credit.
- f. Bought a desktop computer for P55,000; paid 50% down, balance in 30 days.
- g. Acquired a personal copier for P39,500 on credit; paid P9, 500 cash, balance due in 30 days.

- h. Received P7,000 from credit clients.
- i. Bought additional office chairs for P8,000 on credit.
- j. Issued a check for P32,500 to pay for salaries.
- k. Performed services for P10,250 in cash.
- l. Performed services for P11,500 on credit.
- m. Collected P6,000 on accounts receivable.
- n. Issued a check for P4, 000 in partial payment of the amount owed for office chairs.
- o. Paid P2, 250 for the monthly telephone bill.
- p. Paid P2, 500 for the monthly electric bill.
- q. Tria withdrew P10, 000 in cash for personal expenses.

Required:

1. With the aid of T-accounts, record the transactions listed above. Use the following accounts: Cash; Accounts Receivable; Office Furniture; Office Equipment; Accounts Payable; Tria, Capital; Tria, Withdrawals; Consulting Revenues; Salaries Expense; Rent Expense; Utilities Expense and Miscellaneous Expense.
2. Determine the balances of the T-accounts.

CHAPTER 4

TRANSACTION ANALYSIS (Step 1)

The analysis of transactions should follow these four basic steps:

1. Identify the transaction from source documents.
2. Indicate the accounts- either assets, liabilities, equity, income or expenses- affected by the transaction.
3. Ascertain whether each account is increased or decreased by the transaction.
4. Using the rules of debit and credit, determine whether to debit or credit the account to record its increase or decrease.

ACCOUNTING CYCLE

The accounting cycle refers to a series of sequential steps or procedures performed to accomplish the accounting process. The steps in the cycle and their aims follow:

Step 1. Identification of Events to be Recorded

Aim: To gather Information about transactions or events generally through the source documents.

Step 2. Transactions are Recorded in the Journal

Aim: To record the economic impact of transactions on the firm in a journal, which is a form that facilitates transfer to the accounts.

Step 3. Journal Entries are posted to the Ledger

Aim: To transfer the information from the journal to the ledger for classification.

Step 4. Preparation of a Trial Balance

Aim: To provide a listing to verify the equality of debits and credits in the ledger.

Step 5. Preparation of the Worksheet including Adjusting Entries

Aim: To aid in the preparation of financial statements.

Step 6. Preparation of the Financial Statements

Aim: To provide useful information to decision-makers.

Step 7. Adjusting Journal Entries are Journalized and Posted

Aim: To record the accruals, expiration of deferrals, estimations and other events from the worksheet.

Step 8. Closing Journal Entries are Journalized and Posted

Aim: To close temporary accounts and transfer profit to owner's equity.

Step 9. Preparation of a Post-Closing Trial Balance

Aim: To check the equality of debits and credits after the closing entries.

Step 10. Reversing Journal Entries are Journalized and Posted

Alm :To simplify the recording of certain regular transactions in the next accounting period.

This cycle is repeated each accounting period. The first three steps in the accounting cycle are accomplished during the period. The fourth to the ninth steps generally occur at the end of the period. The last step is optional and occurs at the beginning of the next period.

THE JOURNAL

The journal is a chronological record of the entity's transactions. A Journal entry shows all the effects of a business transaction in terms of debits and credits. Each transaction is initially recorded in a journal rather than directly in the ledger. A journal is called the book of original entry. The nature and volume of transactions of the business determine the number and type of journals needed. The general Journal is the simplest journal.

Format

The standard contents of the general journal are as follows:

1. Date. The year and month are not rewritten for every entry unless the year or month changes or a new page is needed.
2. Account Titles and Explanation. The account to be debited is entered at the extreme left of the first line while the account to be credited is entered slightly indented on the next line. A brief description of the transaction is usually made on the line below the credit. Generally, skip a line after each entry.
3. P. R. (posting reference). This will be used when the entries are posted, that is, until the amounts are transferred to the related ledger accounts. The posting process will be described later.
4. Debit. The debit amount for each account is entered in this column.
5. Credit. The credit amount for each account is entered in this column.

Simple and Compound Entry

In a simple entry, only two accounts are affected -one account is debited and the other account credited. An example of this is the entry to record the Initial investment of Diaz. However, some transactions require the use of more than two accounts. When three or more accounts are required in a journal entry, the entry is referred to as a **compound entry**.

TRANSACTIONS ARE JOURNALIZED (Step 2)

After the transaction or event has been identified and measured, it is recorded in the journal.

Note that the rules of double-entry system are observed in each transaction:

1. Two or more accounts are affected by each transaction.
2. The sum of the debits for every transaction equals the sum of the credits.
3. The equality of the accounting equation is always maintained.

THE LEDGER

A grouping of the entity's accounts is referred to as a ledger. Although some firms may use various ledgers to accumulate certain detailed information, all firms have a general ledger. A **general ledger** is the "reference book" of the accounting system and is used to classify and summarize transactions, and to prepare data for basic financial statements.

The accounts in the general ledger are classified into two general groups

1. Balance sheet or permanent accounts (assets, liabilities and owner's equity).
2. Income statement or temporary accounts (income and expenses). Temporary or nominal accounts are used to gather information for a particular accounting period. At the end of the period, the balances of these accounts are transferred to a permanent owner's equity account.

Each account has its own record in the ledger. Every account in the ledger maintains the basic format of the T-account but offers more information (e. B. the account number at the upper right corner and the journal reference column). Compared to a journal, a ledger organizes information by account.

CHART OF ACCOUNTS

A listing of all the accounts and their account numbers in the ledger is known as chart of accounts. The chart is arranged in the financial statement order, that is, assets first, followed by liabilities, owner's equity, income and expenses. The accounts should be numbered in a flexible manner to permit indexing and cross-referencing.

When analyzing transactions, the accountant refers to the chart of accounts to identify the pertinent accounts to be increased or decreased. If an appropriate account title is chart of accounts for the illustration not listed in the chart, an additional account may be added.

POSTING (Step 3)

Posting means transferring the amounts from the journal to the appropriate accounts in the ledger. Debits in the journal are posted as debits in the ledger, and credits in the journal as credits in the ledger. The steps are illustrated as follows:

1. Transfer the date of the transaction from the journal to the ledger.
2. Transfer the page number from the journal to the journal reference (J. R.) column of the ledger.
3. Post the debit figure from the journal as a debit figure in the ledger and the credit figure from the journal as a credit figure in the ledger.

4. Enter the account number in the posting reference column of the journal once the figure has been posted to the ledger.

TRIAL BALANCE (Step 4)

The **trial balance** is a list of all accounts with their respective debit or credit balances. It is prepared to verify the equality of debits and credits in the ledger at the end of each accounting period or at any time the postings are updated.

The procedures in the preparation of a trial balance follow

1. List the account titles in numerical order.
2. Obtain the account balance of each account from the ledger and enter the debit balances in the debit column and the credit balances in the credit column.
3. Add the debit and credit columns.
4. Compare the totals.

The trial balance is a control device that helps minimize accounting errors. When the totals are equal, the trial balance is in balance. This equality provides an interim proof of the accuracy of the records but it does not signify the absence of errors. For example, if the bookkeeper failed to record payment of rent, the trial balance columns are equal but in reality, the accounts are incorrect since rent expense is understated and cash overstated.

The trial balance for the illustration follows

Weddings "R" Us

Trial Balance

May 31, 2015

Cash	P22,200
Accounts Receivable	12,000
Supplies	18,000

Prepaid Rent	8,000	
Prepaid Insurance	14,400	
Service Vehicle	420,000	
Office Equipment	60, 000	
Notes Payable		P210,000
Accounts Payable		53,000
Utilities Payable		1,400
Unearned Referral Revenues		10,000
Diaz, Capital		250,000
Diaz, Withdrawals	14, 000	
Consulting Revenues		62, 400
Salaries Expense	13, 800	
Utilities Expense	<u>4, 400</u>	
	P586,800	P586,800

LOCATING ERRORS

An inequality in the totals of the debits and credits would automatically signal the presence of an error. These errors include:

1. Error in posting a transaction to the ledger

- an erroneous amount was posted to the account.
- a debit entry was posted as a credit or vice versa.

- a debit or credit posting was omitted.

2. Error in determining the account balances

- a balance was incorrectly computed.
- a balance was entered in the wrong balance column.

3. Error in preparing the trial balance

- one of the columns of the trial balance was incorrectly added.
- the amount of an account balance was incorrectly recorded on the trial balance.
- A debit balance was recorded on the trial balance as a credit or vice versa, or a balance was omitted entirely.

