Contents

1 ACCOUTNING FOR BUSINESS TRANSACTIONS

80/100 pts

The Financial Accounting syllabus introduces five business activities:

- Selling Goods or Services: This can involve immediate payment from customers (Cash Sales) or a promise of payment at a later date (Credit Sales).
- Customer Returning Goods: When customers bring back items they bought (Sales Returns).
- Buying Goods or Services: This can involve paying immediately with cash (Cash Purchases) or promising to pay later (Credit Purchases).
- Returning Goods to Suppliers: When our business sends back items we bought (Purchase Returns).
- Small Cash Payments: Handling minor, everyday expenses using a special small cash fund (Petty Cash transactions).

The business activities can be also be furter split into three groups: activites that affect cash, activites that affect credit and activites that affect petty cash. Cash sales and purchases, credit sales and purchases, petty expenses.

Each of these business transactions goes through a consistent three-step process.

Firstly, when a business transaction takes place, it creates a source document. This document acts as an original piece of evidence for the transaction.

Secondly, this source document is used to write down the transaction in a journal entry. The journal entry is a chronological diary where every business transaction is initially recorded. In this entry we figure out what specific accounts (like 'Cash', 'Sales Revenue', or 'Accounts Payable') are affected and whether they need to increase or decrease. This is important because for each transaction, *at least* two accounts will be affected. One will be debited and at least one will be credited for the exact amount.

Lastly, after a journal entry is made, its details are posted to the affected inidividual legder accounts. Each individual ledger account resides within a document called the general ledger. A simple way to think of this is as a binder, where each page is an individual ledger account and the binder is the general ledger account. When an entry is *posted*, we simply take the debit and credit amounts from the journal entry and apply them to the correct sides of their respective individual accounts in the general ledger. This updates the balance of each account, so we always know how much money we have, how much customers owe us, what our expenses arc, and so on.

1.1 Receivables

Receivables are debts owed to a business by its customers, typically originating from previous credit transactions.

2 Formulas

2.1 Allowance for Doubtful Debts

$$\text{Allowance} = \sum_{i=1}^{m}(S_i \times \text{Allowance Rate}_i) + \sum_{j=1}^{n}(G_j \times \text{Allowance Rate}_j)$$

2.1.1 Step 1: Writing off irrecoverable (bad) debt

$$\text{DR Irrecoverable Debts Expense (P/L)} = \text{amount}$$
$$\text{CR Trade Receivables (SFP)} = \text{amount}$$

2.1.2 Step 2: Calculating the allowance

1. Identify specific receivables requiring 100% allowance:

$$\text{Allowance} = \text{Receivable Balance} \times 100\%$$

2. Apply a percentage allowance to the remaining receivables:

$$\text{Allowance} = \text{Remaining Receivables} \times \text{Allowance Rate}$$

3. Closing allowance = total of specific + general allowances.

2.1.3 Step 3: Adjustment for allowance at year-end

If Closing Allowance $>$ Opening Allowance:

$$\text{DR Irrecoverable Debts Expense}, \quad \text{CR Allowance for Doubtful Debts}$$

If Closing Allowance $<$ Opening Allowance:

$$\text{DR Allowance for Doubtful Debts}, \quad \text{CR Irrecoverable Debts Expense}$$

2.1.4 Step 4: When a debt is written off after an allowance was made

$$\text{DR Irrecoverable Debts Expense}, \quad \text{CR Trade Receivables}$$

Simultaneously, reduce the allowance account (credit to expense), so the debt is not double-counted.

2.1.5 Formula Summary

$$\text{Closing Allowance} = \text{Specific Doubtful Debts} + (\text{Remaining Receivables} \times \text{General \%})$$

$$\text{Adjustment} = \text{Closing Allowance} - \text{Opening Allowance}$$

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3 Accounting Equation

$$\text{Capital} = \text{Assets} - \text{Liabilities}$$

$$\text{Capital at Year-end} = \text{Opening Capital} + \text{Capital Introduced} + \text{Profit} - \text{Drawings}$$

Rearranging for Profit:

$$\text{Profit} = (\text{Assets} - \text{Liabilities}) - (\text{Opening Capital} + \text{Capital Introduced}) + \text{Drawings}$$

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4 Control Account Pro formas

4.1 Trade Receivables

$$\text{Credit Sales} = \text{Cash Received from Customers} + \text{Closing Receivables} - \text{Opening Receivables}$$

$$\text{Closing Receivables} = \text{Credit Sales} - \text{Cash Received} + \text{Opening Receivables}$$

4.2 Trade Payables

$$\text{Credit Purchases} = \text{Cash Paid to Suppliers} + \text{Closing Payables} - \text{Opening Payables}$$

$$\text{Closing Payables} = \text{Credit Purchases} - \text{Cash Paid to Suppliers} + \text{Opening Payables}$$

