

Suspense Accounts

Introduction:

This question is concerned with fixing mistakes that have been made by the company when they are pulling together their trial balance.

In the Leaving Certificate exam, there can be a full suspense account question in either Section A (60 Marks) or Section B (100 Marks). It usually is asked every second year.

When it comes up as a full question you will usually be given a number of transactions and told what was posted incorrectly. You will then need to fix the incorrect or missing postings and eliminate the amount currently posted to the temporary suspense account.

You will also recall from Q1 Final accounts that one of our adjustments usually refers to suspense. So a good knowledge of this topic will help with this adjustment when it arises in Q1.

What is a Suspense Account?

This is a temporary account that records all the errors that have arisen in the double entry book-keeping system until such time as they can be fixed.

As you know with the double entry system of book-keeping all debits must be matched with a corresponding credit. In some cases, errors can be made either with the debit & credit posting and when this happens the amount of the error is temporarily posted to the suspense account.

The suspense account is only ever temporary and it should always have a balance of zero when you fix the errors.

Types of Errors:

There are a number of different types of errors that can be made, some will involve a posting to the suspense account, while others will not. Errors that impact the suspense account arise where debits do not equal credits, so for example 100 euro is posted to the debit side, but 10 euro is posted to the credit side. This results in an imbalance and the 90 euro difference would be temporarily posted to the suspense account.

Then there are errors in the trial balance that do not impact the suspense account. If we take the example of a transaction that has been completely forgotten, then this will need to be fixed but it will not impact the suspense account. Nothing has been posted to either debit or credit side, so there is no imbalance between debits and credits.

Suspense accounts are only needed when an imbalance has arisen between the debit and credit postings. The different types of errors that can happen are summarized in the table below:

Types of Errors

Revealed by Trial Balance	Not revealed by Trial Balance
Mathematical errors: Errors with addition or subtraction	Errors of Omission: Left out completely
Double Entry Errors: An entry on one side without a corresponding entry on other side	Errors of Principle: On right side of account but wrong type of account e.g. asset treated as an expense
Misplaced entry: An entry put on wrong side (e.g. 2 debits)	Errors of Commission: Correct side, correct type of account, but wrong account e.g. rent posted to electricity account
	Compensating errors: Where one error cancels another error e.g. 500 posted as 50 to both sides of both accounts.
	Errors of original entry: Where error is made in book of first entry e.g. sales of 500 posted as 50 to both the sales and cash (similar to compensating errors)
	Complete reversal of entry: Where correct accounts are used but the entries are to the wrong sides of both accounts



Suspense account is needed to balance the TB



No suspense account is needed

Requirements:

As mentioned above when this question comes up in the Leaving certificate exam, you will usually be given a number of transactions that have errors, which you need to fix. Some will impact the suspense account while others will not.

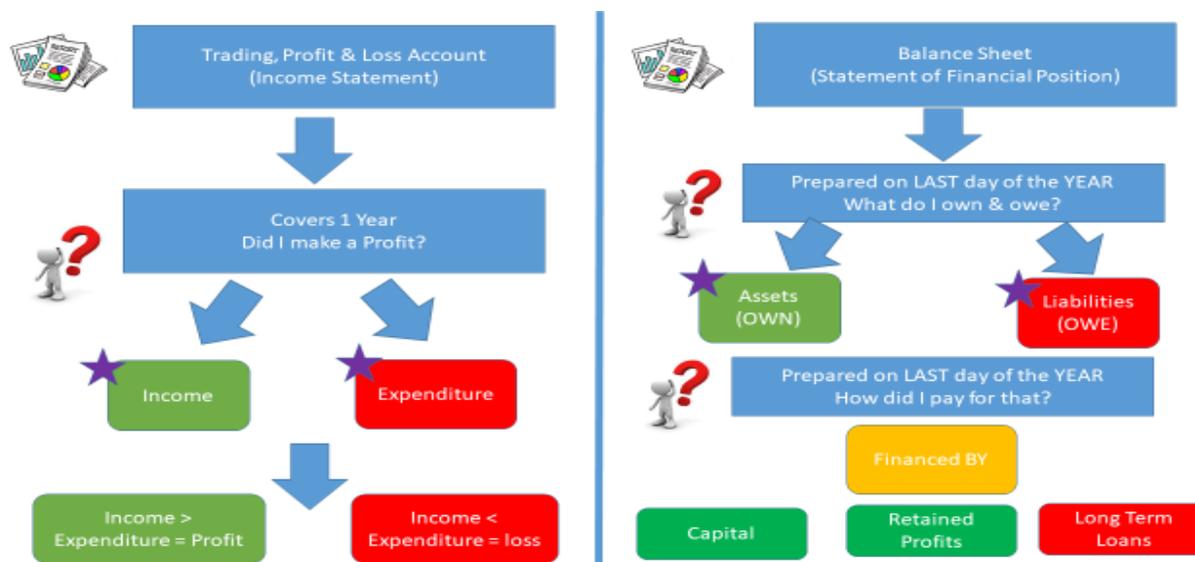
You are required to:

- Fix the errors
- Draw up the suspense account
- Prepare a statement of corrected net profit
- Corrected balance sheet (only required in a 100 mark question)
- Answer a theory question

Pre-requisite knowledge:

An understanding of double entry is required in order to be able to answer these questions. Before you look at these questions familiarise yourself with the basic rules of book-keeping which have been set out below.

Final Accounts Overview:



Income and Expenditure:

Income

This is the money that is generated by the firm, each day or week. It can be from the **Trading activity**, in which case it is called **SALES**, or it could be from other sources such as interest earned on **investments** or rental income received from renting out part of the business premises.



Examples include:

- Rental Income
- Commission Earned
- Discount Received
- Decrease in Bad Debt Provision
- Investment Income
- Bad Debt Recovered

Expenditure

This is the money that is spent by the firm, each day or week. It can be from the Trading activity, in which case it is called **PURCHASES** or it could be on other items such as rent & **rates**, heat, wages of employees.

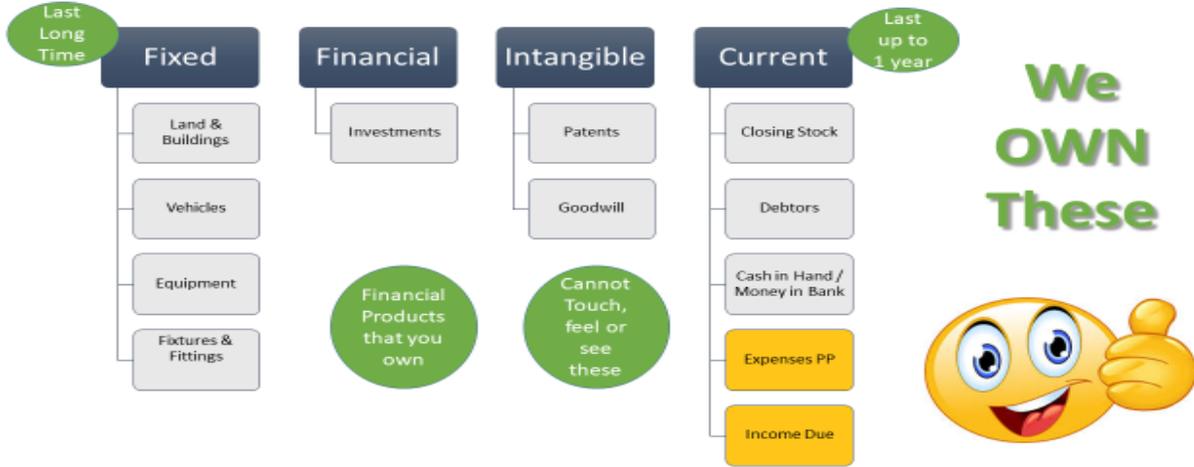


Examples include:

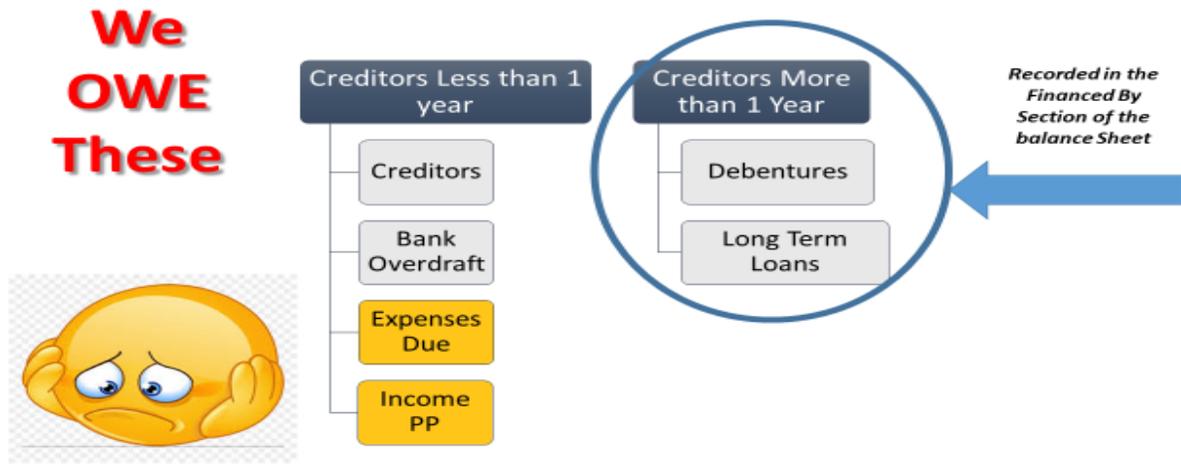
- Light & Heat (A)
- Salaries & wages (A)
- Patent W/O (A)
- Increase in Bad Debt Provision (SD)
- Depreciation (A/SD)
- Mortgage/Debenture Interest
- Tax
- Insurance (A)
- Advertising (SD)
- Rent (A)
- Rates (A)
- Discount Allowed (SD)
- Commission (SD)
- Bad Debts (SD)
- Showroom Exps (SD)

Assets & Liabilities:

Balance Sheet: Assets



Balance Sheet: Liabilities



Financed BY

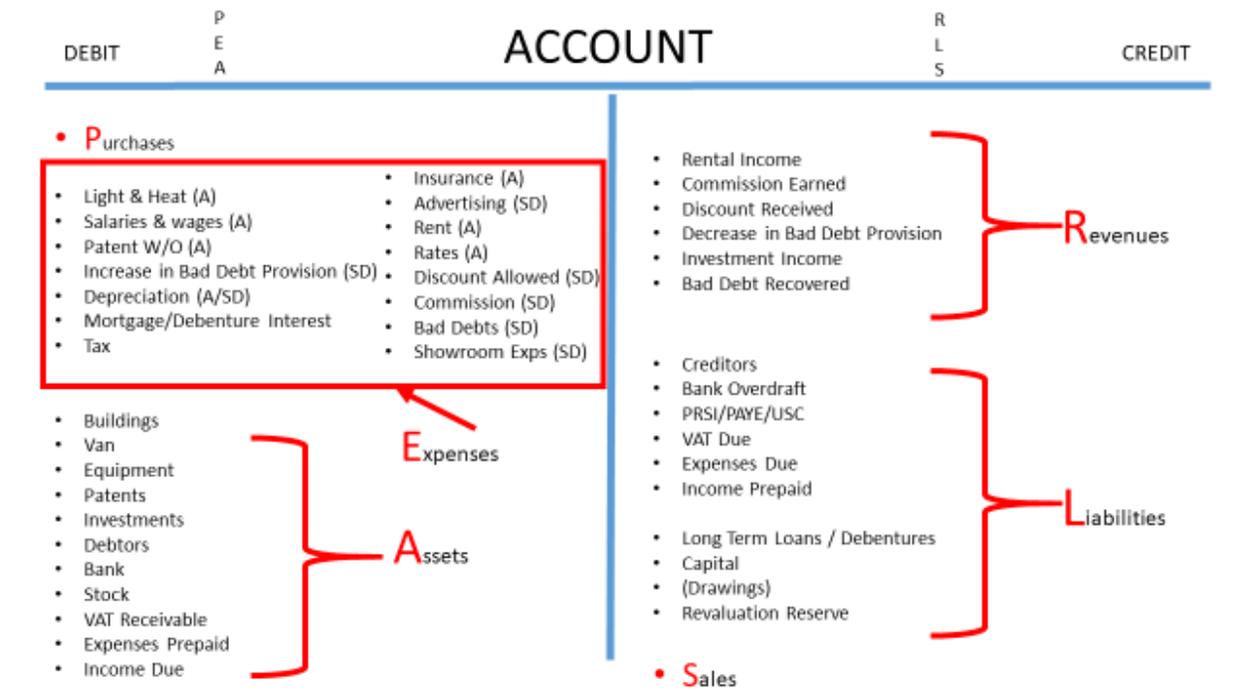
(How did we pay for it all?)



Once you understand the above it is then important to understand how each account is represented by debits and credits. You can use the ACROYNM “PEARLS” to remember this.



