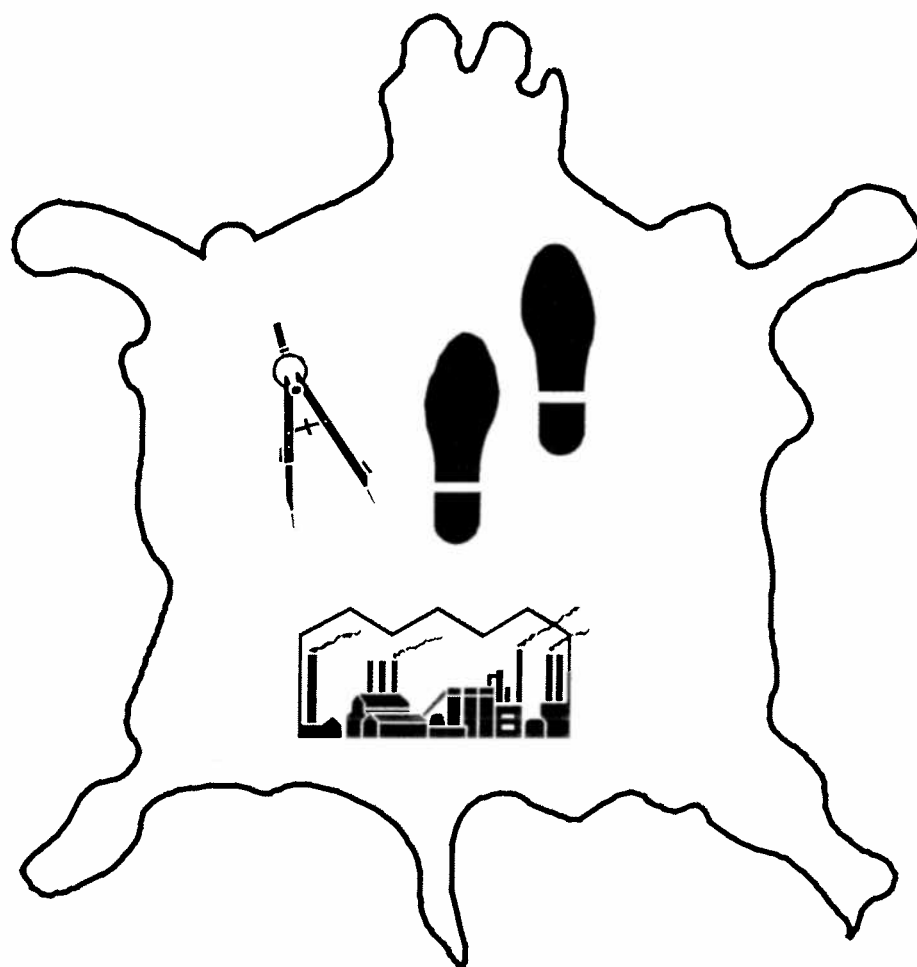


SHOE INDUSTRY CERTIFICATE COURSE



INDUSTRIAL ACCOUNTANCY*



* This document has been produced without formal editing



This learning element was developed by the UNIDO Leather Unit's staff, its experts and the consultants of the Clothing and Footwear Institute (UK) for the project US/PHI/85/109 and is a part of a complete Footwear Industry Certificate course. The material is made available to other UNIDO projects and may be used by UNIDO experts as training aid and given, fully or partly, as hand-out for students and trainees.

The complete Certificate Course includes the following learning elements:

Certificate course

- Feet and last
- Basic design
- Pattern cutting
- Upper clicking
- Closing
- Making
- Textiles and synthetic materials
- Elastomers and plastomers
- Purchasing and storing
- Quality determination and control
- Elements of physics
- General management
- Production management
- Industrial Law
- Industrial accountancy
- Electricity and applied mechanics
- Economics
- SI metric system of measurement
- Marketing
- Mathematics
- Elements of chemistry