4.3 Bank (Cash) Account

$$\text{Opening Bank Balance} + \text{Cash Receipts} = \text{Cash Payments} + \text{Closing Bank Balance}$$

$$\text{Drawings} = \text{Opening Bank Balance} + \text{Cash from Customers} - \text{Cash to Suppliers} - \text{Other Expenses Paid} - \text{Closing Bank Balance}$$

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5 Mark-up, Margin and Inventory Formulas

5.1 1. Mark-up (profit on cost)

$$\text{Sales} = \text{COGS} \times \frac{100 + \text{Mark-up \%}}{100}$$

$$\text{COGS} = \text{Sales} \times \frac{100}{100 + \text{Mark-up \%}}$$

$$\text{Gross Profit} = \text{Sales} \times \frac{\text{Mark-up \%}}{100 + \text{Mark-up \%}}$$

5.2 2. Margin (profit on sales)

$$\text{Sales} = \text{COGS} \times \frac{100}{100 - \text{Margin \%}}$$

$$\text{COGS} = \text{Sales} \times \frac{100 - \text{Margin \%}}{100}$$

$$\text{Gross Profit} = \text{Sales} \times \frac{\text{Margin \%}}{100}$$

5.3 3. Inventory

$$\text{COGS} = \text{Opening Inventory} + \text{Purchases} - \text{Closing Inventory}$$

$$\text{Closing Inventory} = \text{Opening Inventory} + \text{Purchases} - \text{COGS}$$

$$\text{Inventory Lost or Drawn for Personal Use} = \text{Expected Closing Inventory} - \text{Actual Closing Inventory}$$

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5.4 Decision Aid

- If percentage is based on cost → use Mark-up formulas.
- If percentage is based on sales → use Margin formulas.
- If the question involves missing stock or movement → use Inventory formulas.

6 Business Transactions

80/100 pts

Sales Tax (VAT) Ledger

Debit	Credit
Sales tax on purchases (Input VAT)	Sales tax on sales (Output VAT)
Purchase returns (reduction of input VAT)	Sales returns (reduction of output VAT)
VAT payable to tax authority	
VAT refund from tax authority	
Balance c/d (asset if input > output)	Balance c/d (liability if output > input)

7 Receivables and Payables

80/100 pts

Receivables Ledger (Debtors Ledger)

DR		**CR**	
Balance b/d (opening debtors)	$XXX	Cash received from customers	$XXX
Credit sales	$XXX	Sales returns	$XXX
Dishonoured cheques	$XXX	Discounts allowed	$XXX
Interest charged on overdue a/cs	$XXX	Bad debts written off	$XXX
		Irrecoverable debt recovered	$XXX
		Contra entry (set off against payables)	$XXX
		Balance c/d (closing receivables)	$XXX
Total	$XXX	Total	$XXX
Balance b/d (opening debtors)	$XXX		

Payables Ledger (Creditors Ledger)

DR		**CR**	
Cash paid to suppliers	$XXX	Balance b/d (opening creditors)	$XXX
Purchase returns	$XXX	Credit purchases	$XXX
Discounts received	$XXX	Interest charged by supplier	$XXX
Contra entry (set off against receivables)	$XXX	Dishonoured payment	$XXX
Balance c/d (closing payables)	$XXX		
Total	$XXX	Total	$XXX
		Balance b/d (opening creditors)	$XXX

Bank Ledger (per Cash Book)

Debit (Receipts)	**Credit (Payments)**
Cash deposits	Cheques issued
Customer direct transfers	Standing orders
Bank interest received	Bank charges
	Dishonoured cheques
Balance c/d (if debit balance = cash at bank)	Balance c/d (if credit balance = over-draft)

Bank Reconciliation Statement (per Bank Statement vs Cash Book)

Adjustments to reconcile:	
+ Unpresented lodgements (cash book shows, bank doesn't yet)	
– Unpresented cheques (cash book shows, bank doesn't yet)	
– Bank charges not yet recorded in cash book	
– Dishonoured cheques not yet recorded in cash book	
+ Direct credits from customers not yet in cash book	
+ Interest income per bank not yet in cash book	
Balance per Bank Statement	Balance per Cash Book

Inventory Valuation and Cost of Sales

1. Cost of Sales Formula

$$\text{Cost of Sales} = \text{Opening Inventory} + \text{Cost of Goods} - \text{Closing Inventory}$$

2. IAS 2: Lower of Cost or NRV

Net Realisable Value (NRV):

$$\text{NRV} = \text{Estimated Selling Price} - \text{Estimated Future Costs of Completion} - \text{Estimated Future Selling Expenses}$$

Final Inventory Valuation:

$$\text{Inventory Value} = \min(\text{Cost}, \text{NRV})$$

3. Inventory Valuation Methods

First-In, First-Out (FIFO) Method

- **Principle:** Assumes the first units purchased are the first ones sold.
- **Closing Inventory Valuation:** Valued at the *most recent purchase prices*.