What is the most efficient approach in locating an error? The following procedures when done in sequence may save considerable time and effort in locating errors

1. Prove the addition of the trial balance columns by adding these columns in the opposite direction.

2. If the error does not lie in addition, determine the exact amount by which the trial balance is out of balance. The amount of the discrepancy is often a clue to the source of the error. If the discrepancy is divisible by 9, this suggests either a transposition (reversing the order of numbers) error or a slide (moving of the decimal point). For example, assume that the cash account balance is P21,750, but in copying the balance into the trial balance the figures are transposed and written as P21,570. The resulting error amounted to P180 and is divisible by 9. Another common error is the slide, or incorrect placement of the decimal point, as when also be an amount divisible by 9, P21,750. 00 is copied as P2, 175. 00. The resulting discrepancy in the trial balance will

Assume that the office equipment account has a debit balance of P42,000 but it is erroneously listed in the credit column of the trial balance. This will cause a discrepancy of two times P42,000 or P84,000 in the trial balance totals. Since such errors as recording a debit in a credit column are common, it is advisable, after determining the discrepancy in the trial balance totals, to scan the columns for an amount equal to exactly one-half of the discrepancy.

It is also advisable to look over the transactions for an item of the exact amount of the discrepancy. An error may have been made by recording the debit side of the transaction and forgetting to enter the credit side.

3. Compare the accounts and amounts in the trial balance with that in the ledger. Be certain that no account is omitted.
4. Recompute the balance of each ledger account.
5. Trace all postings from the journal to the ledger accounts. As this is done, place a check mark in the journal and in the ledger after each figure is verified. When the operation is completed, look through the journal and the ledger for unchecked amounts. In tracing postings, be alert not only for errors in amount but also for debits entered as credits, or vice versa.

Note that even when a trial balance is in balance, the accounting records may still contain errors. A balanced trial balance simply proves that, as recorded, debits equal credits. The following errors are not detected by a trial balance

1. Failure to record or post a transaction.
2. Recording the same transaction more than once.
3. Recording an entry but with the same erroneous debit and credit amounts.
4. Posting a part of a transaction correctly as a debit or credit but to the wrong account.

Journalizing Transactions

The chart of accounts for Violeta Pitular Delivery Service is as follow:

<i>Assets</i>	<i>Income</i>
110 Cash	410 Delivery Revenues
120 Accounts Receivable	<i>Expenses</i>
130 Prepaid Insurance	510 Salaries Expense
140 Service Vehicle	520 Gas and Oil Expense
150 Office Equipment	530 Repair Expense

<i>Liabilities</i>	540 Advertising Expense
210 Accounts Payable	550 Supplies Expense
<i>Owner's Equity</i>	590 Miscellaneous Expense
310 Pitular, Capital	
320 Pitular, Withdrawals	

The entity completed the following transactions in May 2016:

May 3 Placed four week-end advertisements in the Sun Daily Central Luzon for P18,500; the amount is due in 30 days.

6 Bought supplies on account from Supplies, Inc., P8,800.

15 Violeta Pitular invested in the business own office equipment with a fair market value of P52,500.

17 Received P61,800 from charge customers to apply on their accounts.

22 Received a bill from Park Trucking for repair services performed, P8,500.

26 Paid Supplies, Inc., P8,800 in full payment of account.

29 Paid salaries to employees, P21,000.

30 Received P39,000 for services performed.

31 Received and paid gasoline and oil bill relating to the service vehicle, P12,500.

31 Billed South China Bank for services performed, P45,000.

31 Pitular withdrew cash for personal use, P14,500.

Required:

Prepare the journal entries for May transactions.

Journalizing Transactions

Joanne Java Review School entered into the following transactions during October 2015:

- Oct. 1 Java made additional investments of P50,000 in the business.
- 2 Bought liability insurance for one year, P14,500.
- 3 Received a bill for advertising from SouthMin News, P3,200.
- 4 Paid rent for the month, P8,900.
- 7 Received a bill for equipment repair from E. Hipolito, P2880.
- 10 Received and deposited tuition from students, P62,500.
- 11 Received and paid the telephone bill, P2,300.
- 15 Bought chairs from E. Awayan Furniture, P18,800, paying P8,800 in cash and the balance on account.

- 18 Paid accounts to Southmin News, P3,200.
- 21 Java withdrew P8,000 for personal use.
- 24 Received a bill for gas and oil from Mindanao Oil Corp., P1,800.
- 25 Received and deposited tuition from students, P61,400.
- 27 Paid salaries of the office assistants, P12,000.
- 28 Bought a photocopier on account from Dadiangas Office Machines, P7,500.
- 29 Received P7,000 tuition from a student who had charged the tuition on account last month.
- 30 Received and paid the water utilities bill, P3,600.
- 31 Paid for flower arrangements for front office, P620.
- 31 Java invested personal computer, with a fair market value of P12,300, in the business.

Required:

Prepare the journal entries for the October transactions. Use the following accounts:

Cash; Accounts Receivable; Prepaid Insurance; Equipment; Furniture; Accounts Payable; Java, Capital; Java, Withdrawals; School Fees; Salaries Expense; Rent Expense; Gas and Oil Expense; Advertising Expense; Repair Expense; Supplies Expense; Utilities Expense; Telecommunications Expense and Miscellaneous Expense.

Problem #15

Journalizing, Posting and Preparing a Trial Balance

On Mar. 1, 2016, Rey Fernan Refozar, a recent medical board topnotcher, started his medical practice. During the month of March, the following transactions were completed:

- Mar. 1 Refozar invested P42,500 personal funds in a new bank account in the name of
 Rey Fernan Refozar, M.D.
- 2 Acquired medical equipment costing P95,000 from Tambilo Medical Equipment, paying P15,000 in cash, and financing the remainder by issuing a P80,000 note payable.
- 3 Paid rent for the month of March P7,500.
- 5 Acquired medical supplies from Suiza Medical Supply on account, P15,250.
- 7 Received P18,450 in cash from patients for medical services rendered this week.
- 9 Paid Pablo Labs for preparing laboratory work on a patient, P1,800.
- 12 Paid salaries of medical technician and receptionist, P9,600.
- 15 Billed patients P51,700 for services rendered.
- 17 Paid Suiza Medical Supply P3,750 on account.
- 20 Paid telephone expense, P850.
- 21 Paid miscellaneous expense, P1,150.
- 22 Received P27,500 from patients billed on Mar. 15.
- 23 Acquired additional medical supplies from Suiza Medical Supply on account, P9,100.
- 25 Paid salaries, P11,200.
- 26 Billed patients P40,150 for services rendered.

- 27 Paid Suiza Medical Supply, P6,150 on account.
- 28 Withdrew P15,000 from the medical practice.

Required:

1. Prepare the journal entries for the March transactions.
2. Post the entries to the ledger accounts, using account numbers for cross-reference and using journal page number 1. The following accounts will be needed: Cash (110); Accounts Receivable (120); Medical Supplies (130); Medical Equipment (140); Notes Payable (210); Accounts Payable (220); Refozar, Capital (310); Refozar, Withdrawals (320); Medical Revenues (410); Salaries Expense (510); Rent Expense (520); Laboratory Expense (530); Telephone Expense (540) and Miscellaneous Expense (550).
3. Prepare a trial balance.

Problem #16

Journalizing, Posting and Preparing a Trial Balance

Karen Leon won a concession to rent out bicycles in the Burnham Park during the summer. During the month of April, Leon completed the following transactions for her bicycle rental business:

Apr. 2 Began business by placing P120,000 in a business checking account.

- 3 Purchased supplies on account for P1,500.
- 4 Purchased ten bicycles for P25,000 paying P12,000 down and agreed to pay the balance in thirty days.
- 5 Paid P29,000 in cash for a furnished container to store the bicycles and use for other operations.
- 6 Received P4,700 in cash for rentals during the first week of operation.

- 8 Paid P4,000 in cash for shipping and installation costs (considered an addition to the cost of the container) to place the container at the park entrance.
- 9 Hired a part-time assistant to help on weekends.
- 10 Paid a maintenance person P750 to clean the grounds.
- 13 Received P5,000 in cash for rentals during the second week of operation.
- 16 Paid the assistant P480 for a weekend's work.
- 17 Paid for the supplies purchased on April 3.
- 18 Paid a P550 repair bill on bicycles.
- 20 Received P5,500 in cash for rentals during the third week of operation.
- 22 Paid the assistant P480 for a weekend's work.
- 23 Billed an entity P1,11 for bicycle rentals for employees' outing.
- 25 Paid the P3,000 fee for April to the Park Administration for the right to the bicycle concession.
- 27 Received P4,100 in cash for rentals during the week.
- 29 Paid the assistant P480 for a weekend's work.
- 30 Transferred P5,000 to personal checking account.

