
> Part 1

The accounting system

> Chapter 1

Double-entry bookkeeping: Cash transactions

LEARNING INTENTIONS

In this chapter you will:

- understand that double-entry bookkeeping is used to record the two sides of a transaction
- know what ledgers and ledger accounts are
- understand cash transactions
- use the double-entry system to record cash transactions.

KEY TERMS

Accounting system Capital Capital account Credit side Debit side Double-entry bookkeeping Drawings
Ledger Ledger account Purchases Purchases returns Sales returns

Key skills exercises

Knowledge and understanding

To answer the questions in this chapter, you need to know and understand:

- each financial transaction has two entries (giving and receiving) into the ledger system, hence the name double-entry system
- a ledger system records each financial transaction that takes place in a business
- one entry is on the debit side of an account and the second entry is on the credit side of an account for each transaction
- cash transactions involve money being paid or received straightaway.

You also need to be able to apply your knowledge and understanding of the double-entry system to the ledger accounts.

ARHAM'S CELL PHONE REPAIRS

Arham has decided to open his own cell phone repair shop.

He finds a shop location in Lahore, Pakistan, which is central and easy access for people. He rents the shop to get the business started and, if the business becomes successful, he will consider buying the premises.

To start the business, he needs shop fittings and equipment. In order to pay for these items, he needs some capital, which he deposits into the business bank account. Arham realises that his capital contribution will not cover all of his initial costs and so applies for a bank loan.

1 Double-entry bookkeeping: Cash transactions AS Level

WORKED EXAMPLE 1

Before Arham opens his shop to the public the following financial transactions take place. State the accounts that will be debited and credited for each transaction (double-entry system).

Transaction	Account to debit (received into the account)	Account to credit (what is given)
Arham deposits his capital contribution into the business bank account	Bank	Capital
Paid rent by debit card	Rent expense	Bank
Purchased cell phones, chargers, cell phone covers for resale purposes	Purchases	Bank
Receives the bank loan via a bank transfer	Bank	Bank loan
Purchased equipment (tools etc.) and paid by cheque	Equipment	Bank
Returned some damaged phone covers he had bought for resale purposes	Bank	Purchases returns
Bought furniture for the shop by debit card	Furniture	Bank
Carriage inwards paid by debit card	Carriage inwards	Bank

TIP
 We are dealing with cash transactions, which means money is either being spent or received by the business. The bank account will always be affected by these transactions.

1 Arham has now set up his shop and is ready to open his business to the public. In his first two weeks of business, the following financial transactions took place. State the account to debit and credit for each transaction.

Transaction	Account to debit (received into the account)	Account to credit (what is given)
Sold a cell phone and cover to a customer who paid by cheque		
Carriage outwards paid by cheque		
Banked the takings from selling goods		
Repaired a customer's cell phone and received the payment by a debit card payment		
A customer returned goods and was refunded from the bank account		
Paid light and heating by debit card		
Purchased new office equipment and paid by cheque		
Withdrew money from bank account for personal use		
Paid general expenses by cheque		
Returned unwanted goods to supplier and received refund by bank transfer		



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WORKED EXAMPLE 2

These are the financial transactions that took place in the first week of August 2019, the second month of Arham’s business venture.

Prepare the ledger accounts for these transactions.

- Aug 1 Arham paid rent by bank transfer, \$2 500
- 2 Cash purchases of more stock for his shop to the value of \$3 000 for resale
- 3 Cash purchases of shop fittings for \$1 000
- 4 Received \$400 by debit card from selling cell phones
- 5 Arham returned some damaged goods to the value of \$60
- 6 Arham withdrew \$200 from the business bank account for private use

Answer

Debit		Bank account		Credit	
		\$		\$	
Aug 4	Sales	400	Aug 1	Rent expense	2 500
5	Purchases returns	60	2	Purchases	3 000
			3	Shop fittings	1 000
			6	Drawings	200

Debit		Rent expense		Credit	
		\$		\$	
Aug 1	Bank	2 500			

Debit		Purchases account		Credit	
		\$		\$	
Aug 2	Bank	300			

Debit		Sales account		Credit	
		\$		\$	
			Aug 4	Bank	400

Debit		Purchases returns account		Credit	
		\$		\$	
			Aug 5	Bank	60

Debit		Drawings account		Credit	
		\$		\$	
Aug 6	Bank	200			

1 Double-entry bookkeeping: Cash transactions AS Level

CONTINUED

- Each transaction is entered into the bank account as these are cash transactions.
- The debit side is for cash received whereas the credit side is for cash paid.
- The double-entry from the bank account is to the account for which the cash was either received or spent.