Average Cost (AVCO) Methods

(a) Periodic Weighted Average

$$\text{Average Cost per Unit} = \frac{\text{Total Cost of Opening Inventory} + \text{All Purchases}}{\text{Total Units in Opening Inventory} + \text{All Purchases}}$$

$$\text{Closing Inventory Value} = \text{Number of Closing Units} \times \text{Average Cost per Unit}$$

(b) Cumulative Weighted Average

$$\text{New Average Cost per Unit} = \frac{\text{Total Cost of Inventory after Purchase}}{\text{Total Units of Inventory after Purchase}}$$

8 Tangible Non-Current Assets

80/100 pts

Motor Vehicles –Cost

DR		**CR**	
Balance b/d	$XXX		
Purchase of motor vehicle (cash/credit)	$XXX		
Transfer from personal use	$XXX		
Revaluation increase (gross method)	$XXX		
		Disposal –cost of asset sold	$XXX
		Elimination of cost on revaluation (gross method)	$XXX
		Balance c/d	$XXX
Total	$XXX	Total	$XXX
Balance b/d	$XXX		

Motor Vehicles –Accumulated Depreciation

DR		**CR**	
Disposal –remove accumulated dep'n	$XXX	Balance b/d	$XXX
Revaluation –elimination of dep'n	$XXX	Depreciation charge (P&L)	$XXX
		Balance c/d	$XXX
Total	$XXX	Total	$XXX
		Balance b/d	$XXX

Depreciation Expense (Profit or Loss)

DR		**CR**	
Depreciation charge for year	$XXX	Accumulated Depreciation	$XXX

Revaluation Surplus (Equity)

DR		**CR**	
Transfer to Retained Earnings (realised)	$XXX	Revaluation gain (fair value > carrying amount)	$XXX
Revaluation loss (offset against surplus)	$XXX		

Disposal of Motor Vehicle

DR		**CR**	
Motor Vehicles –Cost (of asset sold)	$XXX	Accumulated Depreciation (of asset sold)	$XXX
		Bank (proceeds)	$XXX
		Profit or Loss on Disposal (balancing figure)	$XXX

Accruals and Prepayments

1. Accruals

Accrual Amount Formula

This formula estimates the value of an expense incurred but not yet paid or invoiced by the end of an accounting period:

$$\text{Accrual Amount} = \left(\frac{\text{Total Cost of Last Invoice}}{\text{Number of Months in Last Invoice}}\right) \times \text{Number of Months Accrued}$$

Example: If electricity costs $7,230 for 3 months, and 2 months need to be accrued:

$$\frac{7,230}{3} \times 2 = 4,820$$

Journal Entry Formulas for Accruals

Creating an Accrual (at year-end)

DR Individual Expense Account
CR Accruals Account

Reversing an Accrual (in the next period)

DR Accruals Account
CR Individual Expense Account

Recording the Expense Payment

DR Individual Expense Account
CR Bank or Payables Account

2. Prepayments

A prepayment is an asset recognized when a business pays for an expense in the current period that relates to a future period. The purpose is to match expenses to the correct accounting period.

Prepayment Amount Formula

$$\text{Prepayment Amount} = \text{Total Amount Paid} \times \frac{\text{Number of Months Prepaid}}{\text{Total Months Covered by Payment}}$$

Example 1: A rent payment of $1,200 covers 3 months (Dec, Jan, Feb). At Dec 31 year-end, 2 months (Jan, Feb) are prepaid:

$$1,200 \times \frac{2}{3} = 800$$

Example 2: A payment of $4,875 covers 12 months (Sept X2–Aug X3). At Dec 31 year-end, 8 months (Jan–Aug X3) are prepaid:

$$4,875 \times \frac{8}{12} = 3,250$$

Expense for the Period Formula

$$\text{Expense for the Period} = \text{Total Amount Paid} - \text{Prepayment Amount}$$

Alternative form:

$$\text{Expense for the Period} = \text{Total Amount Paid} \times \frac{\text{Months in Current Period}}{\text{Total Months Covered}}$$

Example: For the $1,200 rent payment (Dec 1 covering Dec–Feb):

$$1,200 \times \frac{1}{3} = 400$$

The total expense for 20X2 could include multiple payments (e.g. June + September + December portions).