Required:

1. Prepare the journal entries for the April transactions.
2. Set up the follower ledger accounts and post all the journal entries: Cash; Accounts Receivable; Supplies; Container; Bicycles; Accounts Payable; Leon, Capital; Leon, Withdrawals; Rental Revenues; Wages Expense; Maintenance Expense; Repair Expense; and Concession Fee Expense.

3. Prepare a trial balance.

Problem #17

Journalizing, Posting and Preparing a Trial Balance

Winnie Villanueva is a painting contractor. During the month of April, she completed the following transactions:

- Apr. 2 Invested in the business painting equipment valued at P12,300 and placed P71,000 in a business checking account.
- 3 Acquired a service vehicle costing P80,000. Paid P50,000 cash and signed a note for the balance.
- 4 Purchased painting supplies on account for P3,200.
- 5 Completed a painting job and billed the customer P4,800.
- 7 Received P1,500 cash for painting an apartment room.
- 10 Purchased painting supplies for P1,600 cash.
- 11 Received a P4,800 check from the customer billed on April 5.
- 12 Paid P4,000 for an insurance policy for a one-year coverage.
- 13 Billed a customer P6,200 for a painting job.
- 14 Paid the assistant P1,500 for twenty-five hours' work.
- 15 Paid P400 for a tune-up of the service vehicle.
- 18 Paid for the painting supplies purchased on April 4.

20 Purchased new ladder for P6,000 and painting supplies for P2,900, on account.

22 Received a telephone bill for P600, due next month.

23 Received P3,300 in cash from the customer billed on April 13.

24 Transferred P3000 to a personal checking account.

25 Received P3,600 in cash for painting a two-room apartment.

27 Paid P2,000 on the note signed for the service vehicle.

29 Paid the assistant P1,800 for thirty hours' work.

Required:

1. Prepare the journal entries to record the April transaction.
2. Set-up the following ledger accounts and post all the journal entries: Cash; Accounts Receivable; Painting Supplies; Prepaid Insurance; Painting Equipment; Service Vehicle; Notes Payable; Accounts Payable; Villanueva, Capital; Villanueva, Withdrawals; Painting Revenues; Wages Expense; Utilities Expense; and Maintenance Expense.
3. Prepare a trial balance.

Problem #18

Journalizing, Posting, Preparing a Trial Balance and Financial Statements

Teofisto Arenas recently established a business that will operate as Arenas Cleaning Service. The transactions for February 2015 are presented below.

- Feb. 1 Deposited P62,000 cash in a bank account in the name of the new entity.
- 3 Acquired cleaning supplies on account, P21,400.
- 5 Acquired cleaning equipment on account, P15,600.
- 6 Acquired an old service vehicle costing P47,000 for the business, paying P10,000
 cash, and financing the remaining P37,000 by issuing a note payable.
- 7 Paid rent on office space for the month, P7,300.
- 9 Received P31,800 cash for cleaning services rendered.
- 10 Paid for a newspaper advertisement, P1,700.
- 12 Paid for insurance for the next six months by recording prepaid insurance, P4,800.
- 13 Paid P9,000 on account.
- 14 Paid miscellaneous expenses, P2,200.
- 15 Billed customers P18,600 for cleaning services rendered.
- 16 Paid salaries, P8,400.
- 20 Received P9,800 from customers billed on Feb. 15.
- 22 Paid amount due on the note payable, P2,400.
- 25 Paid telephone expense, P900.
- 28 Paid salaries, P7,900.

- 28 Billed customers for cleaning services rendered, P22,500.
- 28 Withdrew P10,000 from the business.

Required:

1. Prepare the journal entries for the February transactions.
2. Post the entries to the ledger accounts using account numbers for cross-reference and using journal page number 1. The following accounts will be needed: Cash (110); Accounts Receivable (120); Cleaning Supplies (130); Prepaid Insurance (140); Cleaning Equipment (150); Service Vehicle (160); Notes Payable (210); Accounts Payable (220); Arenas, Capital (310); Arenas, Withdrawals (320); Cleaning Revenues (410); Salaries Expense (510); Rent Expense (520); Advertising Expense (530); Telephone Expense (540) and Miscellaneous Expense (550).
3. Prepare a trial balance.
4. Prepare an income statement, a statement of changes in owner's equity, and a balance sheet (Note: This requirement *may* be accomplished after the discussion on financial statements).

Problem #19

Journalizing, Posting and Preparing a Trial Balance

After several years with a large accounting firm, Purita Alisuag decided to establish her own accounting practice. The following transactions of Purita Alisuag, CPA, were completed during May 2015:

- May 2 Transferred P92,500 cash from a personal savings account to a checking account,
Purita Alisuag, CPA.
- 3 Acquired office equipment on account from Liboro Furniture, P36,800.
- 4 Acquired office supplies on account from Palatino Office Supply; P17,100.

- 6 Performed accounting services for Gabayan Computers and submitted a bill of P29,200 for those services.
- 7 Paid for accounting and tax books for use in the practice, P19,500.
- 8 Paid Palatino Office Supply, P4,100 on account.
- 10 Acquired a condominium unit for the accounting practice, P265,000. A down payment of P38,000 was made and issued a note payable for the remaining P227,000.
- 12 Paid salaries, P14,200.
- 13 Received P9,750 from Gabayan Computers, billed on May 6.
- 16 Paid telephone expense, P650.
- 19 Received cash in the amount of P14,600 from Mallari Books for accounting services rendered for the month.
- 22 Acquired office supplies on amount from Palatino Office Supply, P4,650.
- 23 Withdrew P8,150 for personal use.
- 25 Paid salaries, P10,300.
- 26 Billed'Chua Exporters P31,600 for accounting services rendered.
- 27 Paid PICPA-Palawan P5,500 for professional dues.
- 28 Paid P3,250 rent on an office-copying machine.

Required:

1. Prepare the journal entries for the May transactions.
2. Post the entries to the ledger accounts, using account number for cross-reference and using journal page number 1. The following accounts will be needed: Cash (110); Accounts Receivable (120); Office Supplies (130); Office Condominium (140); Office Equipment

- (150); Accounting Library (160); Notes Payable (210); Accounts Payable (220); Alisuag, Capital (310); Alisuag, Withdrawals (320); Accounting Revenues (410); Salaries Expense (510); Rent Expense (520); Telephone Expense (530); and Professional Dues Expense (540).
3. Prepare a trial balance.

Prepare a trial balance.

Problem #20

Galicano Del Mundo hired a lawyer to help him start Del Mundo Repair Service. On March 1, Del Mundo deposited P143,750 in a bank account in the name of the entity. When the entity paid the lawyer's bill of P8,750, the lawyer advised the entity to hire an accountant to keep its records. Del Mundo was so busy that it was already March 31 when he hired you to straighten out his records. Your first task is to develop a trial balance based on the March transactions, which are described in the next two paragraphs.

After the business began and the entity had paid the lawyer's bill, the entity borrowed P62,500 from a bank. It later paid P3,250, including interest of P750, on this loan. It also acquired a second-hand service vehicle in the entity's name, paying P31,250 down and financing P92,500. The first payment on the vehicle is due April 15. The entity then leased an office and paid two month rent, P11,250, in advance. Credit acquisitions of office equipment of P10,000 and repair tools of P6,250 must be paid by April 10.

In March, Del Mundo Repair Service completed repairs of P16,250, of which P5,000 were cash transactions. Of the credit transactions, P3,750 were collected during March, and P7,500 remained uncollected at the end of March. The entity paid salaries of P5,620 to its employees. On March 31, the entity received a P930 bill for the March utilities expense and a P620 check from a customer for work to be completed in April. A customer requested a repair on March 31 to be done the following week and agreed to pay P2,500 for it. The entity is considering recording this agreement as revenue in March to make the business look better.

Required:

1. Record all of the transactions for March in journal form. Label each of the entries alphabetically.
2. Set up T-Accounts. Then, post the entries to the T-Accounts. Identify each posting with the letter corresponding to the transaction.
3. Determine the balance of each account.
4. Prepare a trial balance as at March 31.
5. Galicano Del Mundo wants you to evaluate the trial balance. The cash account balance is P155,500 which exceeds the original investment of P143,750 by P11,750. Did the entity make a profit of P11,750?
6. What are the implications of recording the repair order received on March 31 as revenue in March?

Problem #21

Effects of Errors on the Trial Balance

Which of the following errors would cause a trial balance to have unequal totals?

Explain your answers briefly. Be able to state amount of the error, if any.

