SQuestion 1

1) **Going Concern**: This assumes that the business is going to continue to operate for the foreseeable future, and therefore assets will be available for use in future accounting period.
2) **Accruals**: When preparing the profit and loss account, revenue and profits are matched with the associated costs and expenses incurred in earning them. This means that revenues and expenses are recognized when they are incurred, rather than when the related cash is received or paid.
3) **Money Measurement**: only those events and situations that can be reasonably objectively measured in money terms are recorded.
4) **Dual Aspect**: This is the basis of double-entry bookkeeping, in that every transaction has two effects, the end result of which is that assets equal liabilities plus capital (the accounting equation).
5) **Business entity**: A business is a separate entity from its owners. Transactions of a business are recorded as they affect the business, not as they affect the owner.
6) **Cost concept**: the assets are recorded at the price paid to acquire it, that is "at cost".
7) **Realization concept**: this states that profit is only earned when there is a legal right to receive the revenue.

Question 2

Errors not-disclosed by Trial Balance:

a) **Error of omission**: occurs when a transaction is completely omitted from the book
b) **Error of commission**: occurs when one half of a transaction has been entered in the wrong account, but where the error does not affect the view given by the final accounts. i.e. correct and incorrect accounts are of the same type of accounts
c) **Error of principle:** similar to error of commission but the error affects the view given by the final accounts i.e. correct and incorrect accounts are of different type of accounts
d) **Compensating error**: occur when 2 or more errors offsetting one another.
e) **Error of original entries**: occur when wrong figure has been used for the whole transaction i.e. both debit and credit entries.
f) **Reversal of entries**: occurs when entries for a transaction are reversed.

3 accounting conventions:

a) **Materiality Convention**: An item should be regarded as material if there is reason to believe that knowledge of it would influence the decision of informed investor
b) **Prudence Convention**: it states that an accountant should include all anticipated expenses and losses but should not take into account any anticipated profits or gains. However, a possible gain if provided for but not coming through ultimately, could spell disappointment for the company.
c) **Consistency Convention**: the firm should adopt one line of action in relation to a particular situation each time the same situation occurs. If this is not done, then figures and corresponding profit or loss gets distorted. So uniformity should be maintained with regard to the principles and practices adopted or else over the years the accounts of the company will not afford a suitable base for comparison.

Question 3

Factors of depreciation:

a) **Wear and Tear**: loss in value of assets due to physical usage & natural effects.
   - E.g. building, car, equipment
b) **Obsolescence**: loss in value of assets due to technology advancement or change in demand trend and that make assets out of date.
   - E.g. fashion clothes, computer
c) **Depletion**: loss in value of assets due to the assets being depleted
   - E.g. coal mine, oil well, etc...
d) **Passage of time**: loss in value of assets due to assets have a fixed life and the value is positively related to the useful life remained
   - E.g. patent right, lease on building

3 methods of calculating depreciation:

a) **Revaluation Method:** fixed assets are valued at the end of every accounting period.

   Depreciation cost=original cost-present value (based on the evaluation of experts).

   This method used for calculating depreciation of loose tools, farmers' livestock where it is difficult to estimate with any certainty the rate at which the assets will depreciate.

b) **Straight-line method:** the fixed asset is assumed to be depreciated at equal amounts for every year of its expected lifetime. The cost of the asset is spread evenly over its lifetime.

   $$\textbf{Depreciation per annum} = \frac{\textbf{(Original cost – Estimated Scrap Value)}}{\textbf{Number of years of expected useful life}}$$

c) **Reducing Balance or Diminishing Balance method**: the asset is supposed to depreciate at a fixed % of its depreciated value at the beginning of each year. The amount set aside for deprecation will diminish with every successive period since the value of the asset at the beginning of every successive period tends to diminish.

   Depreciation cost =value of fixed assets at the beginning of the year* Fixed rate of depreciation.