Journal Entry Formulas for Prepayments

Recording the Expense Payment

DR Individual Expense Account
CR Bank / Trade Payables

Creating a Prepayment (at year-end)

DR Prepayment Account (Asset)
CR Individual Expense Account

Reversing a Prepayment (in the next period)

DR Individual Expense Account
CR Prepayment Account (Asset)

Share Issues, Dividends, and Finance Costs

8.1 13.1 Capital Structure of Limited Liability Companies

A limited liability company is a legal entity where shareholders, as owners, are only liable for their invested capital. They appoint directors to manage the company. The shareholders earn a return through dividends or appreciation in share value, while the business operates as a separate legal entity.

A business's **capital structure** is the mix of **equity** (shares) and **debt** (loans) used for long-term financing. The primary sources are **ordinary (equity) shares**, which give ownership and voting rights, and **preference shares**, which offer a fixed dividend but usually no voting rights. Additionally, a company can raise capital through **borrowings/loan notes**, which represent a debt to the company.

During a **winding-up** (liquidation), a company's assets are sold to pay off its debts in a strict hierarchy: secured creditors are paid first, followed by preferential creditors (e.g., employees), then unsecured creditors, and finally, any remaining funds are distributed to shareholders, with preference shareholders paid before ordinary shareholders.

8.2 13.2 Sources of Capital

Ordinary (equity) shares represent ownership in a company.

1. They have a **nominal value**, but their market price can differ. 2. Shareholders have the right to a share of the company' s profits, paid out as **dividends**, although payment is not mandatory. 3. They also have **voting rights** on key company decisions. 4. In a liquidation, ordinary shareholders are the last to receive any remaining assets and may lose their entire investment. 5. When a company issues shares, it records the transaction with a double entry:

- **Debit** Bank (for cash received). - **Credit** Ordinary Share Capital (for the nominal value). - **Credit** Share Premium (for any amount received above the nominal value).

Preference shares are a hybrid form of capital with features of both equity and debt. Unlike ordinary shares, preference shareholders have the **right to a fixed annual dividend** that must be paid before any dividends are given to ordinary shareholders. However, they typically **do not have voting rights**. In a company liquidation, preference shareholders have priority over ordinary shareholders for the return of their investment.

There are two types of preference shares:

- **Redeemable preference shares** are classified as a **liability** because the company is obligated to repurchase them at a future date. Their dividends are treated as a **finance expense**.

- **Irredeemable preference shares** are a permanent form of capital and are classified as **equity** because the company has no obligation to redeem them.

The accounting entry for issuing preference shares depends on their type. For redeemable shares, you **debit Bank** and **credit a liability account** called "Redeemable preference shares." For irredeemable shares, you **debit Bank** and **credit an equity account** called "Irredeemable preference shares."

Instead of issuing shares, a company can raise capital through borrowings or loan notes, which are classified as liabilities. These carry a fixed interest rate payable to the lender and a principal amount that will be repaid (redeemed) on a specific future date. Unlike shareholders, lenders are creditors who can take legal action if they don't receive their interest payments. Borrowings can also be secured on a company's assets, meaning the lender has a legal right to claim and sell those assets to recover their money if the company defaults. The accounting entry for a new borrowing is to debit the Bank account for the cash received and credit the Borrowings liability account.

8.3 13.3 Share Capital

A rights issue is when a company offers its existing shareholders the **right to buy new shares**, typically at a price below the current market value. This is a method companies use to raise new funds while giving existing owners priority and maintaining their proportionate control, provided all shareholders participate.

The accounting entry for a rights issue is:

- **Debit Bank** for the total cash received.

- **Credit Ordinary Share Capital** for the total nominal value of the shares issued.

- **Credit Share Premium** for the amount received above the nominal value.

Key advantages include compliance with pre-emption rights, a cheaper administration cost than a public share issue, and the preservation of shareholder control if all parties take up their rights. Disadvantages include the risk of the share price falling and the potential for a change in shareholder control if not all shareholders participate.

A **bonus issue**, also known as a capitalization issue, is when a company gives new shares to existing shareholders for **free** and in proportion to their current holdings. Since no cash is raised, the new shares are funded from the company's existing capital, such as the share premium or retained earnings accounts. The total capital remains unchanged.

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The double-entry to record a bonus issue is to:

- **Debit** either the **Share Premium** or **Retained Earnings** account. This reduces the balance of one of these accounts. - **Credit** the **Ordinary Share Capital** account for the nominal value of the new shares issued.

For example, a "1 for 5" bonus issue means a shareholder receives one new share for every five shares they already hold.

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Advantages: - Increases the number of shares, which can lower the per-share price and make the shares more attractive to investors. - Gives the company the appearance of being well-capitalized by increasing the share capital balance. - Provides a return to shareholders without using cash. - Does not dilute the ownership percentage of existing shareholders.

