

Chapter 36

Value added tax, columnar books of prime entry and the payroll

Learning objectives

After reading this chapter you should be able to:

- 1 explain the meaning of the key terms and concepts listed at the end of the chapter;
- 2 outline the system of value added tax (VAT) found in the UK;
- 3 show the entries in the books of prime entry and ledger in respect of VAT;
- 4 explain the purpose of columnar books of prime entry;

- 5 show the entries in columnar day books and the cash book, and the posting of these entries to the ledger;
- 6 outline the PAYE system found in the UK, prepare a simple payroll and explain its contents; and
- 7 show the journal and ledger entries relating to the items usually contained in a payroll.

Value added tax

Value added tax (VAT) is a **sales tax** that is ultimately borne by the consumer. Most businesses charge their customer with (output) VAT and buy goods and services which are subject to (input) VAT. However, these businesses do not usually suffer VAT as a cost of inputs, in that the input VAT is set off against the output VAT and periodically the difference is paid to HM Revenue and Customs or a refund obtained. Consequently, none of the items shown in the final financial statements normally includes VAT. The only exceptions to this are trade receivables and trade payables. Furthermore, there may be a current liability for VAT at the end of an accounting year that represents the difference between output and input VAT which has not been paid to HM Revenue and Customs at that date.

Various rates of VAT have existed at various times. The current standard rate in the UK is 17.5 per cent. Some products are subject to VAT at 5% (home heating oil, home electricity), some are zero rated, i.e. bear no VAT (children's clothing, farm animal feedstuffs); some businesses are exempt so that they do not charge VAT on their outputs

but do have to pay VAT on their inputs (farm businesses that specialise in animal sales). These entities are small entities that have a turnover below a government set threshold (currently (2008) the threshold for registering for VAT is £67,000 – this usually increases by about £3,000 per year).

The accounting entries for VAT are relatively straightforward in principle. When goods which are subject to VAT are purchased for cash, the price including VAT is credited in the cash book. The price including VAT is called the **gross** price. The corresponding debit consists of two entries: the cost excluding VAT is debited to the purchases account, and the amount of VAT is debited to a VAT account. The price excluding VAT is called the **net** price.

Debit: Purchases, or expense account, or non-current asset account (net amount)

Debit: VAT account/HM Revenue and Customs account (input VAT)

Credit: Cash book (with the gross amount)

Similarly, when goods that are subject to VAT are purchased on credit, the price including VAT is credited to the credit suppliers' account. The corresponding debit consists of two entries: the cost excluding VAT is debited to the purchases account, and the amount of VAT is debited to a VAT or HM Revenue and Customs account, which is essentially a personal account.

Debit: Purchases, or expense account, or non-current asset account (net amount)

Debit: VAT account/HM Revenue and Customs account (input VAT)

Credit: Credit suppliers' account (with the gross amount)

Conversely, when goods which are subject to VAT are sold on credit, the price including VAT is debited to the credit customers' account. The corresponding credit consists of two entries: the price excluding VAT is credited to the sales account, and the amount of VAT is credited to the VAT account.

- Debit:** Credit customers' account (gross amount)
- Credit:** VAT account/HM Revenue and Customs account (input VAT)
- Credit:** Sales account (with the net amount)

A simple illustration is given in Example 36.1.

Example 36.1

A. Ltd. buys goods on credit from B. Ltd. at a price of £200 plus 17.5 per cent VAT. A. Ltd. then sells these goods to C. Ltd. for £320 plus 17.5 per cent VAT. Show the ledger entries in the book of A. Ltd.

<i>B. Ltd.</i>	
	Purchases + VAT 235
<i>Purchases</i>	
B. Ltd.	200
<i>VAT</i>	

B. Ltd.	35	C. Ltd.	56
<i>C. Ltd.</i>			
Sales revenue + VAT	376		
<i>Sales revenue</i>			
		C. Ltd.	320

Periodically, the VAT account is balanced and the difference between the two sides paid to HM Revenue and Customs where this is a credit balance, or a refund obtained where there is a debit balance.

A further complication with VAT is that some businesses are classed as either **zero rated** or **exempt**. This means that they do not have to charge their customers with VAT. In the case of zero-rated businesses, they obtain a refund of the VAT that they have paid on goods and services purchased. Thus, input VAT is debited to the VAT account, and the only credit entry in this account is a cheque received from HM Revenue and Customs as a refund. However, businesses that are classed as exempt do not get a refund. In this case there is no VAT account in the ledger because the cost of goods and services purchased including VAT is simply debited to the relevant nominal account.