- a. A payment to a creditor was recorded as a debit to Accounts Payable for P12,900 and as a credit to Cash for P10,200.
- b. A payment of P15,000 to a creditor for an account payable was debited to Accounts Receivable and credited to Cash.
- c. A purchase of office supplies of P42,000 in cash was recorded as a debit to Office Supplies for P4,200 and as a credit to Cash for P4,200.
- d. A purchase of equipment for P45,000 in cash was recorded as a debit to Supplies for P45,000 and as a credit to Cash for P45,000.

Problem #22

Effects of Errors on the Trial Balance

The following errors occurred in posting transactions from the journal to the ledger:

1. A payment of P1,700 for advertising was posted as a P1,700 debit to advertising expense and a P7,100 credit to cash.
2. The receipt of P3,000 from a client on account was posted as a P3,000 debit cash and a P3,000 credit to sales.
3. The purchase of supplies on account for P1,400 was posted twice as a debit to supplies and once as a credit to accounts payable.
4. The payment of P2,200 to a creditor on account was posted as a credit to accounts payable for P2,200 and a credit to cash for P2,200.

For each of these errors, determine the following:

- a. Is the trial balance out of balance?
- b. Of out of balance, what is the difference between the column totals?
- c. Which column total is larger?

Problem #23

Effects of Errors on the Trial Balance

The trial balance prepared by Remedios Palaganas Consulting as at Sept. 30, 2016 was not in balance. In searching for the error, an employee discovered that a transaction for the purchase of a typewriter on credit for P6,100 has been recorded by a debit of P6,100 to the Office Equipment account and a debit of P[^],100 to Accounts Payable. The credit column of the incorrect trial balance had a total of P926,000.

- a. Was the Office Equipment account overstated, understated, or correctly stated in the trial balance?
- b. Was the total of the debit column of the trial balance overstated, understated, or correctly stated?
- c. Was the Accounts Payable account overstated, understated, or correctly stated in the trial balance?
- d. Was the total of the credit column of the trial balance overstated, understated or correctly stated?

e. How much was the total of the debit column of the trial balance before correction of the error?

Required:

Explain briefly the reasons underlying your answer and state the amount of the error, if any.

Problem #24

Correcting a Trial Balance

The June 2016 trial balance for Davao Duplicators, owned by Allam Brillantes is presented below. The regular bookkeeper has resigned and left the following trial balance. It did not balance.

Davao Duplicators			
Trial Balance			
June 30, 2016			
Cash	P 44,800		
Accounts Receivable	189,600		
Supplies	70,800		
Equipment	560,000		
Accounts Payable		P	72,600

Brillantes, Capital		513,000
Brillantes, Withdrawals		50,000
Revenues		371,000
Salaries Expense	35,000	
Rent Expense		10,000
Utilities Expense	6,400	
Totals	<u>P916,600</u>	<u>P1,017,200</u>

Upon reviewing the trial balance and the process of transferring the amounts in the ledger accounts to the trial balance, two errors were discovered:

- The debit column in the trial balance was footed incorrectly.
- The balance in the accounts payable ledger account of P62,700 was transferred as P72,600.

When the balances of the ledger accounts were recomputed, two more errors were discovered:

- The Utilities Expense account balance was overstated by P1,800.
- The total debits in the Cash account amounted to P184,600 and the credits totaled P149,800.

Discovered four more errors when postings were retraced from the journal to the ledger:

- A debit posting to Accounts Receivable in the amount of P52,000 should have been P5,200.
- A debit posting to Accounts Payable for P46,000 was missing.
- A credit posting to Revenues in the amount of P7,600 was missing.
- A credit of P31,000 was posted to Accounts Payable rather than P30,100.

Required: Prepare a corrected trial balance.

Problem #25

Journalizing, Posting, Preparing a Trial Balance and Financial Statements

Vincent Fabella owns the Jose Rizal Heavy Bombers, a collegiate basketball team in the Phil-Am Basketball Association. Presented below is the Nov. 30, 2015 trial balance representing activities from Jan. 1, 2015 to Nov. 30, 2015, together with the account numbers and titles:

Jose Rizal Heavy Bombers				
Trial Balance				
Nov. 30, 2015				
Acct. No.	Account Titles	Debit	Credit	
110	Cash	P 1,129,800		
120	Accounts Receivable	3,712,500		
130	Uniform Supplies	31,050		
140	Prepaid Insurance	0		
150	Land	2,025,000		
160	Training Facilities	12,750,000		
170	Training Equipment	2,625,000		
180	Player Contracts	11,250,000		
210	Notes Payable		P 1,800,000	

220	Accounts Payable		4,725,000
230	Montgage Payable		10,500,000
310	Fabella, Capital	17,643,750	
320	Fabella, Withdrawals	1,875,000	
410	Game Attendance Revenues		10,125,000
510	Salaries Expense	4,875,000	
520	Advertising Expense	400,950	
530	Travel Expense	1,532,400	
540	Laundry Expense	528,000	
550	Medical Expense	194,550	
560	Utilities Expense	1,734,000	
570	Miscellaneous Expense	130,500	
	Totals	P44,793,750	P44,793,750

During the month of December 2015, the Bombers were participating in the 2015 playoffs and the following transactions took place:

- Dec. 1 Acquired the contact of Agustin Tionco from the Negros Navigators
for P1,875,000; paying P225,000 in cash and financing the P1,650,000
by issuing a note payable.

	2	Collected P2,809,5000 on accounts receivable from season-ticket holders.
Dec.	3	Settled accounts payable, P1,657,500.
	4	Paid for TV advertising, P78,600
	5	Acquired on account additional uniforms for the upcoming series with the San Alcantara Padres, P30,750.
	9	Billed season-ticket holders for the last five games, P320,250.
	10	Paid the amount due on this date for a note payable, P600,000.
	11	Acquired insurance for the months of December to June, P215,250. Required as prepaid insurance.
	12	Acquired additional training equipment on account, P319,500.
	15	Paid players' salaries, P1,136,250.
	17	Received P3,316,050 cash for tickets to playoff games.
	19	Paid travel expenses to San Alcantara, P558,000.
	20	Paid laundry expenses, P12,600.
	23	Paid creditors, P941,850.
	25	Paid miscellaneous expenses, P26,850.
	26	Paid medical expenses, P18,900.
	27	Paid utilities expenses, P210,450.

- 28 Paid players' salaries, P1,240,650.
- 30 Vincent Fabella withdrew P250,000.

Required:

1. Enter the amounts from the November 2015 trial balance into the appropriate ledger accounts.
2. Prepare the journal entries for the December transactions.
3. Post the entries to the ledger using page 12 as the journal page reference.
4. Prepare a trial balance as at Dec. 31, 2015.
5. Prepare an income statement and a statement of changes in equity for the year ended Dec. 31, 2015, and a balance sheet as at Dec. 31, 2015
(Note: The accomplishment of this requirement *may* be deferred.)

Multiple choice

1. Depreciation is
 - a. Added to the cost of equipment on the balance sheet.
 - b. A decrease in the fair market value of an asset.
 - c. An expense that is incurred during accounting period.
 - d. Shown on the balance sheet as a liability.
2. Accumulated Depreciation-Equipment is shown as
 - a. A contra account on the balance sheet.
 - b. A deduction from profit on the statement of owner's equity.
 - c. An addition to equipment on the balance sheet.
3. Accrued salaries are
 - a. Salaries that have been earned by employees but not paid.
 - b. Salaries that have been neither by employees nor paid.
 - c. Salaries that have been paid.

- d. Salaries that have been paid but not earned by employees.
 - e. Salaries that were earned by employees and have been paid.
4. The type of account and normal balance of Accumulated Depreciation is
- a. Asset, Credit.
 - b. Asset, Debit.
 - c. Contra asset, Credit
 - d. Contra asset, Debit
 - e. Liability, Credit.
5. The adjusting entry to record depreciation of equipment is
- a. Debit Accumulated Depreciation; Credit Depreciation Expense
 - b. Debit Accumulated Depreciation; Credit Equipment.
 - c. Debit Accumulated Depreciation; Credit Accumulated Depreciation.
 - d. Debit equipment, Credit Accumulated Depreciation Payable.
 - e. Debit Equipment; Credit Accumulated Depreciation.

6. Wilson Dacillo Animal Breeders bought equipment on January 3 of this year for P100,000. At the time of purchase, the equipment was estimated to have a useful life of nine years and a trade-in-value of P10,000 at the end of nine years. Using the straight -line method, the amount if one year's depreciation is

- a. P11,110.
- b. P12,220.
- c. P90,000.
- d. P10,000.
- e. P20,000.

7. Which of the following accounts is not adjusted?

- a. Accumulated Depreciation

- b. Depreciation Expense
- c. Owner's Capital
- d. Prepaid Insurance
- e. Salaries Payable

8. If equipment cost P200,000 and accumulated depreciation amounts to P60,000, the book value of the equipment is

- a.P260,000
- b.P60,000
- c. P140,000
- d. P200,000

9. Failure to record the entry for accrued salaries result

- a. Profit Being Understated.
- b. Salaries Expense being understated.
- c. Salaries payable being overstated.
- d. Total assets being overstated.
- e. Total assets being understated.