Disadvantages: - The process is costly to administer. - If retained earnings are used, it reduces the amount of profit available for future cash dividends. - The company does not receive any cash from the issue.

There are several key terms related to a company's share capital, including its legal value, the total number of shares it's permitted to issue, and the portion of shares it has actually sold to investors.

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8.4 Share Capital Terminology

- **Par Value (or Nominal Value):** This is the legal face value assigned to each share when a company is set up. The market price of a share can be very different from its par value. For example, a company may have shares with a par value of $1, but they could trade on the market for 50 each.

- **Authorised Share Capital:** This is the **maximum number of shares** that a company is legally permitted to issue, as specified in its constitutional documents. A company can change this limit with shareholder approval.

- **Issued Share Capital:** This is the number of shares that have been **sold to and are held by shareholders**. This number cannot exceed the authorized share capital.

- **Called-Up Share Capital:** This refers to the portion of the par value that a company has formally **requested from its shareholders**. For example, a company might issue shares with a $1 par value but only "call up" 60% of that value, asking shareholders to pay $0.60 per share.

- **Paid-Up Share Capital:** This is the portion of the called-up share capital that shareholders have **actually paid**. Any unpaid amounts are known as "calls in arrears" and are a receivable for the company. The company's statement of financial position will show the called-up share capital in equity and any calls in arrears as a current asset.

Dividends are an appropriation of a company's distributable profits to its shareholders. They are proposed by management and approved by shareholders, typically at an annual general meeting. For accounting purposes, dividends are only recorded in the financial statements when they are **paid** or **declared**. Proposed dividends are only disclosed in the notes to the accounts. The journal entry to record a paid dividend is to **debit Retained Earnings** and **credit Bank**.

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Dividends on Ordinary Shares

Ordinary shareholders are not guaranteed a dividend each year. The payment can be calculated as a percentage of profit for the year, a percentage of the par value of shares issued, or a fixed amount per share. Because these dividends are a distribution of profits, the entry reduces both the company's retained earnings and cash balance.

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Dividends on Irredeemable Preference Shares

These shares are classified as equity, and their dividends are also treated as a distribution of profit. The accounting entry for payment is the same as for ordinary shares: **debit Retained Earnings** and **credit Bank**. Preference dividends must be paid before any dividends are distributed to ordinary shareholders.

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Activity 5: Calculation and Reporting of Dividend

- **Calculate the total dividend payment:** The dividend is calculated as a percentage of the shares' par value.

- Total dividend = 150,000 shares × $1.50 par value × 5% = **$11,250**.

- **Financial statement reflection:** This dividend would **not** be reflected in the financial statements for the year ended 31 December 20X6. Since the dividend was declared on February 17, 20X7 (after the 20X6 year-end), it will only be recorded and accounted for in the financial statements for the year ended 31 December 20X7. It would, however, be disclosed as a proposed dividend in the notes to the 20X6 financial statements.

A company's capital and reserves, found in the equity section of its statement of financial position, represent the owners' interest. Reserves are funds held for specific purposes, are not cash, and are distinct from liabilities. They can be either **distributable** (like retained earnings, which can be used for dividends) or **non-distributable** (with restrictions on their use).

Types of Reserves

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Share Premium

The **share premium** is the amount by which a share's issue price exceeds its nominal (par) value. It's a **non-distributable reserve** and cannot be used for dividends. Its limited uses include issuing bonus shares or covering specific company formation expenses.

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Revaluation Surplus

The **revaluation surplus** records unrealised gains from revaluing non-current assets. It is a **non-distributable reserve** until the asset is sold, at which point the surplus is **realised** and transferred to retained earnings.

— Retained Earnings

Retained earnings represent the accumulated profits of a business that have not been distributed as dividends. This is a **distributable reserve**, meaning it can be used to pay future dividends. Portions of retained earnings may be transferred to other reserves for specific uses. When a revalued asset is sold, the realized revaluation surplus is transferred to retained earnings.

Movements on non-current assets for the year ended 30 September 20X6

Share Capital Ledger

DR		CR	
Share buyback / redemption	$XXX	Balance b/d	$XXX
		Issue of ordinary shares (cash)	$XXX
		Issue of preference shares	$XXX
		Rights issue	$XXX
		Bonus issue (transfer from reserves)	$XXX
Total	$XXX	Total	$XXX
		Balance b/d	$XXX

Reserves / Equity Ledger (Retained Earnings, Share Premium)

DR		CR	
Dividends declared	$XXX	Balance b/d	$XXX
Transfer to bonus issue	$XXX	Profit for the year (from P&L)	$XXX
		Share premium on issue of shares	$XXX
		Revaluation surplus (OCI)	$XXX
Total	$XXX	Total	$XXX
		Balance b/d	$XXX

