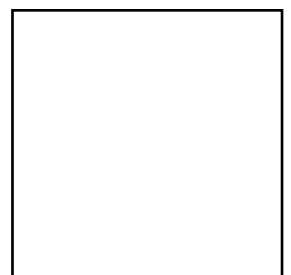
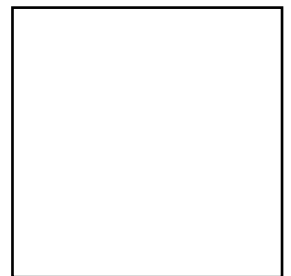
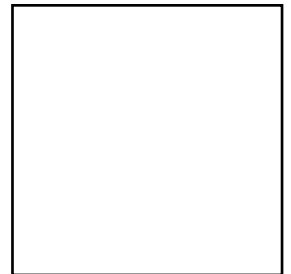


Nelson Thornes  
Distance Learning

# A2 Accounting

Kevin Crosby



Nelson Thornes

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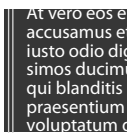
## Key to icons used throughout this pack:



Writing



Hand-in activity (either by post or e-mail)



Reading



Internet research or online activity

# Study Calendar



Study week	Start date	Unit no.	Unit descriptor	Externally assessed assignment
1		Introduction	A2 Accounting Introduction	
2		1.1	Incomplete Records: Revision of accounting techniques	
3		1.2	Calculating profit	Yes
4		1.3	Preparing final accounts	Yes
5		2.1	Partnership accounts: Introduction to accounting for partnerships	
6		2.1	Introduction to accounting for partnership (continued)	Yes
7		2.2	Accounting for changes in partnerships	
8		2.2	Accounting for changes in partnerships (continued)	Yes
9		2.3	Dissolution of partnership	
10		2.3	Dissolution of partnership (continued)	Yes
11		3.1	Published Accounts of Limited companies: Annual report	Yes
12		3.2	Uses and limitations of published accounts	
13		4.1	Accounting Standards: Introduction to international Accounting Standards	Yes
13		4.2	Statement of cash flow	Yes
14		5.1	Inventory valuation: valuation methods	Yes
15		6.1	Manufacturing accounts	
16		6.1	Manufacturing accounts (continued)	Yes
17		7.1	Capital investment appraisal and social accounting	Yes
18		8.1	Absorption costing and activity based costing	
19		8.1	Absorption costing and activity based costing (continued)	Yes
20		9.1	Break-even analysis	Yes
21		9.2	Decision making	Yes
22		10.1	Standard costing	Yes
21		11.1	Budgets and budgetary control	Yes
22 to exams			Revision	

- All the assignments for A2 Accounting can be found in the relevant units of the Nelson Thornes Distance Learning Student Course Materials.
- Students should also take their mock exam at some point during weeks 13–18, to be agreed between the Nelson Thornes Distance Learning tutor and the Link Teacher



# Introduction



Hello and welcome to A2 Accounting!

## **What will I study this year?**

There are two units in A2 Accounting

ACCN3: Further aspects of financial accounting : Topics 1-5

ACCN4: Further aspects of management accounting: Topics 6-11

In topics 1-5 we will use and develop the accounting techniques and skills from the AS course to:

- Prepare final accounts for businesses where the owner does not keep a full set of accounting records.
- Prepare accounts for partnerships including: where new partners join, old partners leave and the partnership ends.
- Investigate the accounts and annual reports of limited companies.
- Explain what accounting standards are and why they are needed.
- Prepare and evaluate statements of cash flow.
- Value inventories.

In topics 6-11 we will look at the role accounting takes in the management of businesses. Managers need to plan, control and make decisions and we will provide information to help them.

- Planning: we will prepare and evaluate budgets; use break-even analysis and absorption costing.
- Control: we will use budgets and standard costing.
- Decision making: we will use marginal costing and capital investment appraisal. We will also recognise the limitations of accounting information in making decisions – we call this social accounting.