INDUSTRIAL ACCOUNTANCY

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Mr. Mario Pantoja

INDUSTRIAL ACCOUNTANCY

I. PRINCIPLES OF ACCOUNTING

1. Purpose of keeping the records is due to the limitations of human memory makes it necessary to keep written records of almost of the everything regarding human activities.
2. Entities interested - Sole proprietorship, partnership and corporation
3. Accounting - is an art of recording, classifying, 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.
4. Definition:
 - Recording - writing the transactions and events in the book or records of the business.
 - Classifying - is the grouping or sorting of items under the same account title.
 - Summarizing - is the preparation of reports periodically either, annually, semi-annually, quarterly or monthly, regarding the status of the business as gathered from data in the accounting records.
 - Interpreting - refers to the interpretation of reports and statements (Balance Sheet & Profit & Loss) for the guidance of management due to the technical and specialized nature of accounting aided by additional supplementary reports and explanatory reports, such as analysis of working capital report.
5. Three major Accounting Elements or Values
 - 5.1 Assets - these are property or rights on property owned by the business or upon which the business has a vested equitable interest. Example; Money, Accounts Receivable, merchandise patents and copyrights.
 - 5.2 Liabilities - financial obligation or debt of the business in favor of persons or parties other than the owner/owners. Example: Taxes, accounts payable and notes payable.

- 5.3 Capital - represents the equity of owners in the property of the business after the amount of debts to outsiders is deducted or it represents the initial investment of the owners.

II. THE ACCOUNTING EQUATION

Assets = Liabilities and Capital. This is the basic foundation of modern accounting.

Method use : Is the double entry method which is the system of recording events and transactions for value received which is on the left side of the general journal and value parted with which is on the right side.

Since all transactions involved only on these three major accounting values therefore, all transactions may be grouped into nine types of effects, as follows:

- Increase in assets = increase in proprietorship
- Increase in assets = increase in liabilities
- Increase in some form of assets = decrease in some forms of assets
- Decrease in assets = decrease in proprietorship
- Decrease in assets = decrease in liabilities
- Increase in liabilities = decrease in proprietorship
- Increase in some form of liabilities = decrease in other forms of liabilities
- Increase in proprietorship = decrease in liabilities
- Increase in some forms of proprietorship- decrease in the other forms of proprietorship

2. Two Major Accounting Reports or Statements - prepare at the end of the accounting period which is any period provided it is a twelve month period, such as Calendar Year or Fiscal Year.

2.1 Balance Sheet - is an itemized statement of the assets, liabilities and proprietorship of the business which reflects the financial condition of the business at the date of preparation which is usually at the end of the accounting period.

2.2 Income Statement - is an itemized statement summarizing the changes in proprietorship resulting from the business operations between dates for the purpose of providing the owner with information regarding the progress of the business at a regular intervals.

III. DEBIT AND CREDIT

Account - is an accounting device used in summarizing the changes in the assets, liabilities and proprietorship caused by business transactions and events.

Two Accounting Books :

1. Journal - is the accounting book wherein the business transactions and events are recorded for the first time. It is called the Book of Original entry.
Parts : the date, the account title, the amounts, the folio and the explanation.

The form : 2 column general journal

2. Ledger - is the group of accounts found in the general journal.

The form: the T -Ledger

The theory of Debit and credit as applied in the accounting equation.

1. Assets - are originally on the debit side to increase it, place the amount on the left side and to decrease it place the amount on the right side, debit and credit, respectively.
2. Liabilities - are originally on the debit side to increase it, place the amount on the right side (credit) and to decrease it place the amount on the left side (debit), same with the proprietorship
3. Proprietorship - same with liabilities.

Complete Rules of Debit and Credit :

<u>Debit to</u>	<u>Credit to</u>
1. Increase on asset	1. Decrease on asset
2. Decrease a liability	2. Increase a liability
3. Decrease a capital or additional investment	3. Increase a capital or additional investment
4. Increase a withdrawal	4. Decrease a withdrawal
5. Decrease an income	5. Increase an income
6. Increase a deduction from income	6. Decrease a deduction from income

IV. JOURNALIZING AND POSTING

Chart of Accounts - is a classified list of account titles prepared for the guide to bookkeeper in the formal recording of transactions and events.

