

expenses incurred by the business grouped under suitable captions (heating and lighting expenses, rent and rates expenses etc); but in the case of very small expenses it may be appropriate to lump them together under a caption such as 'sundry expenses', because a more detailed breakdown would be inappropriate for such immaterial amounts.

Example:

- a) If a statement of financial position shows fixed assets of Sh.2 million and stocks of Sh.30, 000 an error of Sh.20, 000 in the depreciation calculations might not be regarded as material, whereas an error of Sh.20, 000 in the stock valuation probably would be. In other words, the total of which the erroneous item forms part must be considered.
- b) If a business has a bank loan of Sh.50,000 balance and a Sh.55,000 balance on bank deposit account, it might well be regarded as a material misstatement if these two amounts were displayed on the statement of financial position as 'cash at bank Sh.5,000'. In other words, incorrect presentation may amount to material misstatement even if there is no monetary error.
- ix) *Historical cost convention:* It's a basic principle of accounting (some writers include it in the list of fundamental accounting concepts) is that resources are normally stated in accounts at historical cost, i.e. at the amount that the business paid to acquire them. An important advantage of this procedure is that the objectivity of accounts is maximized: there is usually objective, documentary evidence to prove the amount paid to purchase an asset or pay an expense. Historical cost means transactions are recorded at the cost when they occurred.

In general, accountants prefer to deal with costs, rather than with 'values'. This is because valuations tend to be subjective and to vary according to what the valuation is for. For example, suppose that a company acquires a machine to manufacture its products. The machine has an expected useful life of four years. At the end of two years the company is preparing a statement of financial position and has decided what monetary amount to attribute to the asset.

- x) *Objectivity (neutrality):* An accountant must show objectivity in his work. This means he should try to strip his answers of any personal opinion or prejudice and should be as precise and as detailed as the situation warrants. The result of this should be that any number of accountants will give the same answer independently of each other. Objectivity means that accountants must be free from bias. They must adopt a neutral stance when analysing accounting data. In practice objectivity is difficult. Two accountants faced with the same accounting data may come to different conclusions as to the correct treatment. It was to combat subjectivity that accounting standards were developed.
- xi) *Realization concept:* Revenue and profits are recognized when realized. The concept states that revenue and profits are not anticipated but are recognized by inclusion in the income statement only when realized in the form of either cash or of other assets the ultimate cash realization of which can be assessed with reasonable certainty.

- “ 22 J Simpson returned goods to us Sh.14.
 “ 27 Paid A Cliks by cheque Sh.279.
 “ 28 Cash purchases Sh.125.
 “ 29 Bought a motor vehicle paying by cheque Sh.395.
 “ 30 Paid motor expenses in cash Sh.15.
 “ 31 Bought fixtures Sh.120 on credit from R west.