## **What will the exams be like?**

At the end of the course you will take two examinations. They are both 2 hours long and will have 90 marks. Each exam has something called a SYNOPTIC element; this means that you will be asked questions from other parts of the accounting specification. This is to make sure that you have a good understanding of the whole subject.

In ACCN3 (topics 1-5) the synoptic questions will be based on the whole of the AS – so you need to keep all your notes from last year.

In ACCN4 (topics 6-11) the synoptic questions will come from ACCN2 – things like final accounts, ratios, cash budgets and budgetary control.

## Activity

# 1

Start your A2 Accounting file:

Divide it into two units: ACCN3 and ACCN4.

Set up:

- your terminology sheets: use the headings: Term; Definition; Explanation/ Examples
- a questions for tutor sheet – this will have all the questions you come up with as you progress through the topics.
- Make sure you have a copy of the specification – what is covered in each unit and how the exams are organised – you can get this from: [www.aqa.org.uk](http://www.aqa.org.uk). Go to qualifications, then GCE and Accounting.
- While you are online check out the site – you will see there is other useful information such as past exam papers and student guides.



## What grades can I achieve?

Your A level grade is worked out by adding your AS marks (the UMS score) to your A2 marks. So if you scored 120 out of 200 UMS marks at AS and you get 140 out of 200 in the A2 exams then your overall score will be 260 marks. This would give you a C grade. The grades at A level are:

Marks	Grade
160	E
200	D
240	C
280	B
320	A

You can achieve an A\* at A level – to get this you need to get an A grade overall and an A\* at A2, this means getting 180 out of 200 in the A2 exams.

Both A2 exams have something called “stretch and challenge”. This means that you will be set questions that:

*“require you to evaluate accounting issues and apply knowledge, understanding and skills to complex situations.”*

This means that there is a step-up from AS and the questions will make more demands on you. There could be more information or you could be asked to write more in-depth answers. Don’t worry: we will practise this and develop your exam technique during the course.

## How will I study?

These notes will provide you with an introduction to each topic and activities that will give you practice in the techniques/concepts and develop your exam technique. At the end of each unit there will be Exam Style Questions – these will test whether you have understood the work covered in each unit.

You will also be provided with other resources to help you – these will range from an annual report from a major plc to spreadsheets with answers and explanations of how the answers were arrived at.

However, you will need to read more and do many more questions if you are going to be successful in the exams. In each unit you will see a reference to the recommended textbook. Make sure you read the unit and complete the questions at the end of each unit.

This is a reference to the recommended textbook which is:

*A2 Accounting for AQA*  
Authors: Cox and Fardon  
Published by Osborne Books  
ISBN: 978 1 905777 17 4

Other textbooks that are useful:

*Advanced Accounting for A2*  
Author: Ian Harrison  
Published by Hodder Education  
ISBN: 978 0 3409 73592

*AQA Accounting A2*  
Authors: Jacqueline Halls-Bryan & Claire Merrill  
Published by Nelson Thornes  
ISBN: 978 0 7487 9870 4

You will also use these websites:

[www.bized.co.uk](http://www.bized.co.uk)  
[www.tutor2u.net](http://www.tutor2u.net)  
[www.iasplus.com](http://www.iasplus.com)  
[www.duncanwil.co.uk](http://www.duncanwil.co.uk)  
[www.aqa.org.uk](http://www.aqa.org.uk)

When you are working through each unit there will be things that you don't understand, don't make sense, or you want to ask questions about! You must make a note of these questions to ask your tutor – you should keep a "questions for tutor" sheet or book with you at all times and make a note of them as they crop up – don't leave them for later!

### **What is the key to success?**

Make sure that you really understand each topic – you need to be able to tackle questions asked in a variety of different ways and give full answers (this includes detailed explanations and examples) – a good way to test your understanding is to explain things to someone else – if you can do this and they understand then you understand!

### **What do I do now?**

You need to review your AS notes in preparation for the first Topic – Incomplete records.

