

Accounting
6th edition

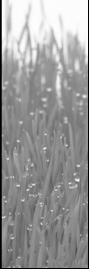
Horngren, Harrison,
Best, Fraser, Willett

PEARSON

PowerPoint to accompany

Current
Liabilities
and Payroll

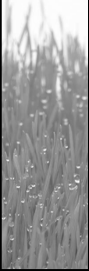
Chapter 12



Learning Objectives

1. Account for current liabilities of known amount
2. Account for current liabilities that must be estimated
3. Calculate payroll amounts
4. Record basic payroll transactions
5. Use a payroll system
6. Report current liabilities on the balance sheet

Horngren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia



Objective 1

Account for current liabilities of known amount.

Horngren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Accounts payable...

- are amounts owed to suppliers for goods or services purchased on account.
- do not bear interest expense for the debtor.

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Accounts payable example

- Suppose that on June 3, Lloyd's Sporting Store purchased \$1,000 of goods on account from Woo Wholesaler.
- What is the journal entry?

Inventory	1,000		
Accounts Payable		1,000	
<i>Purchase inventory on account</i>			

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Short-term bills payable...

- are promissory notes payable due within one year.
- In addition to recording the bill payable, the business must also pay interest expense.
- If interest expense is accrued at the end of the period, interest payable must also be recorded.

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Short-term bills payable example

- On May 30, Woo purchased inventory for \$10,000 by issuing a 90-day, 10% bill payable.
- What is the journal entry?

Inventory	10,000	
Bills Payable		10,000
<i>Purchase inventory on a 90-day, 10% bill</i>		


Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Short-term bills payable example

- Assume the accounting period ended June 30.
- How much interest was accrued as of June 30?
- $\$10,000 \times 10\% \times 31/365 = \84.93
- How does Woo record the payment at maturity?

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Short-term bills payable example

		
August 29		
Bill Payable	10,000.00	
Interest Payable	84.93	
Interest Expense	165.07	
Cash		10,250.00

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Short-Term Bills Payable Issued at a Discount

- Issuing a bill at a discount means the bank subtracts the interest from the bill's face value.
- Suppose that on February 25, Sarah discounts a \$10,000, 90-day bill, payable to the bank at 12%.
- The business will receive \$9,704.11
- $\$10,000 \times 0.12 \times 90/365 = \295.89

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Goods and Services Tax (GST) payable example

- Australia has a 10% GST on most goods and services.
- Suppose that a store made sales of \$3,300 on a given day.
- Included in the sales price is 10% in GST.
- How much is the GST liability?
- \$300

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Accrued expenses (accrued liabilities)...

- are expenses that have been incurred but not recorded.
 - salaries
 - taxes withheld
 - interest
 - utilities (electricity, gas, waste disposal)
 - payroll

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Unearned revenue example

- Assume that on June 1, Dennis's Landscaping collected \$1,500 for services to be provided during the months of June, July, and August.

June 1			
Cash		1,500	
Unearned Revenue			1,500
<i>Received cash in advance</i>			

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Unearned revenue example

- What entry does Dennis record on June 30?

June 30			
Unearned Revenue	500		
Service Revenue		500	
<i>Earned service revenue that was collected in advance</i>			

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Objective 2

Account for current liabilities that must be estimated.

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Estimated warranty payable

- The matching principle says that the company record the warranty expense in the same period that the business recognises sales revenue.

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Estimated warranty payable example

- Fisher and Paykel made sales of \$200,000 subject to warranties
- In the past years, claims have averaged 3%.

Warranty Expense	6,000
Estimated Warranty Payable	6,000

To accrue warranty expense

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Estimated warranty payable example

- During the year F&P paid a total of \$5,800 in payments

Estimated Warranty Payable	5,800
Cash (Inventory)	5,800

To record refund under warranty

This would leave a balance of \$200 in the Warranty Payable account

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Contingent liability

- A contingent liability is a **potential** liability.
- AASB 137 requires details of a contingent liability to be disclosed in the notes to the financial statement.
- Contingent liabilities may arise from current and threatened litigation.

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Objective 3

Calculate payroll amounts.