- 2 Arham has now been in business for six months. He is so busy he can't run the shop on his own. He decides to employ an assistant. The following financial transactions took place in January 2020.

Prepare the ledger accounts for the following financial transactions.

- Jan 1 Arham deposited \$5 000 into the business bank account as additional capital
- 2 Purchased equipment for business use to the value of \$6 700, paid by cheque
- 3 Purchased \$4 800 worth of stock for resale, paid by debit card
- 4 Received \$360 by bank transfer for goods sold
- 5 Returned \$230 worth of damaged goods
- 6 Paid light and heat account \$790 by cheque
- 7 Paid carriage outwards \$450 by bank transfer

- 3 Arham has owned his own business for a year now and it is very successful. He has decided not to buy his business premises yet but has bought another premises elsewhere, which he is renting out. The following financial transactions took place in July 2020.

Complete the table by stating which account to debit and which account to credit for each transaction, *then* prepare the ledger accounts by recording the transactions in the necessary ledger accounts.

	Transaction	Account to debit (received into the account)	Account to credit (what is given)
1	Purchased for cash a motor vehicle for \$3 600		
2	Received \$280 cash for sales		
3	Paid wages in cash \$1 200 for the shop assistant		
4	Returned damaged goods to a supplier, received a refund of \$270		
5	Carriage inwards paid in cash, \$180		
6	Received \$2 500 cash from Hazeem for rent		
7	Cash purchases of shop fittings, \$690		
8	Withdrew \$560 cash for personal use		
9	Paid \$38 cash for stationery		
10	A dissatisfied customer returned goods worth \$470		

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EXAM-STYLE MULTIPLE CHOICE QUESTIONS

- 1 Liyana owns a bakery. She recently bought an oven for business use and paid by cheque. Which entries in Liyana's books record this transaction?

	Debit account	Credit account
A	Bank	Purchases
B	Equipment	Bank
C	Purchases	Bank
D	Bank	Equipment

[1]

- 2 Souma is a plumber. He ordered some plumbing materials from Plumbing Requirements and discovered some were damaged when they were delivered. He returned the damaged materials and received a refund. How would this transaction be recorded in Souma's books of account?

	Debit account	Credit account
A	Purchases returns	Bank
B	Bank	Sales returns
C	Sales returns	Bank
D	Bank	Purchases returns

[1]

> Chapter 2

Double-entry bookkeeping: Credit transactions

LEARNING INTENTIONS

In this chapter you will:

- understand credit transactions
- use the double-entry system to record credit transactions
- know the difference between trade and cash discounts and how to treat them in the ledger accounts
- use the double-entry system to record payments to trade payables and receipts from trade receivables

KEY TERMS

Cash discount Credit transaction Discount allowed Discount received Trade discount Trade payable
 Trade receivable

Key skills exercises

Knowledge and understanding

To answer the questions in this chapter, you need to know and understand:

- credit transactions are when a purchase or sale occurs but the payment or receipt of money happens later
- what a trade payable and trade receivable are
- a trade discount is a reduction in the selling price made by one trader to another
- a cash discount is an allowance given to encourage a customer to pay quickly.

You also need to be able to apply your knowledge and understanding of trade payables, trade receivables, trade discount and cash discount to the ledger accounts.

OMAR'S GROCERY STORE

Chocoholics Malaysia is one of the leading companies in Kuala Lumpur. They manufacture products and sell them to many shops throughout Malaysia for resale purposes. Due to the large quantities of inventory being bought by businesses throughout Malaysia, Chocoholics offers its customers credit transactions.

Omar owns a grocery store in Mont Kiara and buys goods from Chocoholics Malaysia to be resold in his store. Omar has a deal with Chocoholics to make all his purchases on credit (trade payables), with the agreement that he will pay for the goods within 30 days of purchase.

Omar also allows his customers to buy on credit from his store (trade receivables); he allows a 30-day period in which payments need to be made for goods purchased on credit.

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WORKED EXAMPLE 1

The following financial transactions took place in Omar’s grocery store books of account in the month of May 2020.

State the accounts that will be debited and credited for each transaction (using the double-entry system) and then prepare the ledger accounts by recording the transactions in their ledger accounts.