## **Activity 2**

Make sure you have looked at your notes, the textbook etc on the following:

- Cash books and cash accounts
- Bank accounts
- Bank reconciliations
- Control accounts

At vero eos et  
accusamus et  
iusto odio de-  
quimos ducim  
qui blanditis  
praesentium  
voluptatum

- Trial balance
- Depreciation
- Profit and loss on disposal of assets
- Accruals and prepayments
- Bad debts
- Provision for doubtful debts
- Discounts allowed and received
- Layout of final accounts
- Gross profit margin
- Gross profit mark-up



The first unit will be mainly activities to check your understanding of some key AS topics and to get you back to thinking about Accounting.

Topic 3 will introduce the terminology used in International Accounting Standards. If you completed the AS to A2 activities you will already be familiar with this. Although this terminology only has to be used by public limited companies it will eventually be used in all accounts. So, in the study guide we will show both the 'old' and 'new' terminology in Topics 1 and 2 to help you get used to it. In the exam you must use the new terminology when answering questions about limited companies, but you will not be penalised if you use the old or new terminology when answering incomplete record or partnership questions.

**Good luck with the rest of the course – remember to use as many resources as possible to improve your understanding and make sure you have plenty of questions to ask your tutor!**

---

# Topic 1 Incomplete records

## Unit 1.1 Revision of accounting techniques

---

**On completion of this unit you should be able to:**

- Prepare cash accounts
- Prepare bank accounts
- Prepare control accounts
- Calculate depreciation using straight-line and reducing balance methods
- Calculate the profit or loss on the disposal of assets
- Prepare ledger accounts showing accruals and prepayments
- Prepare trading accounts
- Calculate gross profit margin and mark-up
- Prepare trading profit and loss accounts (income statements) and balance sheets

In this topic we will be preparing accounts for businesses that do not keep full accounting records. This may seem strange as we have spent a year learning how to keep records, but as we will see many people who own their own business: either don't know how; cannot be bothered or do not have the time to keep full accounting records – this is one of the reasons that accountants exist!

In this unit we will revise the techniques from last year that will provide our toolkit for tackling incomplete record problems.





The bank reconciliation statement is:

Bank reconciliation statement		£
at 30 September 2009		
	Balance at bank	(3,854)
Add	Uncleared bankings	285
		<hr/>
		(3,569)
Less	Unpresented cheques	1,023
		<hr/>
	Balance in cash book	<hr/> <hr/> (4,592)

### Tip

Remember: *Uncleared bankings* is money received in the cash book but not yet shown on the bank statement – this will increase the bank statement balance – but in this case the bank is overdrawn so it reduces the overdraft.

## Activity

### 3

Prepare a bank reconciliation for Gordon Banks at 30 September 2009.

Overdrawn balance on bank statement at 30 Sep £13,460.

Gordon has paid the cheque for the sale of the car into the bank but it has not appeared on his bank statement yet.

The following cheques to Gordon's suppliers have not been presented to the bank at 30 September.

cheque 2456	£2,143
cheque 2458	£2,000
cheque 2459	£300



## Control accounts

In the AS we used control accounts to check the accuracy of the double entry and arithmetic in the Sales and Purchase ledgers. In the next unit we will be using them to find missing figures such as sales or purchases. Again we need to make sure we know the entries made in the control accounts.

### Tip

You can think of the control account as the TOTAL account for that ledger, so all the entries are on the same side as the individual customer or supplier – but are the totals for the month or the year.

### Tip

Before tackling the next activity make sure you understand the accounting treatment of the provision for doubtful debts.

## Activity 4



Prepare sales and purchase ledger control accounts for Ray Wilson for the month of September from the information given below:

		£
1 Sep	Debit balances in purchase ledger	212
	Credit balances in purchase ledger	12,568
	Debit balances in sales ledger	24,895
	Credit balances in sales ledger	874
Transactions for the month		
30 Sep	Credit sales	34,569
	Cash sales	8,546
	Cheques received from debtors	20,085
	Purchases on credit	14,865
	Payments to suppliers	12,058
	Cash purchases	8,456
	Discount received	658
	Discount allowed	1,586
	Bad debts	523
	Dishonoured cheque from Eusebio	278
	Contra entry	753
	Increase in provision for doubtful debts	687
30 Sep	Debit balances in purchase ledger	178
	Credit balances in sales ledger	672

Sales ledger control account

--	--

Purchase ledger control account

--	--

**Accounting concepts**

Even though the owners of the business do not keep full accounting records, we as accountants will still apply accounting concepts to the preparation of final accounts – the key ones for us are: Accruals, Prudence, Business Entity, Consistency and Going Concern.