10. The balance in the Prepaid Insurance account before adjustment at the end of the year is P7,200, which represents twelve months' insurance purchased on December 1. The adjusting entry required on Dec. 31, 2014 is

- a. Debit Insurance Expense, P600; Credit Insurance Payable, P600.
- b. Debit Insurance Expense, P600; Credit Prepaid Insurance, P600.
- c. Debit Insurance Expense, P6,600; Credit Prepaid Insurance, P6,600.
- d. Debit Prepaid Insurance, P600; Credit Insurance Expense, P600.
- e. Debit Prepaid Insurance, P7,200; Credit Insurance Expense, P7,200.

11. A business pays weekly salaries of P200,000 on Friday for five-day week ending on that day. If the fiscal period ends on Wednesday, the adjusting entry is

- a. Debit salaries Expense, P120,000; Credit Salaries Payable, P120,000.
- b. Debit Salaries Expense, P120,000; Credit Withdrawals, P120,000.
- c. Debit Salaries Payable, P120,000; Credit Salaries Expense, P120,000.
- d. Debit Withdrawals. P120,000; Credit Salaries Payable, P120,000.
- e. None of these.

12. An adjusting entry must contain

- a. A balance sheet account and an income statement account.
- b. An asset account and a liability account.
- c. An asset account and an expense account.
- d. Two balance sheet accounts.

e. Two income statement accounts.

13. The entry to record expired insurance is omitted. This error causes

- a. Assets to be overstated.
- b. An increase in liabilities on the balance sheet.
- c. Expenses to be overstated.
- d. Liabilities to be overstated.
- e. Liabilities to be understated.

14. If an accountants fails to make an adjusting entry at the end of a fiscal period to record expired insurance the omission will cause

- a. Liabilities to be overstated.
- b. Liabilities to be understated.
- c. Total assets to be understated.
- d. Total expense to be understated.

Multiple Choice

1. Sales revenue should be recognized when goods and services have been supplied; costs are incurred when goods and services have been received.

Which accounting concept governs the above?

- A. The substance over form concept
 - B. The materiality concept
 - C. The accrual concept
 - D. The duality concept

2. A sale should be recognized when the goods or services have been provided rather than when the sale is agreed. Which accounting concept does this illustrate?
 - A. The realisation concept
 - B. The consistency concept
 - C. The going concern concept
 - D. The materiality concept

3. The concept of going concern can only be applied to a firm when it:
 - A. is not expected to incur losses in the foreseeable future.
 - B. will never go bankrupt.
 - C. is expected to continue in business for the foreseeable future.
 - D. is not expected to be able to continue its operations.

4. The accrual concept:

- A. applies to revenues and expenses only.
- B. applies to assets and liabilities only.
- C. applies to revenues, expenses, assets and liabilities.
- D. is not a fundamental accounting concept.

5. What are the distinctive features of accrual accounting and cash-basis accounting?

- A. Cash-basis accounting records all transactions.
- B. Accrual accounting records only receivables, payables, and depreciation.
- C. Accrual accounting is superior because it provides more information.
- D. All of the above are true.

6. The revenue principle says

- a. Divide time into annual periods to measure revenue properly.
- b. Record revenue and expenses in order to compute profit.
- c. Measure revenues and expenses in order to compute profit.
- d. Record revenue only after you have earned it.

7. Adjusting the account is the process of

- a. Zeroing out account balances to prepare for the next period.
- b. Subtracting expenses from revenues to measure profit.

- c. Recording transactions as they occur during the period.
- d. Updating the accounts at the end of the period.

8. Which types of adjusting entries are natural opposites?

- a. Prepaid and Accruals
- b. Expenses and Revenues
- c. Prepaid and Depreciation
- d. Profit and Loss

9. Assume that the weekly payroll of Merla tampipi Travel is P30,000. Dec 31, end of the year on Monday , and Tampipi will pay her employee on Friday for the full week. What adjusting entry will Tampipi make on Monday, Dec. 31?

- a.

Salaries Expense	24,000	
Cash		24,000
- b.

Salaries Expense	6,000	
Salaries Payable		6,000
- c.

Salaries Payable	30,000	
Salaries Expense		30,000
- d. No adjustment is needed because the entity will pay the payroll on Friday.

10. Joseph Collado Gym gains a client who prepays P6,000 for a package of six physical training sessions. Joseph Collado Gym collects the P6,000 in advance and will provide the training later. After two training sessions, what should Joseph Collado Gym report on its income statements?

- a. Cash of P4,000
- b. Service Revenues of P2,000
- c. Service Revenues of P6,000
- d. Unearned Service Revenues of P2,000

11. Unearned Revenues is always a (an)

- a. Asset
- b. Revenues
- c. Liability
- d. Owner's equity because you collected the cash in advance

12. Assume you prepay Joseph Collado Gym for aa package of six physical training sessions. Which type of account should you have in your records.

- a. Prepaid Expense
- b. Accrued Expense.
- c. Accrued Revenues
- d. Unearned Revenues

13. The adjusted trial balance shows

- a. Amounts that may be out of balance
- b. Revenues and expenses only

- c. Amounts ready for the financial statements
- d. Assets, liabilities and owner's equity only

Multiple Choice

1. Which of the following is not an application of accrual accounting?
 - a. Adjusting the accounts?
 - b. Applying the cash basis of accounting
 - c. Applying the matching rule
 - d. Recognizing revenues when earned and expenses when incurred

2. The matching rule is applied
 - a. Because it is required by the Tax Code.
 - b. By Expensing certain items immediately and in their entirety.
 - c. To help make the bookkeeper's job easier.
 - d. To help produce a more accurate measurement of an entity's performance.

3. The going concern assumption is not applied to
 - a. Entities about to file for bankruptcy.
 - b. Entities that have been in existence for less than a year.
 - c. Entities that have sustained losses for the previous two years.
 - d. The partnership form of business.

4. A service vehicle might be depreciated over 5 years because

- a. Income tax provisions require depreciation over the next 5 years.
- b. It will be paid for in 5 years.
- c. It will help generate revenue for the company over the next 5 years.
- d. It will lose most of its market value in 5 years.

5. The journal entry to record an accrued expense results in which of the following type of accounts being debited and credited?

- a. Asset and Income
- b. Asset and Liability
- c. Expense and Asset
- d. Expense and Liability

6. If a P2,500 adjustment for depreciation is omitted, which of the following financial statement errors will occur?

- a. Assets will be understated
- b. Expense will be overstated
- c. Owner's Equity will be overstated
- d. Profit will be understated

7.

7. The amount of accrued but unpaid expenses at the end of the period is both an expense and

- A. A deferral.
- B. A liability.
- C. An asset.
- D. An income.

8. Accrued revenues

- A. decrease assets.
- B. decrease liabilities.
- C. increase assets.
- D. increase liabilities.

9. Accrued expenses

- A. decrease assets.
- B. decrease liabilities.
- C. increase assets.
- D. increase liabilities.

10. The word “accrued” implies which of the following?

- A. Money has been paid and the service has been provided.
- B. Money has been paid but no services have been provided.
- C. Money has been paid for a service to be performed during the next period.
- D. Money has not been paid or received but the service has already been performed or rendered.

11. If an adjusting entry were not made at the end of a period to remove the earned revenue from the Unearned Revenues account,

- A. assets would be understated.

- B. liabilities would be overstated.
- C. liabilities would be understated.
- D. owner's equity would be overstated.

12. Which of the following transactions results in an increase in revenues?

- A. Collection of cash on account
- B. Receipt of cash from bank loan
- C. Sale of land at cost for cash
- D. Services rendered on credit

13. The cost of doing business is also known as

- A. A liability
- B. An asset
- c. An expense
- d. Revenue

14. An item that represent services received by the firm for which it will pay for in the future called

- a. An accrued expense.
- b. An accrued revenue.
- c. An unearned revenue.
- d. A prepaid expense.

15. An item represents services provided by a firm for which it will receive payment in the future is called

- a. A prepaid expense.
- b. An accrued expense.
- c. An accrued revenue.
- d. An unearned revenue.

16. Which of the following is an example of an adjusting entry?

- a. Recording depreciation expense on a truck.
- b. Recording the billing of customers for services rendered.
- c. Recording the payment of salaries to employees.
- d. Recording the purchase of supplies on account.

17. Which of the following transactions results in an increase in expenses?

- a. Cost of employee salaries.
- b. Payment on accounts payable.
- c. Purchase of office equipment on credit.
- d. Repayment of principal of bank loan.