Columnar books of prime entry

A **columnar book of prime entry** is one which contains analysis columns. The use of analysis columns in a petty cash book was described in Chapter 14 '*The petty cash book*'. In practice, most of the other books of prime entry, namely the day books and cash book, also frequently contain analysis columns. Each is described below.

The simplest are the sales day book and sales returns day book. These often contain analysis columns relating to the different departments or types of product that the business sells. This makes it possible to compute the gross profit of each department in departmental trading account. The sales and sales returns day books also usually contain an analysis column in respect of VAT.

The purchases day book and purchases returns day book also often contain analysis columns. These may relate to the different departments or types of products. However, a more common form of columnar purchases day book contains not just credit purchases of goods for resale, but also expenses incurred on credit (e.g. the purchase of stationery) and the purchase of non-current assets on credit. Indeed, any invoice received in respect of goods or services purchased on credit is often recorded in the columnar purchases day book. The purchases and purchases returns day books also usually contain an analysis column relating to VAT.

Lastly, the cash book frequently also contains memorandum analysis columns on both the debit and credit sides. Those on the credit side are much the same as in the petty cash book. The columns on the debit side are used in the same way but obviously relate to different types of receipts. The cash book also usually contains an analysis column on each side relating to VAT.

As explained in the context of columnar petty cash books, the purpose of having analysis columns in books of prime entry is to facilitate the posting of the ledger. Each column relates to a particular type of income or expenditure such as stationery or motor expenses. Every transaction is entered in the total column and an appropriate analysis column. At the end of each calendar month the total of each analysis column is posted to the relevant account in the ledger. Thus, instead of posting each transaction to the ledger separately, income and expenditure of the same type is collected together in analysis columns and the total for the period posted to the relevant account.

Illustrations of the use of columnar day books and cash books are given in Examples 36.2 and 36.3, respectively. The latter is a continuation of the former.

Example 36.2

A. Singh is in business as a builders' merchant. The following credit transactions took place during August 20X2:

2 Aug	Purchased goods for resale from AB Ltd. for £560 plus 17.5 per cent VAT.
5 Aug	Bought stationery from CD Ltd. for £120 plus 17.5 per cent VAT.
10 Aug	Purchased fixtures and fittings for the shop from EF Ltd. for £2,000 plus 17.5 per cent VAT.
18 Aug	Sold goods to YZ Ltd. for £1,000 plus 17.5 per cent VAT.
23 Aug	Sold some old loose tools previously used in the shop to WX Ltd. for £1,600 plus 17.5 per cent VAT.
25 Aug	Returned goods costing £200 + VAT to AB Ltd. and received a credit note.
29 Aug	Returned stationery costing £40 + VAT to CD Ltd. and received a credit note.

You are required to make the necessary entries in the relevant columnar books of prime entry and the ledger.

Purchases day book (PDB)

<i>Date</i>	<i>Name of creditor</i>	<i>Total</i>	<i>VAT</i>	<i>Purchases</i>	<i>Stationery</i>	<i>Misc.</i>
20X2		£	£	£	£	£
2 Aug	AB Ltd.	658	98	560		
5 Aug	CD Ltd.	141	21		120	
10 Aug	EF Ltd.	2,350	350			2,000
		<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
		3,149	469	560	120	2,000

Sales day book (SDB)

<i>Date</i>	<i>Name of credit customer</i>	<i>Total</i>	<i>VAT</i>	<i>Sales</i>	<i>Misc.</i>
20X2		£	£	£	£
18 Aug	YZ Ltd.	1,175	175	1,000	
23 Aug	WX Ltd.	1,880	280		1,600
		<hr/>	<hr/>	<hr/>	<hr/>
		3,055	455	1,000	1,600

Purchases returns day book (PRDB)

<i>Date</i>	<i>Name of credit supplier</i>	<i>Total</i>	<i>VAT</i>	<i>Purchases</i>	<i>Stationery</i>	<i>Misc.</i>
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20X2		£	£	£	£	£	£
25 Aug	AB Ltd.		235	35	200		
29 Aug	CD Ltd.		47	7		40	
			<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
			282	42	200	40	—

The ledger

Purchases

20X2

31 Aug Total per PDB 560

Stationery

31 Aug Total per PDB 120

31 Aug Total per PRDB 40

Fixtures and fittings

10 Aug EF Ltd. 2,000

VAT

31 Aug Total per PDB 469

31 Aug Total per SDB 455

31 Aug Total per PRDB 42

AB Ltd

25 Aug Returns + VAT 235

2 Aug Purchases + VAT 658

CD Ltd.