## Activity

# 5



Go back to your notes and define, explain and give examples of the application of the following concepts:

- Accruals
- Prudence
- Business entity
- Consistency
- Going concern
- Materiality

### **Depreciation**

Because we apply accounting concepts to the preparation of final accounts we will have to charge depreciation in the profit and loss account (income statement) and show fixed assets at their net book value (NBV).

You will need to be able to calculate depreciation using both straight-line and reducing-balance methods and to calculate the profit or loss on the disposal of assets. We will start by practising the calculation of the straight-line method.

# Activity 6

Complete the table shown below for the fixed assets of Nobby's Styles. You need to calculate the depreciation charged to the profit and loss account each year and show how the asset would appear on the balance sheet.



### Straight line depreciation

	Year	Cost	Rate	(Change in provision)	Total
				Expense in P&L a/c	Provision
<b>Fixtures</b>	1	100,000	20%	20,000	20,000
	2		20%		
	3		20%		
	4		20%		
	5		20%		
			<b>Useful life</b>		
<b>Equipment</b>	1	88,000	4 years		
	2				
	3				
	4				

### Balance sheet extract

Cost	Dep'n to date	NBV
£	£	£
100,000	20,000	80,000

# Activity 7

Now complete the table for Jackie Charlton's assets – he uses the reducing balance method.



Balance sheet extract			
Cost	Dep'n to date	NBV	
£	£	£	£

### Reducing balance method

(Change in provision)

**Total**

**Provision**

**Expense in P&L a/c**

**Rate**

**Cost**

**Year**

	Year	Cost	Rate	Expense in P&L a/c	Provision
<b>Computers</b>	1	100,000	50%		
	2		50%		
	3		50%		
	4		50%		
	5		50%		

**Useful life**

	Year	Useful life
<b>Machinery</b>	1	25%
	2	25%
	3	25%
	4	25%

Now, let's move on to calculating the profit or loss when we sell (dispose) of an asset.

## Activity 8

Calculate the profit or loss on disposal for the following assets

- 1 A car cost £20,000 when purchased three years ago. The firm uses the straight line method of depreciation and estimates the useful life of a car to be 5 years. The car was sold this year for £8,000.

**Calculate the profit/loss on disposal**



- 2 A firm uses the reducing balance method of depreciation for its machinery using a rate of 50% per annum.

It bought one machine 3 years ago at a cost of £90,000.

It sold the machine this year for £12,500.

**Calculate the profit/loss on disposal.**

### Trading accounts

When we prepare accounts from incomplete records, it is a bit like doing a jigsaw. We have the pieces but we need to see where they fit together – to do this we look at the picture on the box to see what it will look like when we have finished. In the case of incomplete records the picture on the box is the final accounts – we need to know what goes where and how the accounts add up.

We will get some practice preparing trading accounts.

# Activity

## 9



Prepare the trading account for R Moore for the month of September 2009.

	<b>£</b>
Carriage inwards	70
Purchases	2,467
Returns inwards	231
Returns outwards	142
Sales	4,895
Stock at 1 October 2008	3,967
Stock at 30 September 2009	2,789



## Accruals and prepayments

As we have already said, the accounts we prepare will be based on the accruals concept and the amounts paid will need to be adjusted for accruals and prepayments.

### Tip

The accounting treatment for accruals (unpaid expense) is:

Add to the expense and include in current liabilities

The accounting treatment for a prepayment (expense paid in advance) is:

Deduct from the expense and include in current assets

Can you remember how to record accruals and prepayments in the ledger accounts?