Transaction		Account to debit (received into the account)	Account to credit (what is given)
May 3	Omar purchased goods on credit from Chocoholics to the value of \$1 800	Purchases	Chocoholics
8	Omar sold on credit to a customer, Sari, for \$460	Sari	Sales
13	Omar sold goods on credit valued at \$890 to Raj	Raj	Sales
20	Omar returned damaged goods to Chocoholics, \$230	Chocoholics	Purchases returns
26	Sari returned some unwanted goods that she bought on 8 May, \$56	Sales returns	Sari

Purchases		Debit	Credit
		\$	\$
May 3	Chocoholics	1800	

Chocoholics		Debit	Credit
		\$	\$
May 20	Purchases returns	230	
			May 3 Purchases 1800

Sari		Debit	Credit
		\$	\$
May 8	Sales	460	
			May 26 Sales returns 56

Sales		Debit	Credit
		\$	\$
			May 8 Sari 460

Purchases returns		Debit	Credit
		\$	\$
			May 20 Chocoholics 230

Sales returns		Debit	Credit
		\$	\$
May 26	Sari	56	

2 Double-entry bookkeeping: Credit transactions AS Level

- 1 Omar's grocery store had the following financial transactions in June 2020.
- State which two accounts are affected by each transaction and then prepare the ledger accounts by recording the transactions in their ledger accounts.
- Jun 2 Omar sold goods on credit to Zamrud for \$3 400
- 6 Omar bought goods on credit from Chocoholics for \$5 890
- 10 Omar sold goods to Nawar on credit for \$2 370
- 16 Omar returned some unwanted goods to Chocoholics for \$270
- 21 Omar sold goods to Demak on credit for \$4 680
- 29 Nawar returned \$360 worth of goods that she purchased on 10 June as they were damaged

WORKED EXAMPLE 2

Omar's grocery store is struggling to get some trade receivables to pay their accounts on time. He decides to offer cash discounts to some of his credit customers to encourage them to pay their debts early.

Chocoholics also offers Omar trade discount on his large orders and also offers a cash discount to Omar to pay his account early.

State which two accounts are affected by each financial transaction and then prepare the ledger accounts by recording the transactions in their ledger accounts.

Date	Transaction	Account to debit	Account to credit
Jul 3	Omar bought equipment from We Equip You for business use on credit for \$1 300	Equipment	We Equip You
9	Hitam bought goods on credit from Omar's grocery store for \$3 400; Omar offered Hitam a 5% cash discount if he paid his account by 31 July	Hitam	Sales
12	Omar returned some goods to Chocoholics worth \$450	Chocoholics	Purchases returns
15	Omar bought goods on credit to the value of \$6 500 from Chocoholics; they offered him a 4% trade discount as well as a 5% cash discount if he pays his account by 31 July	Purchases	Chocoholics
21	Azura bought goods from Omar's grocery store worth \$3 650; Omar agreed to a 6% cash discount if Azura can pay her account by 31 July	Azura	Sales
23	Hitam returned damaged goods to Omar's grocery store worth \$320; he originally purchased these goods on 9 July	Sales returns	Hitam
25	Omar paid Chocoholics for the goods purchased on 15 July	Chocoholics	Bank Discount received
28	Azura paid her account for the goods purchased on 21 July	Bank Discount allowed	Azura
29	Omar withdrew money for his own personal use, \$1 240	Drawings	Bank
30	Hitam paid his account for the goods purchased on 9 July	Bank Discount allowed	Hitam

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Debit		Equipment		Credit	
	\$				\$
Jul 3	We Equip You	1 300			

Debit		We EquipYou		Credit	
	\$				\$
			Jul 3	Equipment	1 300

Debit		Hitam		Credit	
	\$				\$
Jul 9	Sales	3 400	Jul 23	Returns	320
			30	Bank	2 926
			30	Discount allowed	154

Debit		Sales		Credit	
	\$				\$
			Jul 9	Hitam	3 400
			21	Azura	3 650

Debit		Chocoholics		Credit	
	\$				\$
Jul 12	Returns	450	Jul 15	Purchases	624
25	Bank	5 928			
25	Discount received	312			

Debit		Purchases returns		Credit	
	\$				\$
			Jul 12	Chocoholics	450

Debit		Purchases		Credit	
	\$				\$
Jul 15	Chocoholics	6 240			

TIP

For example, Omar purchased equipment on credit for resale purposes: the purchases account will be debited however; Omar purchased equipment on credit for office use: the equipment will be debited.