29 Aug Stationery + VAT 47

5 Aug Stationery + VAT 141

EF Ltd.

		10 Aug	Fixtures + VAT	2,350
			<i>Purchases returns</i>	
		31 Aug	Total per PRDB	200
			<i>Sales</i>	
		31 Aug	Total per SDB	1,000
			<i>Loose tools</i>	
		23 Aug	WX Ltd.	1,600
			<i>YZ Ltd.</i>	
18 Aug	Sales + VAT	1,175		
			<i>WX Ltd.</i>	
23 Aug	Loose tools + VAT	1,880		

Note

- 1 The amount of each invoice (including VAT) shown in the total columns of the day books is posted individually to the credit customers' and credit suppliers' personal accounts in the normal way. The total of the VAT columns in each day book is posted to the VAT account. Similarly, the total of each of the other analysis columns in the day books is posted to the relevant ledger account. The only exception to this is the miscellaneous column, where each entry would often have to be posted separately because they normally involve more than one ledger account.

Example 36.3

A. Singh had the following cheque receipts and payments during September 20X2:

1 Sep	Balance at bank £8,000.
3 Sep	Introduced additional capital of £900.
7 Sep	Sold goods for £400 plus 17.5 per cent VAT.
12 Sep	Received a cheque from YZ Ltd. for £1,140 after deducting £35 cash discount.
20 Sep	Drawings £250.
22 Sep	Purchased goods for resale costing £320 plus 17.5 per cent VAT.
23 Sep	Bought stationery costing £200 plus 17.5 per cent VAT.
25 Sep	Purchased a motor vehicle for £5,000 plus 17.5 per cent VAT.
27 Sep	Paid AB Ltd. £398 after deducting £25 cash discount.
29 Sep	Paid HM Revenue and Customs the VAT outstanding at the end of August 20X2 of £28.

You are required to make the necessary entries in a columnar cash book and the ledger.

The columnar cash book (debit side) (CB)

<i>Date</i>	<i>Details</i>	<i>Total</i>	<i>VAT</i>	<i>Credit</i>	<i>Discount</i>	<i>Sales</i>	<i>Misc.</i>
				<i>customers</i>	<i>allowed</i>	<i>revenue</i>	
20X2		£	£	£	£	£	£

1 Sep	Balance b/d	8,000					8,000
3 Sep	Capital	900					900
7 Sep	Sales revenue	470	70			400	
12 Sep	Y Ltd.	1,140		1,140	35		
		<u>10,510</u>	70	1,140	35	400	8,900

The columnar cash book (credit side) (CB)

<i>Date</i>	<i>Details</i>	<i>Total</i>	<i>VAT</i>	<i>Credit suppliers</i>	<i>Discount received</i>	<i>Purchases</i>	<i>Stationery</i>	<i>Misc.</i>
		£	£	£	£	£	£	£
20 Sep	Drawings	250						250
22 Sep	Purchases	376	56			320		
23 Sep	Stationery	235	35				200	
25 Sep	Motor vehicles	5,875	875					5,000
27 Sep	AB Ltd.	398		398	25			
29 Sep	HM Revenue and Customs	28	28					
	Totals	<u>7,162</u>	<u>994</u>	<u>398</u>	<u>25</u>	<u>320</u>	<u>200</u>	<u>5,250</u>
30 Sep	Balance c/d	3,348						
		<u>10,510</u>						

The ledger

<i>Capital</i>					
			20X2		
	3 Sep	Bank		900	
<i>Sales revenue</i>					
	31 Aug	Total per SDB		1,000	
	30 Sep	Total per CB		400	
<i>YZ Ltd.</i>					
18 Aug	Sales + VAT	1,175	12 Sep	Bank	1,140
			12 Sep	Discount allowed	35
		<u>1,175</u>			<u>1,175</u>
<i>Discount allowed</i>					
30 Sep	Total per CD	35			
<i>Drawings</i>					
20 Sep	Bank	250			
<i>Purchases</i>					
31 Aug	Total per PDB	560			
30 Sep	Total per CD	320			
<i>Stationery</i>					
31 Aug	Total per PDB	120	31 Aug	Total per PRDB	40
30 Sep	Total per CB	200			
<i>Motor vehicles</i>					