Finance Costs Ledger (Loan Notes / Borrowings)

DR		CR	
Cash/Bank (interest paid)	$XXX	Balance b/d (opening accrual)	$XXX
Balance c/d (closing accrual)	$XXX	Interest expense accrued	$XXX
Loss on early redemption of loan notes	$XXX	Loan finance cost charged	$XXX
		Premium on redemption	$XXX
Total	$XXX	Total	$XXX
Balance b/d	$XXX		

1. Share Issues

(a) Rights Issue

Cash Raised Formula:

$$\text{Cash Raised} = \text{Number of Existing Shares} \times \frac{\text{New Shares}}{\text{Existing Shares}} \times \text{Issue Price per Share}$$

Accounting Entries:

$$\begin{aligned} \text{DR Bank}: &\ \text{Number of New Shares} \times \text{Issue Price} \\ \text{CR Ordinary Share Capital}: &\ \text{Number of New Shares} \times \text{Par Value} \\ \text{CR Share Premium}: &\ \text{Number of New Shares} \times (\text{Issue Price} - \text{Par Value}) \end{aligned}$$

(b) Bonus Issue

Number of New Shares Formula:

$$\text{Number of New Shares} = \text{Existing Shares} \times \text{Bonus Ratio}$$

Increase in Share Capital Formula:

$$\text{Increase in Ordinary Share Capital} = \text{Number of New Shares} \times \text{Par Value}$$

Accounting Entries:

DR Share Premium or Retained Earnings
CR Ordinary Share Capital

2. Dividends and Finance Costs

(a) Ordinary Share Dividends

Percentage of Profit:

$$\text{Dividend Amount} = \text{Net Profit} \times \text{Dividend Percentage}$$

Percentage of Par Value:

$$\text{Dividend Amount} = \text{Number of Shares} \times \text{Par Value} \times \text{Dividend Percentage}$$

Per Share:

$$\text{Dividend Amount} = \text{Number of Shares} \times \text{Dividend per Share}$$

Accounting Entries (when paid):

DR Retained Earnings
CR Bank

(b) Finance Costs

Redeemable Preference Shares:

$$\text{Annual Finance Cost} = \text{Number of Shares} \times \text{Par Value} \times \text{Dividend Percentage}$$

Interest on Borrowings:

$$\text{Annual Finance Cost} = \text{Principal Amount} \times \text{Interest Rate}$$

Accounting Entries (when paid):

DR Finance Costs
CR Bank

9 Statement of Profit or Loss and Other Comprehensive Income

Sales Ledger (Sales Account)

DR		CR	
Sales returns	$XXX	Balance b/d (if over-provision)	$XXX
		Credit sales	$XXX
		Cash sales	$XXX
		Interest charged on late payment	$XXX
		Balance c/d (transfer to P&L)	$XXX
Total	$XXX	Total	$XXX
		Balance b/d	$XXX

Purchases Ledger (Purchases Account)

DR		CR	
Balance c/d (transfer to P&L)	$XXX	Balance b/d (if over-provision)	$XXX
Credit purchases	$XXX	Purchase returns	$XXX
Cash purchases	$XXX	Discounts received	$XXX
Carriage inwards	$XXX		
Total	$XXX	Total	$XXX
Balance b/d	$XXX		

Tax Payable Ledger (Sales Tax / VAT Account)

DR		CR	
Input tax on purchases	$XXX	Output tax on sales	$XXX
Cash paid to tax authority	$XXX	Irrecoverable tax adjustments	$XXX
Bad debt relief (input tax recoverable)	$XXX	Over-claimed input tax repaid	$XXX
Balance c/d (closing liability / asset)	$XXX		
Total	$XXX	Total	$XXX
		Balance b/d (opening liability)	$XXX

Interest Payable Ledger

DR		CR	
Cash paid to lender	$XXX	Balance b/d (opening accrual)	$XXX
Balance c/d (closing accrual)	$XXX	Interest expense accrued	$XXX
		Interest charged by lender	$XXX
Total	$XXX	Total	$XXX
Balance b/d	$XXX		

Expenses Ledger (e.g. Rent, Utilities, Wages)

DR		CR	
Cash/Bank (paid)	$XXX	Balance b/d (opening accrual)	$XXX
Accrued expense (closing accrual)	$XXX	Prepayment (closing adjustment)	$XXX
Balance c/d (transfer to P&L)	$XXX	Balance b/d (opening prepayment)	$XXX
Total	$XXX	Total	$XXX
Balance b/d	$XXX		

Income Ledger (e.g. Rent Income, Service Income)