- A. Assets Titles : The following list of asset titles and brief explanations for each are almost commonly used in the study of accounting while these terms are suitable for most situations, it is not common to come across accounts bearing titles different from the following:

Cash : coins and currency owned by the business. If some of the money of the business are deposited in the bank, there may be two accounts used, namely, cash in bank and cash on hand.

Accounts Receivable : claims due from customers of the business for goods sold or for services rendered on credit. Terms used "On credit", "On accounts" or "Charge accounts".

Notes Receivable : amounts due or collectible from the customers for goods or services sold, or from others, for loans granted, when the claims are evidenced by written promises called "Promissory Notes:"

Merchandise : goods owned and unsold which were purchased by the business for resale as used by the merchandising business or enterprises.

Supplies on Hand: stationaries, pencils, pens, inks, and other supplies unused. Other titles - office supplies, store supplies and factory supplies.

Marketable Securities: Bonds or stocks issued by other concerns and acquired by the business.

Land : used for building sites or other business purposes

Buildings : owned and used by the business for office or factory

Machinery and Equipment : machines, tools, motors, or office equipment

Furniture and Fixtures : tables, desks, chairs, counters, showcases and the like.

Office Equipment : adding machines, typewriters, calculators, & others.

Delivery equipment: trucks, automobiles and other equipment used for transporting merchandise.

B. Liabilities Titles :

Accounts Payable - amounts due to other parties for merchandise or services bought but not paid.

Notes Payable - amounts due to other parties where the claims are supported by written promises (promissory note) made by the business or bill of exchange.

Taxes Payable - amount of levies on property or income due to the government.

Bonds Payable - when the business issues to the public long-term promissory notes under seal, the amount of the issue are recorded in this account.

C. . Proprietorship Titles : Refers owner's capital which includes the capital contributions of the owner or co-owners made at the inception of the business or subsequent thereto.

Owners' Drawing or Personal - is the account used for the recording of the withdrawals of capital by the owner and end-of-period closing of the profits or losses of the business.

- D. Income Titles : The titles for income vary according to the line of business carried and may be sub-divided into subtitles as it may be found necessary. Titles enumerated below are the terms commonly used to designate income.

Sales or merchandise sold - represents the total sales price of the merchandise sold.

Revenue from fees - is the appropriate title for use by professionals like lawyers, industrial engineers, doctors and accountants in the exercise of their professions.

Rent Income - this account absorbs the amounts of rental earned on the properties of the business.

Service Income - this is the appropriate title for income of enterprises, selling services instead of merchandise.

Interest Income - amount earned for the lending of money like banks and other financial institutions.

- E. Deduction from Income Titles : Deductions from income are the costs, expenses and losses.

Cost of Sales or cost of goods sold - this shows the purchase price or the manufacturing cost of the goods sold.

Advertising expense - this includes promotional expenses in connection with the propagandizing of the products.

Salesmen's salaries - fixed wages given to salesmen or sales agents

Salesmen's commissions - compensations granted to salesmen which are usually computed or based on the amount of their sales.

Postage and communication - expenses of postage and other means of communication.

Office salaries - wages of employees connected with the administration of the business.

Supplies expense - cost of supplies used.

Taxes - amount of taxes incurred by the business

Utilities expense - cost of light and water consumed by the business

Insurance expense - premiums on insurance policies paid and incurred by the business.

Repairs and Maintenance - expenses for repairing or servicing the building

Rent expense - amount paid or incurred for the use of properties.

Depreciation expense - is the allocation of expense portion of the fixed assets like building which deteriorated due to wear and tear of the same because of ordinary used.

Interest expense - sum added to the principal of money obligations.

Posting - is the process of transferring to the ledger the same information recorded in the journal.

Trail Balance - is a list of all the accounts with open balances in the general ledger.

Simple Worksheet and Simple Financial Statements

Worksheet - is an analysis paper bridging the trial balance to the financial statement which facilitates the preparations of the individual balance sheet and profit and loss statement.

Two Classes of Balance Sheet : Account Form
Report Form

V. CLASSIFICATION OF ACCOUNT IN BALANCE SHEET

A. Assets Account :

1. Current Assets - include cash and other assets which are to be converted into cash within a reasonable period of time from the balance sheet date without interruption from the regular operations of the business.