25 Sep	Bank	5,000		
<i>AB Ltd.</i>				
25 Aug	Returns + VAT	235	2 Aug	Purchases + VAT
				658
27 Sep	Bank	398		
27 Sep	Discount received	25		
		658		658
		658		658
<i>Discount received</i>				
			30 Sep	Total per CB
				25
<i>VAT</i>				
31 Aug	Total per PDB	469	31 Aug	Total per SDB
				455
31 Aug	Balance c/d	28	31 Aug	Total per PRDB
		497		42
		497		497
30 Sep	Total per CB (credit)	994	1 Sep	Balance b/d
	(including the £28 payment			28
	to HM Revenue and Customs)		30 Sep	Total per CB (debit)
				70
		994	30 Sep	Balance c/d
		994		896
1 Oct	Balance b/d	896		994

Notes

- The total of all the analysis columns on the debit side of the cash book except the discount allowed column should equal the total of the total column. Similarly, the total of all the analysis columns on the credit side of the cash book except the discount

received column should equal the total of the total column.

- 2 The total of each analysis column in the cash book is posted to the relevant ledger account. The exceptions to this are miscellaneous, credit customers' and credit suppliers' columns, where each item has to be posted to the ledger individually.
- 3 Where cheques are received from credit customers and paid to credit suppliers, the VAT included in these amounts is not shown in the VAT column of the cash book. This would result in double counting because the VAT has already been entered in the VAT account in the ledger via the VAT columns of the day books when the goods were purchased/sold. The total amount of the cheque is therefore entered in the credit customers' and credit suppliers' columns and posted to the personal accounts.

Accounting for wages

The main purpose of this section is to explain the ledger entries relating to wages and salaries, including the source of the data.

The term **wages** is usually taken to refer to payments to employees that are made weekly and/or computed using an hourly rate. The term **salaries** is usually taken to refer to payments that are made monthly and/or computed by reference to an annual remuneration. However, the distinction is not critical in that both are often entered in a wages and salaries account.

What is referred to as an employee's **gross pay** is usually computed in one of three ways:

- 1 The employee's annual salary divided by 12 if paid monthly, or by 52 if paid weekly.
- 2 On an hourly basis comprising the basic pay plus any overtime. The basic pay is the number of hours worked by an employee in a given week (excluding any overtime) multiplied by his or her hourly rate (e.g. 40 hours @ £6 per hour = £240). The overtime pay is the number of hours worked by an employee in excess of the basic hours multiplied by the hourly overtime rate, which is often something like one and a half times the basic hourly rate [e.g. 5 hours @ $(1\frac{1}{2} \times £6) = £45$]
- 3 On a piecework basis, whereby the number of units of output produced by an employee in a given week is multiplied by his or her piecework rate per unit of output (e.g. 200 units @ 1 per unit = £200).

The gross pay may also include any bonus based on some measure of performance. Bonus schemes vary considerably between businesses but a performance measure may take the form of time saved, cost reductions, profit increases, etc.

The amount of money that an employee actually receives is referred to as the **net pay**. This is the gross pay less various deductions, which in the UK include the following:

- 1 Income tax under the **Pay As You Earn (PAYE)** system. The amount, which is said to be 'deducted at source', is determined from tax tables using

the employee's tax code number, both of which are supplied to the employer by the HM Revenue and Customs.

2 National Insurance contributions (NIC). The amount of these is also determined from information supplied to the employer by HM Revenue and Customs, and usually takes the form of a given percentage of the employee's gross pay.

There may be other deductions from an employee's gross pay such as superannuation contributions to a pension fund set up by the employer.

In the UK the employer is also required to pay NIC in respect of each employee. Similarly, an employer often makes superannuation contributions on behalf of each of its employees. Neither of these is deducted from the employee's gross pay. From the employer's point of view they represent wage costs that are additional to the gross pay.

Employees' wages are computed using a document known as the **payroll**. An illustration of a payroll is given in Figure 36.1.

FIGURE 36.1 Payroll.

Payroll No.	Employee's name	Gross pay	Deductions			Net pay	Employer's NIC
			PAYE tax	NIC	Total		
		£	£	£	£	£	£
1002	J. Lennon	360	47	36	83	277	54
1003	R. Starr	240	29	24	53	187	36
1005	G. Harrson	320	38	32	70	250	48

1008	P. McCartney	380	55	38	93	287	57
		1,300	169	130	299	1,001	195

Some people regard the payroll as a book of prime entry rather than a basic document. Others argue that the ledger entries relating to wages and salaries should first be recorded in the journal.