DR		CR	
Balance b/d (opening deferred income)	$XXX	Cash/Bank (received)	$XXX
Deferred income (closing liability)	$XXX	Accrued income (earned but not received)	$XXX
Balance c/d (transfer to P&L)	$XXX	Balance b/d (opening accrued income)	$XXX
Total	$XXX	Total	$XXX
Balance b/d	$XXX		

Intangible Assets Ledger (e.g. Patents, Goodwill, Software)

DR		CR	
Cost of acquisition	$XXX	Disposal (at cost)	$XXX
Revaluation increase (OCI/Equity)	$XXX	Amortisation expense	$XXX
Impairment loss (P&L)	$XXX	Revaluation decrease (OCI or P&L)	$XXX
Balance c/d	$XXX		
Total	$XXX	Total	$XXX
Balance b/d	$XXX		

9.1 Sole Trader Statement of Profit or Loss

9.1.1 1st Component: Gross Profit

$$\begin{aligned}\text{Net Sales} &= \text{Sales} - \text{Sales Returns}\\ \text{Cost of Goods Sold (COGS)} &= \text{Opening Inventory} + (\text{Purchases} - \text{Purchase Returns}) - \text{Closing Inventory}\\ \text{Gross Profit} &= \text{Net Sales} - \text{COGS}\end{aligned}$$

9.1.2 2nd Component: Net Profit

$$\text{Net Profit} = \text{Gross Profit} + \text{Other Income} - \text{Expenses}$$

9.2 Company Statement of Profit or Loss and Other Comprehensive Income

$$\begin{aligned}\text{Revenue} - \text{Cost of Sales} &= \text{Gross Profit}\\ \text{Profit before tax} &= \text{Gross Profit} + \text{Other Income} - \text{Distribution Costs}\\ &\quad - \text{Administrative Expenses} - \text{Finance Costs}\\ \text{Other Comprehensive Income} &= \text{Gain on revaluation of non-current assets}\\ \text{Total Comprehensive Income} &= \text{Profit after tax} + \text{Other Comprehensive Income}\end{aligned}$$

9.3 Income Tax Accounting

9.3.1 Step 1: Current Year Tax Estimate

$$\text{Current Tax Estimate} = \text{Profit before tax} \times \text{Tax Rate (\%)}$$

Journal Entry:

- Dr Income Tax Expense (Expense increases)
- Cr Current Tax Payable (Liability increases)

9.3.2 Step 2: Under or Over Provision (Prior Year Adjustment)

$$\text{Adjustment} = \text{Actual Tax (prior year)} - \text{Estimated Tax (prior year)}$$

- If positive (Under-provision, estimate too low):
  - Dr Income Tax Expense
  - Cr Current Tax Payable
- If negative (Over-provision, estimate too high):
  - Dr Current Tax Payable
  - Cr Income Tax Expense

9.3.3 Step 3: Income Tax Expense Reported in SPL

$$\text{Income Tax Expense} = \text{Current Tax Estimate} + (\text{Under / Over Provision})$$

9.3.4 Step 4: Payment of Income Tax

$$\text{Tax Paid} = \text{Bank (Cr)} \quad \text{and} \quad \text{Current Tax Payable (Dr)}$$

9.4 Summary Formulae

$$\begin{aligned}\text{Income Tax Expense} &= (\text{Profit before tax} \times \text{Tax Rate}) + (\text{Under / Over Provision}) \\ \text{Tax Payable (closing balance)} &= \text{Opening Balance} + \text{Current Year Estimate} \\ &\quad + \text{Under-provision} - \text{Over-provision} - \text{Tax Paid}\end{aligned}$$

Blue Co's Statement of Financial Position as at 31 December 20X8

	$
Non-current assets	
Office building	292,500
Office equipment	46,960
Total Non-current assets	339,460
Current assets	
Inventories	219,600
Trade receivables	287,800
Prepayment	600
Total Current assets	508,000
Total Assets	**847,460**
Equity and reserves	
Share capital	40,000
Share premium	10,000
Revaluation surplus	120,000
Retained earnings	391,060
Total Equity	561,060
Non-current liabilities	–
Current liabilities	
Payables	170,000
Bank overdraft	6,000
Accrued finance cost	400
Current tax liability	110,000
Total Current liabilities	286,400
Total Equity and Liabilities	**847,460**

10 Main elements of the Statement of Cash Flows

10.1 Operating Activities - Direct Method

Cash generated from operations

Comprises of:

cash receipts from customers: Opening receivables + Sales - closing receivables cash paid to suppliers: Opening payables + purchases - closing payables cash paid to employees: Amount owed to employees at the start of the period + Wages and salaries expense - closing amounts owed to employees net total = cash generated from operations

Interest paid: Opening interest payable + interest charge - closing interest payable Tax paid: Opening tax payables + tax charge - closing tax payables net total = Net Cash from operating activities