PEARLS in more detail is shown below:

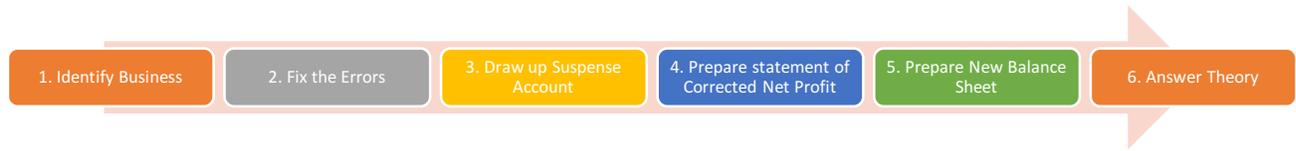


Understanding how the accounts are represented in terms of debits and credit is essential in order to be able to complete these questions successfully.

The following is a summary of some typical transactions and the accounts that should be debited and credited for each transaction. These may help you in identifying the postings that should have been made in step 2 of the procedure below.

	DR	CR		DR	CR
Bought Goods on Credit	DR: Purchases	CR: Creditors	Capital Introduced	DR: Asset or Purchases	CR: Capital
Bought Goods on Credit with VAT	DR: Purchases (NET) DR: VAT (VAT amt)	CR: Creditors TOTAL	Drawings	DR: Drawings	CR: Purchases/ Cash
Restocking Charge	DR: Purchases	CR: Creditors	Bad Debt Recovered	DR: Debtors (amt yet to be paid) DR: Bank (amt paid)	CR: Bad Debt Recovered
Purchase Return	DR: Creditors	CR: Purchases	Bounced Cheque by Debtor	DR: Debtors	CR: Bank
Sold Goods on Credit	DR: Debtors	CR: Sales	Debtor Write off	DR: Bad Debts	CR: Debtors
Sold Goods on Credit with VAT	DR: Debtors TOTAL	CR: VAT (VAT amt) CR: Sales (NET)	Asset Disposal	DR: Acc Depn DR: Bank (sales proceeds) DR: Loss on Disp.	CR: Asset CR: Profit on disposal
Sales Return	DR: Sales	CR: Debtors	Expense Accrual	DR: Expense	CR: ACC CL
			Expense Prepayment	DR: PP CA	CR: Expense

Procedure:



1. Identify the type of business that the company is operating in.

This is very important in distinguishing between purchases and other accounts. For example, when a company selling furniture, buys furniture this is treated as purchases, whereas a company selling cars would post this to furniture account. Highlight this in the question and refer back if any doubt.

2. Fix the errors:

- Identify what postings should have taken place
- Identify what postings did take place
- Identify the fix that is needed to correct the accounts to reflect what should have happened. Show these in RED pen.
- Write up the journal entry
- Repeat the process for the transactions given

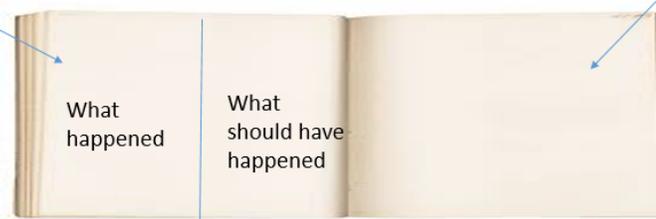
The easiest way to do this is using T accounts. Once you have identified the fix using the T accounts you then write up the journal entry that is needed to fix the error.

A suggested approach to layout your work is set out below:

Workings

Journal Entries

For each working label the working and you will use the working to identify the journal entries



1. On the workings page split your page in half
2. Establish what postings should have happened – show these in the relevant T accounts
3. Establish what postings happened – show these in the relevant T accounts
4. In the “what happened section” – **make the entries that are needed to make this the same as those in the “what should have happened” column. Use a different coloured pen.**
5. These will be your journal entry postings

An example question is outlined below to demonstrate this point.

In this case the company is a furniture retailer:

- (i) Coffee tables purchased on credit for €2,800, had been entered on the incorrect side of the creditor's account and credited as €1,800 to the equipment account.

- Identify what happened and what should have happened.

What Happened:

PURCHASES		CREDITORS	
		Purchases 2800	
Equipment			Suspense
	Creditors 1800		Equipment/ Creditors 1000

What should Have Happened:

PURCHASES		CREDITORS	
Creditors 2800			Purchases 2800

- Identify the correction needed to what happened, to reflect what should have happened. This is shown in RED below.