Before examining the ledger entries it is important to understand some basic principles. The wages and salaries account (or accounts) is used to determine the total wages costs to the employer which will be charged to the income statement. This consists of the total gross pay plus the employer's NIC and any superannuation contributions it has to make. This is not immediately obvious from the ledger entries because the entries representing the gross pay take the form of the net pay and the various deductions from the employees' gross pay.

The reason why the deductions are shown separately arises from the need for a double entry to a liability account representing the employer's responsibility to pass on the deductions from the employees' pay to the appropriate authority. In the case of the PAYE income tax and NIC this is the HM Revenue and Customs.

An illustration of the ledger entries for wages and salaries is given in Example 36.4, which uses the data in Figure 36.1.

Example 36.4

Wages and salaries

	£	£		£
Bank/cash—net pay	1,001			
Inland revenue—				
PAYE tax	169			
Employees' NIC	130			
Gross pay	1,300		Income statement	1,495
Employer's NIC		195		
		1,495		1,495
		1,495		1,495

Bank/cash

	Wages and salaries	1,001
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HM Revenue and Customs

	Wages and salaries—	
	PAYE tax	169
	employees' NIC	130
	employer's NIC	195

The balance on the wages and salaries account at the end of the accounting year (i.e. £1,495) will be transferred to the income statement.

Summary

Most businesses charge their customers with (output) VAT and buy goods and services

that are subject to (input) VAT. Periodically, the input VAT is set off against the output VAT, and the difference paid to HM Revenue and Customs. Most businesses therefore neither benefit from output VAT, nor suffer input VAT. Thus, VAT is not included in any of the income, expense or asset accounts (other than trade receivables and cash) in the ledger or final financial statements. VAT is only entered in the cash/bank accounts, and personal accounts of credit customers (sales ledger) and credit suppliers (purchases ledger), with a corresponding entry in a VAT account. However, the accounting treatment of VAT in businesses that are either zero rated or exempt is slightly different.

In practice, it is common for all books of prime entry (other than the journal) to be kept in columnar form. The sales and sales returns day books may have analysis columns that relate to departments or products. So may the purchases and purchases returns day books, although it is more common for these to include columns representing the different expenses incurred on credit, and purchases of non-current assets on credit. The cash book also usually has analysis columns on each side. Those on the debit side normally relate to sales and cheques received from credit suppliers. Those on the credit side normally relate to cheques paid to credit suppliers, purchases and various expenses. The cash book and all the day books also usually have an analysis column for VAT. The purpose of columnar day books and cash books is to facilitate the periodic bulk posting of transactions of the same type to the ledger.

Employee wages are computed using a document known as a payroll. This shows each employee's gross pay, deductions in a respect of PAYE income tax and NIC, and the resulting amount of net pay. It also shows the employer's NIC. The net pay, PAYE tax

and NIC of both the employee and employer are all debited to the wages and salaries account in the ledger. The PAYE tax and NIC are credited to a liability account since these have to be paid to the HM Revenue and Customs.

Key terms and concepts

Columnar book of prime entry

Exempt

Gross pay

Input VAT

Net pay

Output VAT

Payroll

Pay As You Earn (PAYE)

Sales tax

Value added tax

Zero rated

Review questions

36.1a Briefly explain the nature of value added tax (VAT) and its

associated cash flows.

b Describe how this affects the items shown in the final financial statements of businesses.

c What does it mean when a business is classified as: (i) zero rated; and (ii) exempt for VAT purposes?

36.2a Explain the main purpose of columnar day books.

b Describe the possible format of: (i) a columnar purchases day book; and (ii) a columnar cash book. Your answer should include reference to VAT.

36.3a Briefly describe how each of the following is computed: (i) employee's gross pay; (ii) employee's net pay.

b Outline the nature of those items that are required by UK law to be deducted from employees' wages and salaries.

Exercises

36.4 Level I

The following are extracts from the payroll of J. Sutcliffe Ltd. for the week ending 24 January 20X1.

	£
Gross wages	6,800
National insurance contributions —	
employees	0,680

employers	1,020
PAYE tax	0,950

There were no other deductions from the employees' pay.

You are required to prepare journal entries to record the relevant items shown in the weekly payroll (including any cash payments).