10.2 Cash flows from investing activities

Payments to acquire non-current assets: Closing NCA - Opening NCA + Depreciation + Carrying value of NCA sold Proceeds from sale of non-current assets: Cost - Accumulated depreciation + Profit/(Loss) on sale Investments: inflows Interest received: inflows Dividends received: inflows

net total = (Net cash from investing activities)

10.3 Cash flows from financing activities

Proceeds from issue of share capital Loans/Borrowings: Cash received from loans and borrowings is a cash inflow, while the repayment of the loans is a cash outflow, interest on loans is recorded separately dividends paid: Cash outflows

net total = Net cash from financing activities

11 Consolidated Financial Statements

When a company gains 50% control of another company it becomes a parent and the company be invested in is called a subsidary. Consolidated financial statements are single combined financial statements that combine the net assets, expenses and revenue of the parent company and the subsidary that reflect the substance of the investment, without it the parent's unconsolidated financial statements may mislead users as it won't accurately and fairly represent the investment.

Blue Co's Statement of Profit or Loss and Other Comprehensive Income
for the year ended 31 December 20X8

	$
Revenue	2,957,000
Cost of sales:	
Opening inventory	236,400
+ Purchases	1,748,200
– Purchase returns	(5,330)
+ Delivery cost on purchases	33,100
+ Wages (10% allocation)	28,200
– Closing inventory	(219,600)
Total cost of sales	(1,820,970)
Gross profit	1,136,030
Distribution costs:	
Distribution expenses	347,250
+ Wages (20% allocation)	56,400
+ Advertising	2,000
+ Building depreciation	7,500
Total distribution costs	(413,150)
Administrative expenses:	
Wages (70% allocation)	197,400
+ Accountancy fees	5,000
+ Sundry administrative expenses	81,000
+ Irrecoverable debts (per TB)	14,680
+ Additional irrecoverable debts	8,000
+ Increase in allowance for receivables	4,000
+ Equipment depreciation	11,740
– Insurance prepayment	(600)
Total administrative expenses	(321,220)
Finance cost:	
Interest paid	1,000
+ Accrual	400
Total finance costs	(1,400)
Profit before tax	400,260
Income tax expense:	
Current year provision	110,000
+ Prior year under provision	2,200
Total income tax expense	(112,200)
Profit for the year	288,060
Other comprehensive income:	
Gain on property revaluation	120,000
Total comprehensive income for the year	408,060

Statement of Profit or Loss for the year ended 31 October 2016

Sales	£100,250
Cost of Sales	
Purchases	£60,400
Less: Closing inventory	(15,600)
Cost of sales	£44,800
Gross profit	**£55,450**
Expenses	
Salaries	£29,300
Motor expenses	£1,200
Rent	£950
Insurance	£150
General expenses	£85
Total expenses	£31,685
Profit for the year	**£23,765**

Jesstika Co's Statement of Cash Flows for the year ended 31 December 20X6

	$'000	
Cash flows from operating activities		
Cash generated from operations	2,070	
Interest paid	(155)	
Tax paid	(375)	
Net cash from operating activities		1,540
Cash flows from investing activities		
Payments to acquire non-current assets	(1,228)	
Proceeds from sale of non-current assets	105	
Interest received	84	
Dividends received	162	
Net cash from investing activities		(877)
Cash flows from financing activities		
Proceeds from issue of share capital	500	
Repayment of loans	(350)	
Dividends paid	(160)	
Net cash from financing activities		(10)
Net movement in cash and cash equivalents		653
Cash and cash equivalents at beginning of period		128
Cash and cash equivalents at end of period		781

Jesstika Co's Statement of Cash Flows (Indirect Method) for the year ended 31 December 20X6

	$'000	
Cash flows from operating activities		
Profit before tax	XXXX	
Adjustments for:		
Depreciation	XXX	
Finance costs	155	
Investment income	(246)	
Profit on sale of non-current assets	(XX)	
Operating profit before working capital changes	XXXX	
Increase in inventories	(XX)	
Increase in receivables	(XX)	
Increase in payables	XX	
Cash generated from operations	2,070	
Interest paid	(155)	
Tax paid	(375)	
Net cash from operating activities		1,540
Cash flows from investing activities		
Payments to acquire non-current assets	(1,228)	
Proceeds from sale of non-current assets	105	
Interest received	84	
Dividends received	162	
Net cash from investing activities		(877)
Cash flows from financing activities		
Proceeds from issue of share capital	500	
Repayment of loans	(350)	
Dividends paid	(160)	
Net cash from financing activities		(10)
Net movement in cash and cash equivalents		653
Cash and cash equivalents at beginning of period		128
Cash and cash equivalents at end of period		781