Example: Cash, merchandise, prepaid expenses
and account receivable.

2. Fixed Assets - include capital assets of more or less permanent nature acquired for use rather than for resale.

Example: Land, Building

B. Liabilities Account :

1. Current liabilities - include debts maturing within the next year from the balance sheet date.

Example: notes payable
accounts payable

2. Fixed liabilities - include debts maturing generally beyond next year.

Example: long-term notes payable
bonds payable
mortgage payable

Closing of the books or the ledger - is the process of transferring all the temporary proprietorship accounts or nominal accounts in the profit and loss statement to the capital account at the end of the accounting period usually a year. The closing entries are recorded in the general journal and posted to the ledger.

In the closing process the individual income and expense account are first transferred or summarized to the Revenue and Expense Account. Then the net balance of the Revenue and Expense account is transferred to the owner's capital account.

The closing process involves the following procedures:

1. Debit revenue and expense account and credit all nominal accounts with debit balances.
2. Credit Revenue and Expense account and debit all nominal accounts with credit balances.
3. Close to capital account the net balance of the Revenue and Expense account after entries in Nos. 1 and 2 above.

Post Closing Trial Balance - is prepared after the accounts are ruled after the closing entries are made to prove the equality of the debits and credits of the accounts remaining with open balances in the ledger as contained in the balance sheet.

VI. MERCHANDISE ACCOUNTS

1. Nature of Merchandise business - is one engaged in the buying and selling of goods or merchandise in the same form for profit.
2. Activities covered:
 - 2.1 Purchasing - refers to the cost of goods bought which borne part of the merchandise inventory for an unsold goods.
 - 2.2 Handling - refers to the costs of transportation in bringing the purchases (freight in) is part of purchases.
 - 2.3 Returned of goods purchased - refers to defective or unsatisfactory merchandise received which is returned to the seller or an allowance is given.
 - 2.4 Selling - refers to the selling of goods purchased above the cost price for an adequate margin of profit.
 - 2.5 Returned of goods sold - refers to merchandise returned by the customer which are defective or unsatisfactory for which an allowance is given.
 - 2.6 Merchandise Inventory - refers to maintaining adequate stock on hand.

3. Merchandise Accounts

The following are the merchandise accounts usually employed for trading concerns:

- 3.1 Sales Account - sales of merchandise are recorded in this account at selling prices. This account is credited.
- 3.2 Sales returns account - this account is debited for the merchandise returned by customers.
- 3.3 Sales Allowances account - when the goods delivered to a customer are found to be defective or not as ordered and the purchase desires to retain the goods as is, the customer is permitted to deduct a certain amount from the selling prices of the goods delivered. This account is debited.
- 3.4 Purchase account - this is a temporary account to which the cost of goods bought during the period is debited. This account has usually a debit balance at the end of the period.
- 3.5 Purchase Returns account - goods bought and returned to the supplier or creditor are credited to this account at invoice price.
- 3.6 Purchase Allowances account - goods bought and received as defective, or not as ordered, when not returned to the supplier, may be subject to certain reductions from their acquisition prices. This account is credited.
- 3.7 Freight and Cartage in account - if the buyer pays the expenses of transporting the goods from the place of the seller to the place of the buyer, such expenses are debited to the Freight and Cartage In account.
- 3.8 Merchandise Inventory - at the end of every accounting period a physical count of the unsold merchandise on hand is taken. This account is debited.

A N N E X

Trade discounts and Cash discounts illustrated :

1. Assume a credit invoice of ₱1,000.00 Terms: 2/10, n/30

List price	₱1,000.00
Less: Trade discounts-20%	<u>200.00</u>
	₱ 800.00
Less: Cash discount -2%	<u>16.00</u>
Amount due if paid within 10 days,	₱ 784.00

2. Cost of Sales: At the end of the accounting period, a trading concern should determine the cost of the merchandise it has sold for the period. This is called the Cost of Sales or Cost of Goods Sold. The cost of goods sold is deducted from the total net sales in order to arrive at the amount of gross profit on sales.

Computations of Cost of Sales are hereunder illustrated with the following assumed figures.