36.5 Level I

G. Flay has three employees (A, B and C).

A gets paid £6.00 per hour and worked 35 hours normal time this week and 2 hours overtime.

B gets paid £7.00 per hour and worked 35 hours normal time this week and 5 hours overtime.

C gets paid £7.50 per hour and worked 35 hours normal time this week.

Overtime is paid at the rate of time plus 50%,

All of the employees have received income from a different activity which fully used up their tax free allowance. Therefore they are subject to income tax on the full amount earned. G. Flay deducts 20% for income tax and 11% for employee's national insurance contributions. G. Flay also has to pay employers national insurance contribution at the rate of 12.8%.

a Prepare a payroll schedule with the above information

- b** Write a journal to post the wages for the week.

36.6 Level I

Write journals to post the following transaction.

VAT is chargeable at 17.5%.

1. The purchase of a motor vehicle for £11,750 (gross) in cash.
2. The purchase of goods for £500 (net price quoted).
3. The sale of goods – net value £2,000 - for cash.
4. The sale of goods – net value £3,500 – on credit to S. Silver.

36.7 Level I

Using the information from 36.6 write up the VAT account and highlight the amount that should be paid to, or received from HM Revenue and Customs.

36.8 Level I

Mudgee Ltd. issued the following invoices to customers in respect of credit sales made during the last week of May 20X2. The amounts stated are all net of value added tax. All sales made by Mudgee Ltd. are subject to VAT at 15 per cent.

<i>Invoice no.</i>	<i>Date</i>	<i>Customer</i>	<i>Amount</i>
--------------------	-------------	-----------------	---------------

			£
3045	25 May	Laira Brand	1,060.00
3046	27 May	Brown Bros	2,200.00
3047	28 May	Penfold's	170.00
3048	29 May	T. Tyrell	460.00
3049	30 May	Laira Brand	<u>1,450.00</u>
			<u>5,340.00</u>

On 29 May Laira Brand returned half the goods (in value) purchased on 25 May. An allowance was made the same day to this customer for the appropriate amount.

On 1 May 20X2 Laira Brand owed Mudgee Ltd. £2,100.47. Other than the purchases detailed above, Laira Brand made credit purchases of £680.23 from Mudgee Ltd. on 15 May. On 21 May Mudgee Ltd. received a cheque for £2,500 from Laira Brand.

Required

- a** Show how the above transactions would be recorded in Mudgee Ltd.'s sales book for the week ended 30 May 20X2.
- b** Describe how the information in the sales book would be incorporated into Mudgee Ltd.'s double-entry system.
- c** Reconstruct the personal account of Laira Brand as it would appear in Mudgee Ltd.'s ledger for May 20X2. (AAT)

36.9 Level I

Kwella Ltd. received the following invoices from suppliers during the week commencing 23 November 20X2. All purchases made by Kwella Ltd. are subject to value added tax at 15 per cent. The following list gives the *gross* value of each invoice received.

<i>Date received</i>	<i>Invoice no.</i>	<i>Date of invoice</i>	<i>Supplier</i>	<i>Gross amount</i> £
23 Nov	GL 788	19 Nov	Glixit plc	506.00
24 Nov	899330	19 Nov	Moblin Ltd.	115.00
25 Nov	G 1101	17 Nov	S & G Gates	724.50
26 Nov	AX 1256	23 Nov	Goldrins Glues	1,115.50
27 Nov	CS 772	25 Nov	Wixit Wires Ltd.	1,794.00

On 25 November Kwella Ltd. rejected all the goods invoiced on 19 November by Moblin Ltd. (invoice no. 899330) because they were not what had been ordered. The goods were returned to Moblin Ltd. along with Kwella Ltd.'s debit note (D 56) for the full invoice amount.

On 26 November Kwella Ltd. had to return some of the goods purchased on 17 November from S & G Gates (invoice no. G1101) because they were substandard. A debit note (D 57) for a gross value of £241.50 was returned with the goods.

Required

- a Write up Kwella Ltd.'s purchases book and purchases returns book for the week commencing 23 November 20X2, totalling the columns off as at 28 November 20X2.
- b Describe how the information in the purchases book and purchases returns book would be incorporated into Kwella Ltd.'s ledger.
- c The balance brought forward on S & G Gates' account at 1 November 20X2 was £920.00, which Kwella Ltd. settled in full by cheque on 13 November after deducting 5 per cent discount. There were no transactions with S & G Gates during the month of November other than those detailed above.