Question 4

Users of accounting information:

1) **Directors/Managers:** need accounting information for making decision regarding company's strategies and to protect interest of other stakeholders.
2) **Employees:** concern with profit sharing & financial strength of company and to see how they have contribute to the company success
3) **Investors/shareholders:** need accounting info to determine risk and profitability of their investment.
4) **Creditors/Suppliers:** need to determine risks of credit given to the company.
5) **Government:**
   a) Taxation: to calculate and collect the company tax responsibilities
   b) Employment: foresee the unemployment problems of the firm and to take necessary actions to ovoid unemployment
   c) Social security: to calculate and collect social security responsibilities of the firm
   d) Industrial development: to determine the product potentials and to decide the development direction of the industry
   e) Inflation/statistic: to calculate and control inflation; to determine figures for statistic purposes.
   f) Monopoly/free trade: to prevent monopolists.

Question 5

Cash Book is a journal recording cash receipts and cash payments of the organisation.
Purchase Day Book is a journal recording purchasing transaction of the organisation.
Purchase Return Day Book is a journal recording returns of goods previously purchased by the organisation for resale.
Sales Day Book is a journal recording sale of goods and services provided by the organisation.
Sales Return Day Book is a journal recording return of goods and services provided by the organisation from the organisation's customers.

Journal vs. Ledger

Journal	Ledger
– Book of original entries	– Book of secondary entries, i.e. after entries in journal
– Prepared after accounting transaction occurs	– Prepared weekly, monthly
– Listing format	– Account format
– Serve checking purpose	– Serve calculating purpose

Question 8

- **Bank/ Finance Companies:** These organisations provide financing such as loans to the firms. They are interested in the financial statements of the firms so that they can safely determine the probability of they loans to the firms will be repaid.
- **Proprietors/Shareholders:** these are owners of the firms. They invest money into the firms to receive profit sharing. They are interested in the financial statements of the firms so that they can determine the risk and profitability of they investment into the firm.
- **Suppliers:** They supply products and services to the firm mostly on credit. They are interested in the financial statements of the firm to determine the probability of their credit will be paid in time, and sufficiently.
- **Stockbrokers:** these are people who trade (buy and sell) shares of the firm. They are interested in the financial statements of the firm to determine the demand and supply of the shares in the market so as to decide whether to trade these shares or not.

Advantages of Computerized Accounting

- The computer works many times faster than the human brain.
- The computer is very accurate-it doesn't make mistakes if programmed correctly.
- The computer can process large volumes of data.
- Large volume of data can be stored on a single disk.
- Production of reports and analysis can be done automatically.

Question 5 (9)

Why it is necessary for a firm to make a provision for depreciation of its fixed assets in its books? Name and explain three methods of calculating depreciation. What are the main advantages and disadvantages of each of these methods?

Answer

1) Fixed asset loose their value over a period which is often longer than one year. The expense due to the loss in value of assets (i.e. depreciation) therefore cannot be expressed by actual money transaction during the usage period (i.e before the assets are sold). Some methods to estimate the depreciation expense must be applied so that the expense of one year is to be provided within that year (according to the accruals concepts).

2) Three methods of calculating depreciation:

- **Revaluation Method:**

Depreciation = market value of the asset at the beginning of the year - market value of the asset at the end of the year.

This method is used mainly for assets of small value; assets that are difficult to estimate their useful life period; assets that are difficult to estimate the % of depreciation.

The main advantage is the fixed asset is shown at its current or reliable value at the end of the year in the Balance Sheet. This allows for a more realistic financial position to be expressed.

- **Straight line method**

Depreciation = Purchasing price / estimated useful life - or a fixed percentage of the purchasing price.

Depreciation is the same every year for the whole useful life period

This is the most common method for assets with long useful life such as building, equipment, machinery, warehouse etc.
The main advantage is that it is easy to calculate and easy to understand. The main advantage is that this method assumes that the fixed assets will give the same amount of service annually throughout their life time.

- **Reducing balance method**

Depreciation = a% of the value at the beginning of the year
Depreciation is higher at the beginning of usage and lower toward the end of usage.
Reducing balance method is most appropriate for assets that have short useful life or assets that depreciate quickly at the beginning of usage such as car, vehicles, computers
The main advantage of this method is that in the Profit and Loss Account, this amount of overall expenses charged for the use of a fixed asset would be more or less constant throughout the asset's lifetime.