

# Advanced Bookkeeping

## FLASH CARDS

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### WHEN DO WE NEED TO PREPAY OR ACCRUE INCOME?

Income must be accounted for in the period to which it relates. Income that has not been received by the end of the financial year must be accrued, and is an asset at the year-end. Income that has been received in the year but relates to the next year is prepaid income and is a liability at the year-end.

### WHEN DO WE NEED TO PREPAY OR ACCRUE EXPENSES?

Expenses must be accounted for in the period to which they relate. Expenses that have not been paid by the end of the financial year must be accrued and are a liability at the year-end. Expenses that are paid for in the year but relate to the next year are prepayments and are an asset at the year-end.

### HOW ARE INCOME OR EXPENSES ALLOCATED WHEN CALCULATING PREPAYMENTS OR ACCRUALS?

Income or expenses relating to two accounting periods must be allocated, pro-rata, to the two periods. The calculation for each of the two periods is:

$$\frac{\text{Income or Expense}}{\text{Months to which the income/expense relates}} \times \text{Months in the period}$$

### WHAT ARE SUSPENSE ACCOUNTS AND WHAT ARE THEY USED FOR?

A suspense account is an account in the general ledger where amounts are temporarily recorded until the proper account for the entry has been identified. If a trial balance does not balance then the difference is posted to a suspense account and then investigated.

## WHAT METHODS OF DEPRECIATION CAN A BUSINESS USE?

The three main methods of depreciation that a business can use are:

**Straight-line** – an equal amount of the asset's value is charged to each period.

**Diminishing balance** – a set percentage of the asset's carrying value is charged to each period.

**Units of production** – based on the number of units produced in the period as a proportion of the total number of units the asset is predicted to produce in its useful life.

## STRAIGHT-LINE VS DIMINISHING BALANCE DEPRECIATION

What is the difference?

Using **straight line depreciation**, an asset's value is shared equally over the useful life of the asset.

Using **diminishing balance**, the depreciation % is applied to the carrying value of the asset, which means that the depreciation charge in the earlier years is higher than in later years.

## WHAT IF THE ASSET HAS A VALUE AT THE END OF ITS USEFUL LIFE?

Often, at the end of an asset's useful life, it will have a residual value. This is an estimate of the amount the asset could be sold for when the business decides to dispose of it. If a business uses straight-line depreciation this should be subtracted from the cost of the asset before calculating the depreciation.

## ACCUMULATED DEPRECIATION

What is the double entry?

The journal to post the depreciation for the year is:

**Dr Depreciation**

**Cr Accumulated depreciation**

The balance on the accumulated depreciation account is the total depreciation charged on an asset since it was purchased.

## DOUBTFUL DEBTS

What are they and how do we provide for them?

If a business is uncertain about whether a debt will be paid, the debt is 'doubtful', and it must make an allowance for doubtful debts. This can be a specific allowance that relates to a known doubtful debt, or a general allowance that is calculated as a percentage of total trade receivables after writing off irrecoverable debts and any specific doubtful debt allowances.

## IRRECOVERABLE DEBTS

What do we do when we know a debt will never be paid?

An irrecoverable debt is an amount owing to a business that it does not believe will ever be paid.

This must be written off in the business's accounts:

**Dr Irrecoverable debts**

**Cr Trade receivables**

The irrecoverable debt is an expense in the business's Statement of Profit or Loss.