Solutions

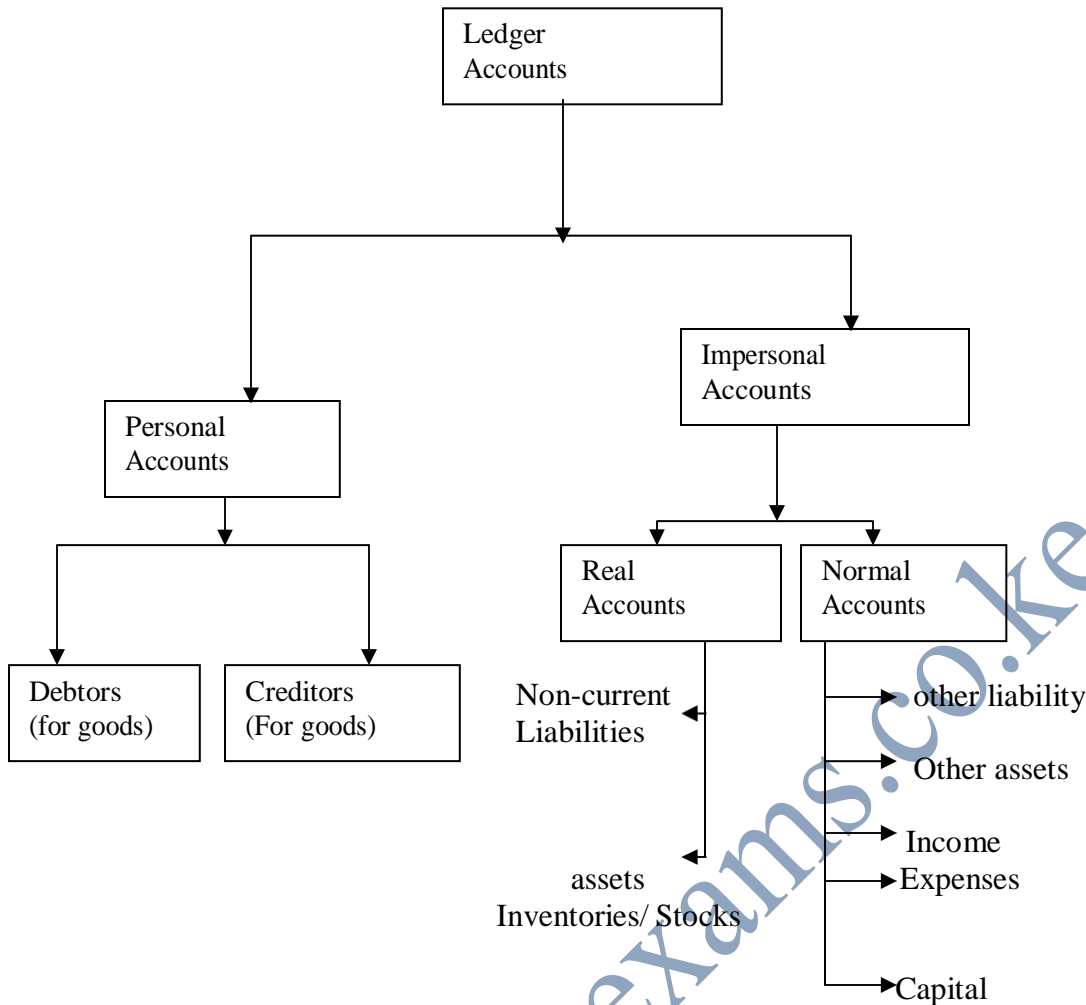
Capital a/c				Cash in hand a/c			
2003	Sh.	2003	Sh.	2003	Sh.	2003	
31/3 bal c/d	<u>1,500</u>	1/3 Cash	<u>1,500</u>	1/3 Capital	1,500	3/3 Rent	28
				1/3 Sales	49	4/3 Bank	1,000
						20/3 Repairs	18
						28/3 Purchases	125
						30/3 Motor exp.	15
						31/3 Bal c/d	<u>363</u>
					<u>1,549</u>		<u>1,549</u>

Purchases a/c			
2003	Sh.	2003	Sh.
2/3 Hanson	296	31/3 Bal c/d	421
28/3 Cash	125		
	<u>421</u>		<u>421</u>

Creditors – A Cliks ac			
2003		Sh.	2003
14/3 Returns out	17	2/3 Purchases	296
27/3 Bank	<u>279</u>		
	<u>296</u>		<u>296</u>

Rent – Expenses a/c			
2003	Sh.	2003	Sh.
3/3 Cash	<u>28</u>	31/3 Bal c/d	<u>28</u>

Bank a/c			
2003	Sh.	2003	Sh.
3 Cash	1,000	5/3 Stationery	15
		27/3 A. Hanson	279
		29/3 Motor van	395
		31/3 Bal c/d	<u>311</u>
	<u>1,000</u>		<u>1,000</u>



3.8 Review Questions

Question One

Mr J Ockey commenced trading as a wholesaler stationer on 1 May 2000 with a capital of Sh.5, 000.00 with which he opened a bank account for his business.

During May the following transactions took place.

- May 1 Bought shop fittings and fixtures from store fitments Ltd for Sh.2,000.00
- May 2 Purchased goods on credit from Abel Sh.650.00
- May 4 Sold goods on credit to Bruce Sh.700.00
- May 9 Purchased goods on credit from Green Sh.300.00
- May 11 Sold goods on credit to Hill Sh.580.00
- May 13 Cash sales paid into bank account Sh.200.00
- May 16 Received cheque from Bruce in settlement of his account
- May 17 Purchased goods on credit from Kay Sh.800.00