18. Which of the following pairs of accounts would not appear in the same adjusting entry?

- a. Interest revenue and interest payable.
- b. Rent expense and Rent payable

- c. Service revenue and Accounts Receivable
- d. Service revenue and Unearned revenues

19. The supplies account had a P2,800 debit balance at the end of the accounting period before adjustment for supplies used, and an inventory of P600 worth of unused before adjustment for supplies was on hand. Which of the following is the required adjusting entry?

- a. Debit supplies expense P600 and credit supplies P600.
- b. Debit supplies P600 and credit Supplies P600.
- c. Debit supplies P2,200 and credit supplies expense P2,200.
- d. Debit supplies expense P2,200 and credit supplies P2,200.

20. A law firm began November with office supplies of P16,000. During the month, the firm purchased supplies of P29,000. On the November 30, supplies on hand totalled P21,000. Supplies expense for the period is

- a. P24,000
- b. P29,000
- c. P45,000
- d. P21,000

21. The adjusting entry to accrue salaries expense

- a. Debits salaries expense and credits cash.
- b. Debits salaries expense and credits salaries payable.
- c. Debits salaries payable and credits cash.

d. Debits salaries payable and credits salaries expense.

22. Adjusting entries involve

- a. At least one real and one nominal account.
- b. Only capital accounts.
- c. Only nominal accounts.
- d. Only real accounts.

23. A prepaid expense is not an

- a. Asset.
- b. Economic resource.
- c. Depreciation.
- d. Deterioration

24. The decrease in usefulness of property and equipment as time passes is called

- a. Consumption.
- b. Contra asset.
- c. Depreciation.

d. Deterioration.

25. Accumulated Depreciation is reported in the

- a. Balance sheet.
- b. Income statement
- c. Statement of owner's equity
- d. Both a and b

26. Under the revenue recognition principle, revenue is recorded.

- a. After it has been earned, but not before.
- b. At the earliest acceptable time
- c. At the end of the accounting period.
- d. At the least acceptable time.

27. The broad classification of adjusting entries are

- a. Accruals and closing
- b. Accruals and deferrals.
- c. Closing and trails.

d. Trials and deferrals.

28. On Nov. 15, 2014, cash is received in advance of rendering services. Assuming that the services have been performed by Dec. 31, 2014, the adjusting entry would be a debit to

- a. Cash and a credit to service revenues.
- b. Service revenues and a credit to accounts receivable.
- c. Unearned revenues and a credit to cash.
- d. Unearned revenues and a credit to Service Revenues.

29. Which of the following pairs of accounts could not be included in the same adjusting entry?

- a. Interest Expense and Interest receivable
- b. Rent expense and rent payable.
- c. Salaries expense and salaries payable
- d. Unearned revenues and service revenues.

30. Which of the following is an example of an accrual?

- a. Payment of two years' insurance in advance.
- b. Salaries incurred but yet paid
- c. The purchase of office supplies.

d. Tuition revenue collected in advance

31. An adjusted trial balance is prepared to

- a. Both test that the ledger is still in balance after the accounts have been adjusted and facilitate preparation of the financial statements.
- b. Facilitate preparation of the adjusting entries.
- c. Facilitate preparation of the financial statements.
- d. Test that the ledger is still in balance after the accounts have been adjusted.

32. Which of the following accounting would normally be found on the credit side of the adjusted trial balance?

- a. Accumulated depreciation-Equipment
- b. Depreciation Expense-Equipment.
- c. Janet Matuguinas, Withdrawals
- d. Prepaid Insurance

33. Which of the following is not application of accrual accounting?

- a. Adjusting unearned advertising revenue to the proper balance at the end of the month
the month.

- b. Recording advertising revenues at the time the cash payment is received.
- c. Recording advertising revenues at the time the work is done.
- d. Recording telephone expense when the monthly bill is received.

34. Which of the following accounts is an income statement account?

- a. Account Receivable
- b. Owner's Capital
- c. Salaries Expense
- d. Salaries Payable

35. Which of the following is an example of a deferral?

- a. Legal fees already earned but not yet collected
- b. Property taxes accrued but not yet paid
- c. The accumulation of interest in a bank account
- d. The purchase of an entity vehicle

36. Which of the following situations involve a deferral?

- a. Recording accrued interest

- b. Recording depreciation
- c. Recording unrecorded revenue
- d. Recording unrecorded salaries

37. Which of the following accounts is a contra account?

- a. Accumulated Depreciation-Office Equipment
- b. Depreciation Expense-Equipment
- c. Office Equipment
- d. Unearned revenues

38. Which of the following situations is an example of an accrual?

- a. Recording depreciation
- b. Recording supplies consumed
- c. Recording the portion of prepaid rent that has expired
- d. Recording unrecorded revenues

40. Failure to adjust for accrued salaries at the end of the period will result in an

- a. Overstatement of Assets.

- b. Overstatement of Liabilities
- c. Overstatement of profit for the period.
- d. Understatement of profit for the period.

41. Companies usually choose a fiscal year that end

- a. At different time each year, depending on the tax consequences.
- b. During the peak of the busy season.
- c. During the slack season.
- d. on July 31.

42. Expenses are incurred

- a. Only during the adjustment process.
- b. To generate revenue
- c. To produce assets
- d. To produce liabilities

43. The matching rule relates the least to

- a. Accrual accounting

- b. Cause-and-Effect relationships
- c. Systematics and rational allocation
- d. The cash of accounting

44. Which of the following assets is not subject to depreciation?

- a. Art equipment
- b. Computers
- c. Land
- d. Store fixtures

45. The carrying value of a depreciable asset equals

- a. The estimated amount for which the asset could be sold.
- b. The estimated cost to replace the asset
- c. The original cost minus accumulated depreciation
- d. The original cost minus depreciation expense for the current period.

46. Which of the following transactions is the most difficult to assign to specific time periods?

- a. The accrual of Interest

- b. The expiration of Insurance
- c. The incurrence of salaries
- d. The use of equipment

47. Financial statement time periods should be of equal length

- a. And should correspond with the calendar year.
- b. And should end during the peak season.
- c. To comply with loan agreements.
- d. To make comparison meaningful

48. An entity recorded office supplies in an asset account when the supplies were purchased. Failure to take an inventory and make an adjusting entry will result in an

- a. Overstatement of owner's equity
- b. Understatement of assets.
- c. Understatement of liabilities
- d. Understatement of owner's equity

49. Which of the following is an application of accrual accounting?

- a. Depreciation a building as quickly as allowed by income tax regulations
- b. Expensing a machine in its entirety when purchased

- c. Recording revenue at the time payments is received.
- d. Recording utilities expense when the monthly bill is received.

50. An entity's weekly payroll of P5,000 is paid on Fridays. Assume that the day of the month falls on Wednesday. Which of the following is required adjusting entry?

- a. Debit Salaries Expense P3,000 and Credit Salaries Payable P3,000
- b. Debit Salaries Expense P2,000 and Credit Salaries Payable P3,000
- c. Debit Salaries Expense P3,000 and Credit Salaries Expense P3,000
- d. Debit Unpaid Salaries P3,000 and credit Salaries Payable P3,000

51. Which of the following transactions results in the recognition of an expense?

- a. Expiration of usefulness of equipment during the accounting period
- b. Payment of the principal of a loan
- c. Payment on accounts payable
- d. Withdrawal of cash by the owner

52. A customer's promise to pay for goods or services

- a. Creates a liability for the company
- b. Decrease the company's liabilities.

- c. Increase the assets of the company
- d. Increases the company's Cash account

53. The journal entry to record an accrued revenue results in which of the following types of accounts being debited and credited?

- a. Asset and and Income
- b. Asset and Liability
- c. Expense and Asset
- d. Expense and Liability

54. A business received cash of P30,000 in advance for revenue that will be earned later.. That cash receipt entry debited cash and credited unearned revenues for P30,000. At the end of the period, P11,000 is still unearned. The adjusting entry for this situation will

- a. Debit revenues and credit unearned revenues for P19,000
- b. Debit revenues and credit unearned revenues for P11,000
- c Debit unearned revenues and credit revenues for P19,000
- d. Debit unearned revenues and credit revenues for P11,000

55. As the usefulness of the asset Property and Equipment expires,

- a. A liability is created
- b. An amount is transferred from one asset account to another.