## Activity

# 11



Record the following transactions in the Rent and Rates account of A Ball. Balance the account at 31 December 2007 and 31 December 2008 and show the amount transferred to the profit and loss account (income statement).

		£
1.1.07	Prepaid balance b/d (debit)	1,000
31.12.07	Payments for the year	14,000
31.12.07	Prepayment	3,000
31.12.08	Payments for the year	16,000
31.12.08	Prepayment	2,000

Look carefully at the accounts – can you explain the effect of the opening prepayment at 1 January 2007 and 1 January 2008 on the amount charged to the profit and loss account?

### Rent and rates

Rent and rates	

# Activity 12



Enter the following transactions in the wages account of R Hunt. Balance the account at 31 December 2007 and 31 December 2008 and show the amounts transferred to the profit and loss account.

		£
1.1.07	Accrued expense b/d (credit)	3,000
31.12.07	Payments for the year	15,000
31.12.07	Wages unpaid at the end of the year	4,000
31.12.08	Payments for the year	16,000
31.12.08	Wages unpaid at the end of the year	2,000

Look carefully at the accounts – can you explain the effect of the opening prepayment at 1 January 2007 and 1 January 2008 on the amount charged to the profit and loss account?

## Wages

---

--	--

### **You should now be able to:**

- Prepare cash accounts
- Prepare bank accounts
- Prepare control accounts
- Calculate depreciation using straight-line and reducing balance methods
- Calculate the profit or loss on the disposal of assets
- Prepare ledger accounts showing accruals and prepayments
- Prepare trading accounts
- Calculate gross profit margin and mark-up
- Prepare trading profit and loss accounts and balance sheets



Tick off each item – if you are not sure that you can do one then note below what you will do to make sure that you can!

### **Actions:**



## End of unit questions

### 1

Below is the schedule of fixed assets for Jaybon Ltd.

REQUIRED

- Calculate the cost, provision for depreciation and net book value at 30.09.09 and enter the figures in the fixed asset schedule.
- Calculate the profit or loss on the disposal of each category of asset.

	<b>Motor vehicles</b>	<b>Plant &amp; machinery</b>	<b>Fixtures &amp; fittings</b>	<b>Office equipment</b>
	<b>£</b>	<b>£</b>	<b>£</b>	<b>£</b>
Cost at 1.10.08	100,000	68,520	15,800	38,570
Depreciation at 1.10.08	25,000	32,820	12,800	28,570
<b>NBV at 1.10.08</b>	<b>75,000</b>	<b>35,700</b>	<b>3,000</b>	<b>10,000</b>
Cost of assets disposed during year	20,000	28,600	3,800	18,500
Proceeds of disposal	8,000	5,560	800	750
Depreciation on disposals	10,000	18,640	3,000	12,750
Additions at cost	40,000	42,600	5,000	36,500
<b>Depreciation policy</b>	20% pa straight line	15% pa straight line	25% pa reducing balance	50% pa reducing balance

	<b>Motor vehicles</b>	<b>Plant &amp; machinery</b>	<b>Fixtures &amp; fittings</b>	<b>Office equipment</b>
	<b>£</b>	<b>£</b>	<b>£</b>	<b>£</b>
Cost at 30.09.09				
Depreciation at 30.09.09				
<b>NBV at 30.09.09</b>				

**Profit/loss on disposal**

\*To calculate the charge for the year:

Straight line – calculate cost at end of year and multiply by depreciation rate, e.g. 20%.

Reducing balance –

- 1 Calculate cost at end of year.
- 2 Calculate depreciation left after taking away disposal.
- 3 Take depreciation in 2 away from cost in 1 and then multiply by percentage.

## 2

The following information has been extracted from the ledgers of Ken Tucky at 31 March 2006.