Case A. Purchase during the year 19A	₱ 100,000.00
Merchandise Inventory, Dec. 31, 19A	<u>30,000.00</u>

Cost of Sales is computed as follows:

Purchases	₱ 100,000.00
Less: Merchandise Inventory, Dec. 31, 19A	<u>30,000.00</u>
Cost of Sales	<u>₱ 70,000.00</u>

- Case B. Assuming that in the year 19B, the following additional facts apply: (Note: This is a continuation of Case A)

Purchases during 19B	₱ 150,000.00
Merchandise unsold, Dec. 31, 19B	<u>70,000.00</u>

Cost of Sales for the year 19B is computed as follows:

Merchandise Inventory, Jan. 1, 19B	₱ 30,000.00
Add: Purchases	<u>150,000.00</u>
	₱ 180,000.00
Less: Merchandise Inventory, Dec. 31, 19B	<u>70,000.00</u>
Cost of Sales	₱ 110,000.00

Case C. Assume the following facts for the year 19C

Merchandise Inventory, Jan. 1, 19C	P 70,000.00
Purchases during 19C	120,000.00
Freight In	3,000.00
Purchase Returns and Allowances	8,000.00
Purchase Discounts	500.00
Merchandise remaining unsold on Dec. 31, 19C	60,000.00

Cost of Sales for 19C is computed as follows:

(1) If discounts are shown as deductions from purchases -

Merchandise Inventory, Jan. 1, 19C	P 70,000.00
Add: Purchases	P 120,000.00
Freight In	3,000.00
	<u>P 123,000.00</u>

Less:

Purchase Returns & Allowances	P 8,000.00
Purchase Discounts	500.00
	<u>P 8,500.00</u>
	P 114,500.00
Goods Available for Sale	P 184,500.00
Less: Merchandise Inventory, Dec. 31, 19C	60,000.00
Cost of Sales	<u><u>P 124,500.00</u></u>

(2) If discounts are not treated as deductions from purchases -

Merchandise Inventory, Jan. 1, 19C	P 70,000.00
Add: Purchases	P 120,000.00
Freight In	3,000.00
	<u>P 123,000.00</u>
Less: Purchase Returns & Allowances	8,000.00
	<u>P 115,000.00</u>
Goods available for sale	185,000.00
Less: Merchandise Inventory, Dec. 31, 19C	60,000.00
Cost of Sales	<u><u>P 125,000.00</u></u>

Illustrative Problem for a Trading Concern:

The transactions of A. Arias for the month of Decmmber 19A, were the following:

December

1. Started business under the name of Arias Trading with investments of cash of ₱ 30,000.00 and merchandise of ₱ 5,000.00. Paid rent for the month, ₱200.00.
Bought furniture and equipment from F.E. Co. on credit, ₱2,000.00
- 3 Purchases merchandise in cash ₱10,000.00. Purchased merchandise on account from Jose Brown, ₱ 5,000.00. Terms: 2/10, n/30.
- 4 Sold merchandise on account to Juan Cruz, ₱3,000.00 Terms: 3/10, n/30.
- 6 Sold merchandise for cash, to various customers, ₱3,500.00
- 7 Returned to Jose Brown merchandise worth ₱500.00 on account of defect in quality. Jose Brown issued a credit memo for the same amount.
Purchased merchandise on account from Pedro Oria, ₱8,000.00. Terms: 2/10, 1/20, n/60.
Paid ₱150,000 to Serrano Trucking for the delivery of the merchandise bought from Pedro Oria.
- 10 Paid general expenses, ₱450.00
- 12 Sold to various customers, ₱6,000.00.
- 13 A. Arias withdrasw for personal use, the following: cash ₱200.00 and merchandise costing ₱100.00/
- 14 Collected account from Juan Cruz in full less the discount allowed.
- 15 Paid salaries of employees, ₱500.00
Purchased merchandise on account from Jose Brown, ₱12,000.00 Terms: 2/10,n/30
- 16 Sold to Mary David on account, ₱7,000.00. Terms: n/60, Cash sales, ₱2,000.00. Paid selling expenses, ₱200.00 .
- 18 Issued a credit memo to Mary David for merchandise returned, ₱600.00
Sold to Nick Trono om account, ₱1,500.00. Terms: 2/10, n/30
- 22 Paid ₱900.00 to F.E. Co. to apply partially on account. Cash Sales ₱4,000.00

- 25 Paid general expenses, ₱150.00
- 26 Paid in full the account to Pedro Oria.
- 31 Paid salaries of employees, ₱500.00. Cash sales, ₱2,000.00. Sold on account to Ted Cloma, ₱2,000.00. Terms 2/10, n/30.