- c. A related expense account is reduced
- d. The cost of the asset is allocated to an expense account

56. Which of the following account could not be credited in an adjusting entry?

- a. Interest Receivable
- b. Office Supplies
- c. Prepaid Rent
- d. Service Revenues

57. The principle difference between depreciation and most other types of express is that depreciation

- a. Can be avoided if the asset is in good condition as when it was purchased.
- b. Does not required an immediate cash outlay.
- c. Is not deductible if will cause a loss
- d. Is subject to more precise measurement

Multiple Choice

1. Which of the following events would be associated with an end-of-period adjustment?

- a. The decision to start a second production shift.
 - b. The payment of salaries and wages.
 - c. The recording of depreciation on equipment.
 - d. The transfer of staff to another department.
2. Deferred revenues should be reported as
- a. Contributed capital on the balance sheet.
 - b. Expenses on the income statement.
 - c. Income on the income statement.
 - d. Liabilities on the balance sheet.
3. Accrued revenues should be reported as
- a. Assets on the balance sheet.
 - b. Expenses on the income statement
 - c. Liabilities on the balance sheet
 - d. Reveneues on the Income statement
4. WIN.com sells one-year and two-year subscriptions for its electronic book-of-the-month download business. Subscriptions are collected in advance and credited to sales. An analysis of the recorded sales activity revealed the following:

	2014	2015
Sales	P420,000	P500,000
Less: Cancellations	20,000	30,000

Net Sales	P400,000	P470,000
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Subscriptions Expirations:

2014	P120,000	
2015	155,000	P130,000
2016	125,000	200,000
2017		<u>140,000</u>
	P400,000	P470,000

In WIN.com's Dec.31, 2015 balance sheet, the balance of unearned subscription revenues should be

- a. P470,000
- b. P465,000
- c. P400,000
- d. P340,000

5. A deferred expense should be recorded when

- a. An expense is incurred as cash is paid.

- b. A non- cash resource in consumed after cash is paid.
- c. A service is rendered before payment of cash.
- d. Cash is paid before an expense has been incurred.

6. An accrued expense should be recorded

- a. By a buyer when a service is received on payment of cash.
- b. By a seller when a service is rendered before payment of cash.
- c. When an expense is incurred as cash is paid.
- d. When an expense is incurred before cash is paid.

7. An analysis of Angelina Tagay Antiques unadjusted prepaid expense account at Dec. 31, 2015 revealed the following:

- An opening balance at P15,000 for Angelina Tagya's comprehensive insurance policy. Angelina Tagay paid an annual premium of P30,000 on July 1, 2014.
- A P32,000 annual insurance premium payment made July 1, 2015.
- A P20,000 advance rental payment for a warehouse leased for one year beginning Jan 1, 2016.

8. An accrued revenue should be recorded by a

- a. Buyer when a service is received on payment of cash.
- b. Seller when a service is rendered before the service is rendered

- c. Seller when a service is rendered before receipt of cash.
- d. Seller when a service is rendered on receipt of cash.

9. On Nov. 1, 2015, Alevir Pido Portraits paid P36,000 to renew its insurance policy for 3 years. On Dec 31, 2015, Alevir Pido's unadjusted trial balance showed a balance of P900 for prepaid insurance and P44,100 for insurance expense. What amount should be reported for prepaid insurance and insurance expense in Alevir Pido's Dec 31, 2015 financial statements?

<u>Prepaid Insurance</u>	<u>Insurance Expense</u>
a. P33,000	P12,000
b. P34,000	P12,000
c. P34,000	P11,000
d. P34,000	P10,100

10. An entity that pays employees every two weeks has paid workers P375,000 in wages and salaries for work completed during 2014. In addition, the employees earned one week's salary of P7,200 at the end of December that will be paid as part of the P14,400 payroll at the end of first week of January in 2015. How much should the company report for salaries and wages expense 2014?

- a. P367,800
- b. P375,000
- c. P389,400
- d. P382,200

11. Deferred expenses should be reported as

- a. Assets on the balance sheet
- b. Expenses on the income statement
- c. Income on the income statement
- d. Liabilities on the balance sheet

12. Accrued expenses should be reported as

- a. Assets on the balance sheet
- b. Expenses on the income statement
- c. Liabilities on the balance sheet
- d. Revenues on the income statement

13. Robert Orcajada Realty pays commissions to its sales staff at the rate of 3% of net sales. Sales staff are not paid salaries but are given monthly advances of P15,000. Advances are charged to commission expense, and reconciliations against commissions are prepared quarterly. Net sales for the year ended Mar. 31, 2015 were P15,000,000. The unadjusted balance in the commissions expense account on March 31, 2015 was P400,000. March advances were paid on Apr. 3, 2015.

In its income statement for the year ended Mar. 31, 2015, what amount should Roberto Orcajada report as commission expense/

15. Salaries Payable were P3,500 at the end of September and P2,800 at the end of October. Salaries Expense for October was P18,000. How much cash was paid for salaries during October?

- a. P18,700
- b. P24,100
- c. P17,300
- d. P11,700

16. An adjusting entry can include a debit to a(n)

- a. Asset and a credit to a liability
- b. Expense and a credit to a revenue
- c. Liability and a credit to a revenue
- d. Revenue and a credit to an asset

17. The adjustment for that portion of revenue received in advance which now has been earned is to debit.

- a. Cash and credit unearned revenues
- b. Service revenues and credit unearned revenues
- c. Unearned revenues and credit cash
- d. Unearned revenues and credit service revenues

18. Which of the following transactions during the year would most likely not need an adjusting entry at the end of the period?

- a. Cash withdrawal by the owner
- b. Performance of a service that previously was paid for
- c. Purchase of a two-year insurance policy
- d. Purchase of office equipment

19. An adjusting entry cannot include a debit to a (n)

- a. Asset and a credit to a liability
- b. Asset and a credit to a revenue
- c. Expense and a credit to an asset
- d. Liability and a credit to a revenue

20. An adjusting entry made to record accrued interest on a note payable due next year consists of a debit to

- a. Interest expense and a credit to cash
- b. Interest expense and a credit to interest Payable
- c. Interest expense and a credit to notes payable
- d. Interest receivable and a credit to interest earned

21. Failure to record depreciation at year-end will result in an

- a. Overstatement of total assets
- b. Overstatement of total liabilities
- c. Understang of profit
- d. Understand of total liabilities

22. which of the following transactions will not result in an increase in revenues?

- a. Accumulation of interest in bank account
- b. An investment in the business by the owner
- c. Sale of goods in credit
- d. Sale of services for cash

23. Unearned Revenues was P6,000 at the end of February and P7,500 at the end of March. Service Revenues was P42,000 for the month of March. How much cash was received for services provided during March?

- a. P55,500
- b. P40,500
- c. P28,500
- d. P43,500

24. Failure to adjust for accrued Salaries at year-end will result in an

- a. Overstatement of liabilities
- b. Overstatement of profit

- c. Understatement of assets
- d. Understatement of owner's equity

Use the following information to answer questions 25 to 29 below. The following information pertains to Luz Un Machine Shop:

- a. Accrued interest on a note receivable amounted to P1,000
- b. A one-year insurance policy was purchased for P20,000. Three months have passed since the purchase.
- c. Depreciation on buildings is at P50,000
- d. The company received a P36,000 advance payment during the year on services still to be performed. By the end of the year, one-fourth of the services had been performed.

The company's Supplies account showed a beginning debit balance of P2,000 and supplies purchased of P8,000; P3,000 o

Problem #1

Identification of the Types and Effects of Transactions

- a. Received cash investments from the owner
- b. Paid cash on accounts payable
- c. Received cash advance for services to be provided in the future
- d. Incurred operating expenses on account
- e. Bought land for cash
- f. Acquired office equipment for cash
- g. Performed services on account
- h. Paid cash advance for rental of office space
- i. Adjusted books to reflect the amount of expired prepaid rent during the period
- j. Performed services for cash
- k. Paid cash for operating expenses
- l. Recorded accrued salaries
- m. Owner made cash withdrawals from the business

- n. Collected cash from accounts receivable
- o. Recorded depreciation expense on office equipment
- p. Purchased a building with cash and issued a note payable
- q. Paid cash for salaries accrues in a prior period

Required:

Indicate whether each of the above transactions is a source of assets (SA), use of assets (UA), exchange of asstes (EA), or exchange of claims (EC) transactions. For each transaction, indicate whether the assets, liabilities or owner’s equity increased (+), decreased (-) or did not change (0) by placing the appropriate sign in the appropriate column. The first two events are recovered as examples.

Type	Assets	=	Liabilities	+	Owner’s Equity
a. SA	+		-		+
b. UA	-		-		0

Problem #2

Types of Accounts Affected

	Account	Account
	Debited	Credited
Deferrals:		
Prepaid Expenses		
Asset Method		

Expense Method	_____	_____
Depreciation	_____	_____
Unearned Revenues		
Liability method	_____	_____
Income method	_____	_____
Accruals:		
Accrued Expenses	_____	_____
Accrued Revenues	_____	_____

Required:

Complete the table by filling in the accounts to be debited and to be credited in preparing the adjusting entries.