Reconstruct Kwella Ltd.'s ledger account for S & G Gates for the month of November 20X2, balancing off the account as at 30 November 20X2. (AAT)

36.10 Level I

A business commenced trading for the week commencing 28 May 20X1 with £79 in cash and a bank overdraft of £515.

The following receipts and payments occurred during the week ending 3 June 20X1.

28 May Paid travelling expenses of £37 in cash.

- 29 May Paid a telephone bill of £115 (including £15 value added tax) by cheque.
- 29 May Grant Degan, a credit customer, settled an invoice for £90 paying £81 in cash and receiving £9 discount for prompt settlement.
- 30 May Made cash sales totalling £460 including £60 value added tax. The amount was received by cheque and was immediately banked.
- 31 May Paid an invoice for £100 from Gaga Ltd. by cheque for £92. £8 discount was received for prompt settlement.
- 1 June Made cash purchases totalling £115 including value added tax of £15 paying by cheque.
- 1 June Made cash sales of £230 inclusive of value added tax of £30.
- 2 June Paid staff wages of £300. This was partly paid by cheques totalling £230, the balance being paid in cash.
- 2 June Paid £200 from the till into the business bank account.

Required

- a** Draw up a cash book with separate columns for dates, narrations, folios, discount, VAT, bank and cash. Enter the opening balances and record the transactions for the week commencing 28 May 20X1. Balance the cash book as at 3 June 20X1.
- b** Describe how the totals for the Discount and VAT columns will be entered into the ledger. (AAT)

36.11 Level II

After completing a training course at a technical college, Michael Faraday set up in business as a self-employed electrician on 1 January 20X2.

He was very competent at his job, but had no idea how to maintain proper accounting records. Sometimes during 20X2 one of his friends asked Michael how well his business was doing. He replied 'All right ... I think ... but I'm not quite sure'.

In the ensuing conversation his friend asked whether he had prepared financial statements yet, covering his first quarter's trading, to which Michael replied that he had not. His friend then stressed that, for various reasons, it was vital for financial statements of businesses to be prepared properly.

Shortly afterwards Michael came to see you to ask for your help in preparing financial statements for his first quarter's trading. He brought with him, in a cardboard box, the only records he had, mainly scribbled on scraps of paper.

He explained that he started his business with a car worth £700, and £2,250 in cash, of which £250 was his savings and £2,000 had been borrowed from a relative at an interest rate of 10 per cent per annum. It was his practice to pay his suppliers and expenses in cash, to require his customers to settle their accounts in cash and to bank any surplus in a business bank account. He maintained lists of cash receipts and cash payments, of supplies obtained on credit and of work carried out for customers and of appliances sold, on credit.

The list of credit suppliers comprised:

<i>Date supplied</i>	<i>Supplier</i>	<i>Amount owed</i>	<i>Date paid</i>	<i>Amount paid</i>	<i>Remarks</i>
20X2		£	20X2	£	
Jan	Dee & Co.	337.74	Mar	330.00	Received discount £7.74
	AB Suppliers	528.20	Mar	528.20	
Feb	Simpson	141.34	Mar	138.00	Received discount £3.34
	Cotton Ltd.	427.40	Mar	130.00	Payment on account
			Apr	297.40	Remainder
	Dee & Co.	146.82	Mar	140.00	Received discount £6.82
Mar	AB Supplies	643.43	Apr	643.43	
	Simpson	95.60			Not yet paid

The purchase in January from Dee & Co. was of tools and equipment to enable him to carry out electrical repair work. All the remaining purchases were of repair materials, except for the purchase in February from Cotton Ltd., which consisted entirely of electrical appliances for resale.

In addition to the above credit transactions, he had bought repair materials for cash, as follows:

20X2	£
Jan	195.29
Feb	161.03
Mar	22.06

Other cash payments comprised:

20X2		£
Jan	Rent of premises for Jan to Jun 20X2	400.00
	Rates of premises for Jan to Mar 20X2	150.00
	Stationery	32.70
	Car running expenses	92.26
Feb	Sundries	51.54
	Car running expenses	81.42
Mar	Sundries	24.61
	Car running expenses	104.52
	Transfer to bank	500.00

He had also withdrawn £160.00 in cash at the end of each month for living expenses.