	£		£
Purchases	280,797	Bad debts	1,368
Sales	587,461	General expenses	33,713
Returns inwards	837	Premises at cost	145,000
Stock 1 April 2005	39,771	Equipment at cost	11,400
Wages	128,528	Motor vehicles at cost	42,000
Motor expenses	47,870	Provisions for depreciation at 1 April 2005	
Rates	7,810	Premises	46,400
Insurances	7,780	Equipment	6,840
		Motor vehicles	26,880

### Additional information at 31 March 2006

- 1) Stock was valued at £40,135.
- 2) A motor van purchased during the year for £18,500 has been included in the motor expenses account.
- 3) Wages remaining unpaid amounted to £1,383.
- 4) Insurances paid in advance amounted to £286.
- 5) Ken took goods to the value of £2,170 from the business for his own personal use.
- 6) Depreciation is to be charged at the following rates:
  - Premises at 2% per annum using the straight-line method.
  - Equipment at 10% per annum using the straight-line method.
  - Motor vehicles at 40% per annum using the reducing-balance method.

It is Ken's policy to charge a full year's depreciation on all assets held at the end of the financial year.

### REQUIRED:

Prepare the trading and profit and loss account (income statement) for Ken Tucky for the year ended 31 March 2006.

### 3

The trial balance of Dawson's Delicatessen together with additional information is shown below

#### Dawson's Delicatessen

##### Trial Balance as at 30.09.09

	£	£
Capital at 1.10.08		28,000
Plant & machinery	66,554	
Provision for dep – Plant		36,554
Cash at Bank	10,250	
Drawings	48,500	
Rent	16,500	
Provision for doubtful debts		1,500
General expenses	35,500	
Wages	38,920	
Debtors	38,775	
Creditors		25,654
Heat & light	3,654	
Sales		350,600
Purchases	170,850	
Stock at 1.10.08	10,340	
Insurance	2,465	
	<u>442,308</u>	<u>442,308</u>

##### Additional information

	£
Stock at 30.09.09	11,840
Wages owing at 30.09.09	1,020
Rent paid in advance	1,500
Heat & light owing	346
Bad debts to be written off	775

The provision for doubtful debts is to be 5% of debtors.

Depreciation is provided on plant and machinery at 25% pa using the reducing balance method.

#### REQUIRED:

Prepare the trading and profit and loss account for the year ended 30 September 2009 and a balance sheet at that date.

---

# Topic 1 Incomplete records

## Unit 1.2 Calculating profit

---

**On completion of this unit you should be able to:**

- Calculate profit by comparing opening and closing capital
- Evaluate the advantages and disadvantages of this method of calculating profit.
- Use a range of tools such as: cash accounts, bank accounts, total accounts, and ratios to find missing figures

**Read Chapter 2 of *AQA Accounting A2*.**

**Key term:**

- Statement of affairs: a simplified balance sheet used to calculate the capital figure

In this unit we look at the techniques available to an accountant when faced with a situation where the owner of the business has not kept full accounting records. Firstly we will see what we can do if the owner has not kept any records of the transactions during the year. We will then move on to the situation where the owner has kept some records and we will use a number of accounting techniques to find missing figures for the final accounts.

# The accountant's toolkit!

## Case study

Imagine you are an accountant! A stranger walks in to your office and says:  
*"Hi my name is Martin. I have been doing some buying and selling for the last year. You know buying some of this and selling some of that! Just making a few bob on the side. I've just received a letter from the Revenue and Customs saying that they have been told that I have been in business and they want me to complete a tax return showing how much profit I've made and paying income tax!! Someone has dobbed me in it!"*

You: "Have you kept any records? For instance; do you know what your sales are for the year?"

*NO!!*

Do you have any idea how much cash you have received or spent?

*No!! What can you do for me? Will I be investigated by the taxman? I've heard that they want to know where all your money has come from for years and years once they start!*

Yes they do. But I am sure we can work something out. Can you give me a list and the value of any assets – things you own – you started your business with? And the value of any assets and liabilities – amounts you owe- now?

*I think so...*

Then don't worry I can work out your profit – for a small fee!

## How can we work out the profit?

We need to go back to a technique we learned at the beginning of the AS course – the accounting equation

### Tip

Accounting equation is:  $\text{Assets} - \text{Liabilities} = \text{Capital}$

So if we know the assets and liabilities of the business we can work out the capital.