Problem #4

Accrual of Royalties

Elisa Diaz Technologies produces computer software that Batangas Solutions sells. Diaz receives a royalty of 15 percent of sales. Batangas Solutions pays royalties to Diaz Technologies on a semi-annual basis-on May 1 for sales made in July through December of the previous year and on November 1 for sales made in January through June of the current year.

Royalty expense for Batangas Solutions and royalty income for Diaz Technologies in the amount of P600,000 were accrued on Dec. 31, 2014. Cash in the amounts of P600,000 and P1,000,000 was paid and received on May 1 and Nov. 1, 2015, respectively. Software sales during the July to December 2015 period totaled P15,000,000.

Required:

1. Calculate the amount of royalty expense for Batangas Solutions and royalty income for Diaz during 2015.
2. Record the adjusting entry that each entity made on Dec. 31, 2015.

Problem #5

Accrual of Interest Expense

Florencia Quino Forwarders borrowed P600,000 from the bank on Sept. 1, 2015. The note carried an 8% annual rate of interest and was set to mature on Feb. 28, 2016. Interest and principal were paid in cash on the maturity date.

Required:

1. What was the amount of interest expense paid in cash in 2015?

2. What was the amount of interest expense recognized on the 2015 income statement?
3. What was the amount of total liabilities shown on the 2015 balance sheet?
4. What was the total amount of cash that was paid to the bank on Feb. 28, 2016 for principal and interest?
5. What was the amount of interest expense shown on the 2016 income statement?

Problem #6

Accrual of Interest Revenue

Reynaldo San Mateo, an angel investor, decided to invest P1,200,000 excess cash in an certificate of deposit on April 1, 2014. The certificate carried an 8% annual rate of interest and a 1-year term to maturity. Interest will be withdrawn monthly (disregard tax effects).

Required:

1. What amount of income will be recognized for the year ending Dec. 31, 2014?
2. What is the effect of the adjusting entry on the accounting equation?
3. What amount of cash will be collected for interest revenue in 2014?
4. What is the amount of interest receivable as of Dec. 31, 2014?
5. What amount of cash will be collected for interest revenue in 2015?
6. What amount of interest revenue will be recognized in 2015?
7. What is the amount of interest receivable as of Dec. 31, 2015?

8. Problem #8

9. Adjusting Entries and Accounting Policy

10.

11. At the start of the year, V. Espiritu D. Mallari, and D. Ramos Service Firms, each had P75,000 of supplies on hand. The three companies use different accounting procedure for recording supplies.
- 12.
13. V. Espiritu and D. Ramos show the beginning balance in the Supplies on Hand Account, but D. Mallari reflects the beginning balance in the Supplies Expense account. V. Espiritu debits the account Supplies on Hand when supplies are acquired, while D. Mallari and D. Ramos follow the policy of debating Supplies Expense upon acquisition. Each of the three companies acquired P452,000 of supplies at various times throughout the year, and each has P96,000 of supplies on hand at year-end.
- 14.
15. Required:
16. Prepare the adjusting entry for each entity.

Problem #2

Permanent or Temporary Accounts

Classify the accounts listed below as permanent or temporary, and indicate whether or not each account is closed. Also, indicate the financial statement in which each account will appear.

Account Title	Permanent	Temporary	Closed		Balance Sheet	Income Statement
			Yes	No		
Example: Building	x			x		
a. Rent Expense						
b. Prepaid Insurance						
c. Accounts Receivable						

d. Supplies Expense					
e. Accum. Depreciation-F/F					
f. Interest Payable					
g. Service Revenues					
h. Notes Payable					
i. Depreciation Expense-F/F					

Problem #3

Extension of Account Balances to Proper Worksheet Columns

Listed below are the ledger accounts appearing in the adjusted trial balance columns of a worksheet from Elaine Joy Claudel Animators:

1. Cash _____	11. Accounts Receivable _____
2. Buildings _____	12. Interest Expense _____
3. Salaries Expenses _____	13. Interest Revenues _____
4. Mortgage Payable _____	14. Unearned Revenues _____
5. Prepaid Insurance _____	15. Office Supplies _____
6. Equipment _____	16. Withdrawals _____
7. Utilities Expense _____	17. Interest Payable _____
8. Land _____	18. Accum. Depreciate-Bldg. _____
9. Service Revenues _____	19. Rent Expense _____
10. Salaries Payable _____	20. Accounts Payable _____

Required:

On the space provided, indicate in which column of the worksheet the amount in each account would be extended by entering the following letters: a. income statement, debit; b. income statement, credit; c. balance sheet, debit; d. balance sheet, credit.

Problem #5

Comprehensive Problem

Presented below is the unadjusted trial balance of the Moises Dondoyano Information Systems for the year ended Dec. 31, 2015

Moises Dondoyano Information Systems

Unadjusted Trial Balance

Dec. 31, 2015

Cash	P	45,000	
Notes Payable		360,000	
Accounts Receivable		156,000	
Office Supplies		63,000	
Land		300,000	
Building		1,590,000	
Accumulated Depreciation-Building			P 254,000
Equipment		2,150,000	
Accumulated Depreciation-Equipment			612,000
Accounts Payable			213,000
Unearned Consulting Revenues			450,000

Dondoyano, Capital 1/1/2015		2,655,000
Dondoyano, Withdrawals	600,000	
Consulting Revenues		2,108,000
Salaries Expense	875,000	
Repairs Expense	116,000	
Miscellaneous Expense	37,000	
Totals	P6,292,000	P6,292,000

Additional Information:

- Office supplies on hand as at Dec. 31, 2015 is P21,000.
- One-third of the unearned revenues has been earned as at Dec. 31, 2015.
- Depreciation for the year amounted to P38,000 for the building and P123,000 for the equipment.
- Salaries in the amount of P14,000 have accrued at year-end.
- The notes receivable were accepted from several customers. The notes were issued on Sept. 1, 2015 and will be settled together with a 20% interest on May 31, 2016.

Required:

- Establish a ledger account for each of the account in the unadjusted trial balance.
- Journalize and post the adjusting entries.
- Prepare an adjusted trial balance.
- Prepare an income statement, a statement of changes in equity and a balance sheet.

Problem #7

Financial Statements

Indicate whether each of the following would appear on the income statement, the statement of changes in equity or balance sheet of Tressa Mortola Skincare.

<i>Item</i>	<i>Income Statement</i>	<i>Statement Of Changes In Equity</i>	<i>Balance Sheet</i>
Example: Total liabilities at the end of the year.			x
a. Supplies on hand at the end of the year.			
b. Total insurance expired during the year.			
c. Accounts receivable at the end of the year.			
d. Total revenues earned during the year.			
e. Total withdrawals by the owner.			
f. The book value of the entity's equipment.			
g. The amount of depreciation taken on equipment during the year.			
h. The cost of supplies used during the year.			
i. Owner's equity at the beginning of the year.			
j. Profit for the year.			

Problem #9

Preparation of the Income Statement and the Statement of Changes in Equity

The income and expense accounts of Nora Maniquiz Real Estate Agency, which are listed below, represent the activities for the month of June 2015.

Advertising Expense

P 163,000

Commissions Expense	475,000
Office Supplies Expense	27,000
Real Estate Revenues	1,250,000
Rent Expense	48,000
Salaries Expense	264,000
Utilities Expense	42,000
Depreciation Expense	5,000

Required:

1. Prepare an income statement for the month ended June 30, 2015.
2. On June 1, 2015, Maniquiz has a P123,000 capital balance. During the month, Maniquiz invested an additional P16,000 in the business and withdrew P250,000. Prepare a statement of changes in equity for the month ended June 30, 2015.

Problem #13

Statement of Cash Flows

- a. Cash received from sale of a building.
- b. Cash paid for salaries.
- c. Cash received for interest on a note receivable.
- d. Cash paid to acquire a new truck.
- e. Cash loaned out to a customer in the form of a long-term note.
- f. Cash received for services rendered.
- g. Cash paid for interest.

- h. Cash paid for insurance on equipment.
- i. Cash received from a debtor representing payments of principal.
- j. Cash paid out to acquire a building.

Required:

Categorized each flow as (O) for operating, (I) for investing, or (F) for financing.

Problem #14

Cash flows from Operating Activities-Indirect Method

Imara Anda Business Solutions had a profit of P330,000 in 2015. During the year, the entity had depreciation expense of P70,000. Accounts receivable increased by P110,000 and accounts payable increased by P50,000. The entity started operations in 2015 and the foregoing are the entity's only current liabilities.

Required:

Determine the net cash flows from operating activities using the indirect method.