(Actual count showed merchandise inventory on December 31 of ₱13,570.00)

- Required:
- a). Journal entries
 - b). Ledger accounts
 - c). Trial balance
 - d). Profit and Loss Statement
 - e). Balance sheet

Date	Explanation	F	Debit	Credit
19A				
Dec. 15	Salaries	20	500 -	
	Cash	1		500 -
	Employees' Salaries			
15	Purchases	15	12000 -	
	Jose Broan	8		12000 -
	Account purchases. Terms: 2/10, N/30.			
16	Mary David	3	7500 -	
	Sales	13		7500 -
	Account Sales. Terms: n/30			
16	Cash	1	2000 -	
	Sales	13		2000 -
	Cash sales.			
16	Selling Expenses	18	200 -	
	Cash	1		200 -
	Selling expenses paid.			
18	Sales Returns and Allowances	14	600 -	
	Mary David	3		600 -
	Return of merchandise sold.			
18	Nick Trono	4	1500 -	
	Sales	13		1500 -
	Account sales, Terms: 2/10, n/30.			
22	F. E. Company	10	900 -	
	Cash	1		900 -
	Partial payment of account Dec. 1			

Date 10A		Explanation	F	Debit	Credit
Dec.	22	Cash	1	4000 -	
		Sales	13		4000
		Cash sales.			
	25	General Expenses	19	150 -	
		Cash	1		150
		General Expenses paid.			
	27	Pedro Oria	9	8000 -	
		Cash	1		7920 -
		Purchase Discounts	23		80 -
		Full pyament of account on Dec. 7.			
	31	Salaries	20	500 -	
		Cash	1		500 -
		Employees' salaries	1		
	31	Cash	1	2000 -	
		Sales	12		2000 -
		Cash Sales			
31	31	Ted Oloma	5	2000 -	
		Sales	13		2000 -
		Account sales. Terms: 2/10, n/30.			

Cash						1
Date				Date		
19A	Item	F	Debit	19A	Item	Credit
Dec. 1		1	30000 -	Dec. 1		200 -
6		1	5500 -	3		10000 -
12		2	6000 -	7		150 -
14		2	2910 -	10		450 -
16		3	2000 -	13		200 -
22		4	4000 -	13		4410 -
31		4	2000 -	15		800 -
				16		800 -
				22		900 -
				25		150 -
				28		7520 -
				31		500 -
			Juan Cruz			2
Dec. 4		1	3000 -	Dec. 14		3000 -
			Mary David			3
Dec. 16		3	7500 -	Dec. 18		600 -
			Nick Trono			4
Dec. 18		3	1500 -	Dec.		
			Ted Gloma			5
Dec. 31		4	2000 -			
			Merchandise Inventory			6
Dec. 1		1	5000 -			
			Furniture and Equipment			7
1		1	2000 -			

Jose Brown							
Date				Date			
19A	Item	F	Debit	19A	Item	F	Credit
Dec.7		1	500 -	Dec.3		1	5000 -
13		3	4500 -	15		3	12000 -
			Pedro Oria				9
Dec.23		4	3000 -	Dec.7		2	3000 -
			F. E. Company				40
Dec.22		3	900 -	Dec.1		1	2000 -
			A. Arias, Capital				11
Dec.				Dec.1		1	35000 -
			A. Arias, Personal				12
Dec.12		2	300 -				
			Sales				13
				Dec.4		1	3000 -
				6		1	5500 -
				12		2	3000 -
				16		3	7500 -
				16		3	2000 -
				18		3	1500 -
				22		4	4000 -
				31		4	2000 -
				31		4	2000 -
			Sales Returns and Allowances				14
Dec.18		3	600 -				