The list of credit customers comprised:

<i>Date of sale</i>	<i>Customer</i>	<i>Amount owed</i>	<i>Date received</i>	<i>Amount received</i>	<i>Remarks</i>
20X2		£	20X2	£	
Jan	D. Hopkins	362.80	Feb	357.00	Allowed discount £5.80
	P. Bolton	417.10	Mar	417.10	
Feb	G. Leivers	55.00	Mar	055.00	
	M. Whitehead	151.72	Apr	151.72	
	N. John Ltd	49.14	Apr	049.14	
	A. Linnekar	12.53	Mar	012.53	
Mar	E. Horton	462.21	Apr	462.21	
	S. Ward	431.08	Mar	426.00	Allowed discount £5.08

W. Scothern & Co.	319.12	Not yet received
N. Annable	85.41	Not yet received

The above amounts relate to charges for repair work which he had carried out, except that the amounts shown in February for G. Leivers, N. John Ltd. and A. Linnekar are for sales of electrical appliances.

In addition to the above credit transactions, he had cash takings, as follows:

20X2		£
Jan	Repair work	69.44
Feb	Repair work	256.86
Mar	Repair work	182.90
	Appliances	112.81

He estimated that, at the end of March 20X2, his inventory of electrical repair materials was £691.02 and of electrical appliances for resale was £320.58, his tools and equipment were worth £300.00 and his car was worth £600.00.

Apart from loan interest, the only accrual was for heating and lighting, £265.00.

Required

a Prepare:

- i purchase day book with analysis columns for each type of purchase; and
- ii sales day book with analysis columns for each class of business undertaken.

b Open, post to 31 March 20X2 only, and balance a columnar cash book suitably analysed to facilitate ledger postings.

c Open, post to 31 March 20X2 only, and balance a purchases ledger control

account and a sales ledger control account. Use the closing balances in your answer to (g) below.

(NB: Individual accounts for credit suppliers and credit customers are *not* required.)

- d** Open, post and balance sales and cost of sales accounts, each with separate columns for 'Repairs' and Appliances'.
- e** Prepare M. Faraday's trading account for the quarter ended 31 March 20X2, distinguishing between gross profit on repairs and on appliance sales.
- f** Prepare M. Faraday's general income statement for the quarter ended 31 March 20X2.
- g** Prepare M. Faraday's statement of financial position as at 31 March 20X2.

(ACCA)

36.12 Level II

M. Essex is in business as a wholesale coal merchant. The following transactions took place during December 20X2:

- 1 Dec Balance at bank £5,000.
- 3 Dec Purchased goods on credit from English Coal for £400 plus VAT.
- 4 Dec Received an invoice for £240 plus VAT from Solihull Garage in respect of vehicle repairs on credit.
- 5 Dec Bought stationery costing £240 plus VAT and paid by cheque.
- 6 Dec Sold goods on credit to Black for £600 plus VAT.
- 7 Dec Bought goods on credit from Scottish Coal for £320 plus VAT.

- 8 Dec Paid wages by cheque of £350.
- 10 Dec Sold goods for £520 plus VAT and received a cheque for this amount.
- 11 Dec Purchased goods costing £720 plus VAT and paid by cheque.
- 12 Dec Sold goods on credit to White for £800 plus VAT.
- 13 Dec Received an invoice for £360 plus VAT from Solihull Garage relating to motor expenses incurred on credit.
- 14 Dec Bought goods for resale costing £480 plus VAT and paid by cheque.
- 15 Dec Purchased a motor vehicle on credit from Solihull Garage costing £4,000 plus VAT.
- 16 Dec Received telephone bill from English Telecom for £560 plus VAT.
- 17 Dec Sold a motor vehicle on credit to Solihull Garage for £2,000 plus VAT.
- 18 Dec Sold goods for £640 plus VAT and received a cheque.
- 19 Dec Paid insurance premium on vehicles of £720 by cheque.
- 20 Dec Purchased stationery for £160 plus VAT by cheque.
- 23 Dec Sold on old motor vehicle for £3,000 plus VAT and received a cheque for this amount.
- 28 Dec Received a cheque from Black for £680 after deducting £25 cash discount.
- 29 Dec Received a cheque from White for £905 after deducting £35 cash discount.
- 30 Dec Paid English Coal £450 by cheque after deducting cash discount of £20.
- 31 Dec Paid Scottish Coal £346 by cheque after deducting cash discount of £30.

Required

- a** Write up the sales and purchases day books and the cash book using appropriate analysis columns where there is more than one transaction of the same type.
- b** Make the necessary entries in the ledger. Assume the rate of VAT to be 17.5 per cent.