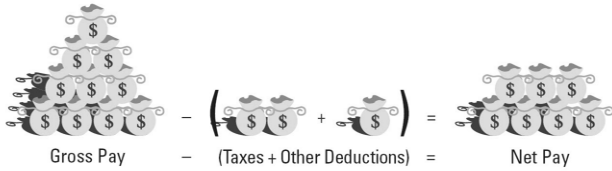
Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Payroll

- Can be calculated different ways
 - Salary – a set amount per week, month or year
 - Wages – paid at an hourly rate
 - Commission – based on a % of sales
 - Bonus – paid in addition to normal pay normally to reward performance
 - Benefits – additional items paid on behalf of the employee, e.g. insurance, superannuation

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Gross pay and net pay



Horngren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Income tax and Medicare Levy

- The tax deducted from your salary has two components:
 - 1 **Income Tax** (progressive based on your income)
 - 2 **Medicare Levy** (minimum 1.5% applied to all employee earnings – if earning more than about \$15,000)

Horngren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Other deductions

- Include
 - Superannuation
 - Union fees
 - Insurance
 - Membership fees (e.g. social clubs)

Horngren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

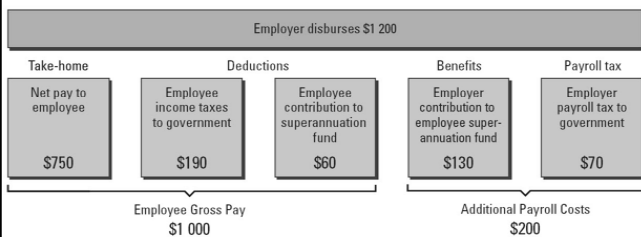
Payroll taxes

- State government tax.
- Paid by businesses with annual salaries above a threshold amount (\$500,000 - \$1,000,000 depending on the state).
- Paid by the employer in addition to gross salary.

Horngren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Breakdown of payroll costs

EXHIBIT 12-4 Typical breakdown of payroll costs for one employee



Horngren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

p. 481

Objective 4

Record basic payroll transactions.

Horngren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Salary expense

- Salary expense to the employer is the gross salary of all employees.
- Employees pay their own income tax, Medicare levy as well as union fees, etc.
- The employer serves as a collecting agent and sends these amounts to the Australian Taxation Office and union, etc.

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Accounting by the employer


- 3 Parts
 - a) Salary Expense
 - Dr Gross wage
 - Cr any deductions
 - Cr the difference as payable (cash)
 - b) Benefits expense
 - Dr any benefits expense
 - Cr benefits payable
 - c) Payroll tax expense
 - Dr Payroll tax expense
 - Cr Payroll tax payable

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Objective 5

Use a payroll system.


Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia



Payroll system components

- payroll record.
- payroll cheques (direct deposit record).
- earnings record (for each employee).

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia



Payroll record...

- is also referred to as the payroll journal.
- lists payroll data for each employee.
- serves as a cheque register.
- provides information for recording payroll expenses and related deductions (withholdings).

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia



Payroll bank account

- When companies use a payroll bank account, the company draws one cheque (or electronic funds transfer) for the net amount of salary payable to employees on its regular bank account.
- The company deposits this cheque in the special payroll bank account.

Hongren, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Payroll cheques

- The company writes pay cheques to employees out of the payroll account. Or EFT
- The employee will receive a copy of the cheque or a summary
- See page 483 for examples
- At the end of the financial year the employee also receives a PAYG payment summary for the year

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Paying the payroll

- When the employer pays the employees, the company debits Salary Payable to Employees and credits Cash.
- The liabilities to the government, unions, and other parties are also debited when cash is paid.

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Internal control over payroll

- controls for efficiency.
- controls for safeguarding payroll payments.

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Controls for efficiency

- Payroll transactions are good for computer processing.
 - All data stored in a file
 - Computer makes all calculations,
 - Prints the cheques (or makes EFT)
 - Updates all records
- If paying by cheque some firms will use two accounts and alternate between pays to make reconciling easier

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Controls for safeguarding payroll payments

- Large organisations must establish controls to ensure that payroll payments are made only to legitimate employees.
- Duties of hiring and firing should be **separated** from the duties of accounting for payroll and distributing pay cheques.

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Controls for safeguarding payroll payments

- Requiring an identification badge bearing an employee's photograph also helps internal control (especially access control).
- A formal time-keeping system helps ensure that employees have actually worked.

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Objective 6

Report current liabilities on the balance sheet.

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Reporting current liabilities

- Companies report current liabilities on the balance sheet:
 - current liabilities of known amount (e.g. payroll)
 - current liabilities that must be estimated (e.g. warranties).

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Report current liabilities

- At the end of the year, companies report the amount of payroll liabilities owed to all parties.
- The liability at year end is the amount of the payroll expense that is still unpaid.

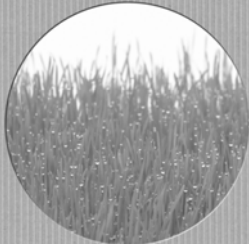
Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Ethical issues

- High level profits may make managers appear more successful
- Failing to accrue expenses and liabilities can increase appearance of profit
- Contingent liabilities also pose a challenge as they are not real liabilities

Horngrén, Best, Fraser, Willett: Accounting 6e © 2010 Pearson Australia

Accounting
6th edition



Horngrén, Harrison,
Best, Fraser, Willett

PEARSON

PowerPoint to accompany

End of
Chapter 12