75

Date				Date			
19A	Item	F	Debit	19A	Item	F	Credit
1	Dec. 3	1	10000 -	Dec. 13		2	100 -
2	3	1	5000 -				
3	7	2	8000 -				
4	15	3	12000 -				
5							
6							
7			Purchase Returns and Allowances				16
8				Dec. 7		1	500 -
9							
10							
11			Freight In				17
12	Dec. 7	2	150 -				
13							
14							
15			Selling Expenses				18
16	Dec. 16	2	200 -				
17							
18							
19			General Expenses				19
20	Dec. 10	2	450 -				
21	25	4	150 -				
22							
23							
24			Salaries				20
25	Dec. 15	3	500 -				
26	31	4	500 -				
27							
28							
29			Rent Expense				21
30	Dec. 1	1	200 -				
31							
32							
33			Sales Discounts				22
34	Dec. 14	2	90 -				
35							
36							

[illegible]

(C) TRIAL BALANCE

ARIAS TRADING
Trial Balance
December 31, 19A

Cash	₱26,830.00	₱
Mary David	6,900.00	
Nick Trono	1,500.00	
Ted Cloma	2,000.00	
Merchandise Inventory	5,000.00	
Furniture and Equipment	2,000.00	
Jose Brown		12,000.00
F. E. Company		1,100.00
A. Arias, Capital		35,000.00
A. Arias, Personal	300.00	
Sales		33,500.00
Sales Returns and Allowances	600.00	
Purchases	34,900.00	
Purchase Returns and Allowances		500.00
Freight In	150.00	
Selling Expenses	200.00	
General Expenses	600.00	
Salaries	1,000.00	
Rent Expenses	200.00	
Sales Discount	90.00	
Purchase Discounts		170.00
	<u>₱82,270.00</u>	<u>₱82,270.00</u>

(D) Income Statement

ARIAS TRADING
Income Statement
As of December 31, 19A

Sales		₱33,500.00
Less: Sales Returns and Allowances		600.00
Net Sales		<u>₱32,900.00</u>
Less: Cost of Sales:		
Merchandise Inventory, December 1	₱ 5,000.00	
Add: Purchases	₱34,900.00	
Freight In	150.00	
Gross Purchases	<u>₱35,090.00</u>	
Less: Purchase Returns & Allowances	500.00	
Goods Available for Sale		<u>₱39,590.00</u>
Less: Merchandise Inventory, December 31 ...	<u>13,570.00</u>	<u>₱25,980.00</u>
Gross Profit on Sales		<u>₱ 6,920.00</u>
Less: Expenses:		
Selling Expense	₱ 200.00	
General Expenses	600.00	
Salaries	1,000.00	
Rent Expense	<u>200.00</u>	<u>₱ 2,000.00</u>
Net Profit from Operations		<u>₱ 4,920.00</u>

Net Profit from operations forwarded	P 4,920.00
Add: Other Income:	
Purchase Discounts	170.00
Net Profit Plus Other Income	P 5,090.00
Less: Other Expenses:	
Sales Discounts	90.00
Net Income for the month	<u>P 5,000.00</u>

(E) Balance Sheet

ARIAS TRADING
Balance Sheet
As of December 31, 19A

Assets

Current Assets:

Cash	P26,830.00
Mary David	6,900.00
Nick Trono	1,500.00
Ted Cloma	2,000.00
Merchandise Inventory	13,570.00
Total Current Assets	<u>P50,800.00</u>

Fixed Assets:

Furniture and Equipment	2,000.00
Total Assets	<u>P52,800.00</u>

Liabilities and Capital

Current Liabilities:

Jose Brown	P12,000.00
F.E. Company	1,100.00
Total Current Liabilities . . .	<u>P13,100.00</u>

Capital:

A. Arias, Capital, December 1 ...	P35,000.00
Less: A. Arias, Personal	300.00
Net Capital	P34,700.00
Add: Net Income	5,000.00
A. Arias, Capital, December 31 ..	<u>P39,700.00</u>
Total Liabilities and Capital	<u>P52,800.00</u>