PURCHASES		CREDITORS	
Correction 2800		Purchases 2800	Correction 5600
Equipment			Suspense
Correction 1800	Creditors 1800	Correction 1000	Equipment/ Creditors 1000

- Write up the journal entry, you can see the marking scheme in the image below. Always put a description on the journal that summarizes why the fix is needed.

	Dr	Cr
	€	€
(i) Equipment a/c	1,800 [2]	
Creditors a/c		5,600 [2]
Purchases a/c	2,800 [3]	
Suspense a/c	1,000 [3]	
Correction of an incorrect treatment of a credit purchase		

3. Draw up the suspense account

- This is shown in T account format
- Identify all the entries from the journals that you have completed above.
- The closing balance will ALWAYS be ZERO.
- Calculate the opening balance working backwards. See example below, balancing figure is circled.

<u>Suspense Account</u>			
Original difference	25,500 [1]	Creditors/purchases (v)	26,500 [2]
Equipment/creditors (i)	1,000 [2]		
	<u>26,500</u>		<u>26,500</u>

4. Prepare the statement of Corrected Net Profit

- Identify the original net profit from the balance sheet given
- On your journal entries show, write – above the DR column and + above the credit column.
- Review the accounts and identify any Trading, Profit & Loss accounts, highlight these with your highlighter.
- If they are in the DR column you will subtract them from the original net profit, if they are in the CR column you will add them to original net profit.
- You should come up a statement of corrected net profit that looks like this:

<u>Statement of Corrected Net Profit</u>			
		€	€
Original net profit as per books			88,000
Add Sales/motor vehicles (ii)			<u>1,530 [2]</u>
			89,530
Less Purchases (i)		2,800 [2]	
Loss on sale (ii)		150 [2]	
Rent/insurance (iii)		800 [1]	
Sales returns (iv)		880 [1]	
Purchases returns (v)		<u>10,500 [1]</u>	(15,130)
Correct net profit			<u>74,400 [5]</u>

5. Prepare New Balance Sheet

- Identify the balance sheet accounts that need to be changed from your list of journal entries above.
 - Assets that have a DR adjustment will need to be increased. If they have a CR adjustment they will need to be decreased.
 - Liabilities that have a DR adjustment will need to be decreased. If they have a CR adjustment they will need to be increased.
 - The account that holds the suspense account will need to be adjusted by the amount of the original difference that you identified in step 3 above.
- Prepare the new balance sheet, show the adjustments on the face of the balance sheet. It should be presented as follows:

Balance Sheet as at 31/12/2015					
		€	€	€	
Fixed Assets					
Premises		630,000	---	630,000	[1]
Equipment	[56,000 + 1,800]	57,800	[1]	12,000	[1]
Motor vehicles	[92,000 – 2,400] [26,000 – 900]	89,600	[1]	25,100	[1]
		<u>777,400</u>	<u>37,100</u>	<u>740,300</u>	
Current Assets					
Stock (including suspense)	[98,000 – 25,500]			72,500	[1]
Debtors	[41,600 + 1,530 - 880]			42,250	[3]
Cash	[2,400 + 1,350]			3,750	[2]
				118,500	
Less: Creditors: amounts falling due within 1 year					
Creditors	[72,000 + 5,600 - 16,000]	61,600	[3]		
Insurance company		340	[1]		
Creditor - tenant		460	[1]		
Bank		<u>22,000</u>	[1]	(84,400)	<u>34,100</u>
				<u>774,400</u>	
Financed by:					
Capital				700,000	[2]
Profit and loss account				<u>74,400</u>	[1]
				<u>774,400</u>	

6. Answer the theory

What is the purpose of a suspense account?

- A suspense a/c is used when there is a mistake in the accounts that prevents the trial balance from balancing.
- The difference between the debit and the credit side of the trial balance is entered in the suspense a/c, until the errors are discovered, in order to allow the trial balance to balance.
- When the relevant errors are corrected through the suspense account the balance on the suspense account is eliminated.

What is the purpose of a Trial Balance?

To ensure the accuracy of the book keeping system and to ensure that the double entry principle has been applied to all transactions. If double entry has not been applied the trial balance will highlight this fact.

Name three types of errors that affect the balancing of a Trial Balance

- Errors in figures and addition
- Posting only one side of the double entry
- Entering one amount on the debit side of one ledger account and entering a different amount on the credit side of another ledger account.

Name and Explain the different types of errors that may occur.

See table below. Note you will not usually be required to explain all of these, usually the examiner will select 2 and ask you to explain those 2.

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