Classification of Accounts in the Income Statement of a Trading Concern-

If the Profit and Loss Statement is to be useful to the owner in the management of his business, information contained therein should be classified to emphasize the following items:

- (1) Net Sales - is the total selling price of the goods sold less the amount of returns and allowances on such sales. Inasmuch as the main source of income of a trading concern is the selling of merchandise, then, this item (net sales) is of the utmost significance. Sales discount may also be deducted to arrive at net sales.
- (2) Cost of Sales - is the total cost of the goods sold. This item is the immediate factor determinative of the profitability of the business. The information regarding the cost of sales helps the owner in setting up the selling prices of goods in amount sufficient

to provide the desired margin of profit. The cost of goods sold also serves as guide in the calculation of the turnover of merchandise.

- (3) Gross Profit - is the excess of Net Sales over the Cost of Sales. The realization of adequate gross profit is the primary concern of the owner. The amount of gross profit should be sufficient to absorb operating expenses and to provide a normal return on capital.
- (4) Expenses - are the amounts expended or incurred in carrying on the operations of the business. These are more appropriately called "operating expenses." Operating expenses may further be classified into:
 - (a) Selling expenses - items of expense directly incurred for the selling function. Examples are advertising expenses, traveling expenses of salesmen, salesmen's salaries, salesman's commissions, expenses of the delivery truck, and the like.
 - (b) General and Administrative expenses - items of expense incurred in the operations of the business which are not connected with the selling function. These are also termed as expenses directly incurred for the administration or management phase of the business. Examples are insurance expense, postage, rent expense, property taxes, administrative and office salaries, travelling allowances for non-selling personnel, utilities expense, office supplies and stationeries used, and the like.
- (5) Net Profit from operations - is the excess of the gross profit on sales over the operating expenses. This is the direct index of the profitability of the business. This item measures the success of the management of the business.
- (6) Other Income - - represents the total income of the business from sources other than its main source of income. Items falling under this classification represents secondary auxiliary gains, profits, and savings. Examples are gain on sale of things other than merchandise, purchase discounts, interest on money loaned, and the like.
- (7) Other Expenses - represent the expenses or losses incurred not in connection with the regular operations of the business. Examples are losses on sale of non-merchandise items, sales discounts, interest on money borrowed, and the like.
- (8) Net Income - is the excess of all the incomes of the business over all the costs, expenses, and losses. This amount is the increase in the capital of the owner derived from the business operations covering one accounting period.

Work Sheet for a Trading Concern-

As an auxiliary procedure, a work sheet is prepared to expedite the preparation of financial statements. In trading or merchandising concerns, a new feature is encountered in the preparation of the work sheet. This is the inclusion of the merchandise inventory at the end of the accounting period. The preparation of the work sheet permits the quick determination of the profit or loss of the business before the final recording of the cost of sales and preparation of the final financial statements.

The procedures listed hereunder are observed in the preparation of the work sheet for Arias Trading on page ____.

1. The trial balance is copied as is with the amount being written under the first pair of money columns.
2. The merchandise inventory on December 31, 19A is written on the line following the totals of the trial balance. The amount of inventory is extended to the credit side of the Income Statement columns and

the debit side of the Balance Sheet columns. This is the work sheet presentation of the formal journal entry explained on page ____ as follows:

Merchandise Inventory	₱ x x x	
Revenue and Expense		₱ x x x
Inventory of merchandise at the end set up		

3. The balances of the Real accounts are extended to the Balance Sheet columns.
4. The balances of the Nominal accounts are extended to the Income Statement Columns.
5. The columns under Income Statement are totalled. If the credit total is more than the debit, the difference represents the profit or income of the business. If it is the reverse then there is a loss.
6. The difference found in step (5) is placed under the column of the Income Statement with a lesser total. See the ₱5,000.00 (₱42,740.00) being placed on the debit column. This is done to make the two columns equal. Total the Income Statement columns.
7. The amount of differences mentioned in step (6) is then extended to the Balance Sheet under its proper column. In the illustration, the ₱5,000.00 is a credit balance, ~~stherefore~~, it is extended to the credit column of the Balance Sheet. Total the Balance Sheet columns.