## Activity

# 1

Before we go on have a look at the balance sheet of a sole trader and write down below the Capital section of the balance sheet.





If you look at the capital section you will see that the difference between the opening capital and the closing capital is: Capital introduced; net profit and drawings. So if we know the opening and closing capital and drawings and any capital introduced we can work out the net profit for the year.

Let's see how this works!

Martin is able to provide you with the following information:

Assets at 1 September 2008	<b>£</b>
Computer valued at	600
Cash	200
Stock	<u>300</u>
	<u>1,100</u>

This means that Martin's opening capital was £1,100.

Assets at 31 August 2009	<b>£</b>
Computer valued at	400
Cash	150
Stock	<u>400</u>
	<u>950</u>

Martin's closing capital is £950.

Martin estimates that he has spent about £200 a week on going out, clothes etc using the money he made from buying and selling and that he hasn't put any of his own money into the business.

We can now calculate his profit:

		<b>£</b>
	Capital at end	950
<b>LESS</b>	Capital at start	<u>1,100</u>
<b>Equals</b>	change in capital	(150)
<b>LESS</b>	Capital introduced	
<b>ADD</b>	Drawings (200 x 52)	<u>10,400</u>
<b>Equals</b>	Net profit for the year	<u>10,550</u>



Before attempting Activity 2 make sure you understand the process by opening the spreadsheet that accompanies this unit. You will find a worked example similar to Activity 2. If you hover the cursor over the cells with the red triangles in the top corner you will be given an explanation of what is happening.

# Activity 2

On the following page is a table showing the assets and liabilities of a business – the owner has not kept full accounting records.

You should calculate the profit or loss for the years 2006-2009. The year 2005 has been completed for you as an example.

Incomplete records	Calculation of profit/loss for the year					
	2004	2005	2006	2007	2008	2009
	£	£	£	£	£	£
Fixed assets	4,520	4,165	3,965	5,265	9,645	8,445
Current assets	205	225	285	216	426	486
<b>Total assets</b>	<u>4,725</u>	<u>4,390</u>	<u>4,250</u>	<u>5,481</u>	<u>10,071</u>	<u>8,931</u>
Current liabilities	286	316	296	378	486	416
Long term liabilities	3,000	3,000	3,000	3,000	4,500	4,000
<b>Total liabilities</b>	<u>3,286</u>	<u>3,316</u>	<u>3,296</u>	<u>3,378</u>	<u>4,986</u>	<u>4,416</u>
<b>Capital</b>	<u>1,439</u>	<u>1,074</u>				
<b>Difference</b>		(365)				
<b>Add Drawings</b>		6,521				
<b>Less Capital introduced</b>		0				
<b>NET PROFIT FOR YEAR</b>		<u>6,156</u>				
Drawings for the year		6,521	8,210	9,610	10,248	14,860
Capital introduced		0	2,500	0	2,000	3,000

In practice the owner may provide you with a list of balances at the year end and you will have to decide which is an asset and which a liability. In exams these could include accruals, prepayments, debtors (trade receivables) and creditors (trade payables).

You need to prepare a **statement of affairs**. This is sort of summarised balance sheet – you do not need to distinguish between fixed and current assets or long term and current liabilities – you list all the assets and liabilities and then calculate the capital figure.

Let us have a look at an example.

Geoff has provided the following information about his business, Hurst Hat Tricks. The accounting year end is 31 December.

## Hurst Hat Tricks

Calculate the net profit for the year ended 31 December 2009

Assets and liabilities at 31 December 2009

	2008	2009
	£	£
Premises at cost	86,000	86,000
Fixtures at valuation	10,800	9,200
Motor vehicles at valuation	12,560	18,460
Stock	3,654	4,824
Trade debtors (trade receivables)	865	1,086
Trade creditors (trade payables)	7,892	8,794
Insurance paid in advance	1,200	600
Wages in arrears	80	118
Bank	2,564	14,865
Drawings for the year	24,000	28,000
Capital introduced in June 2009		15,500

To calculate the profit or loss for the year ended 31 December 2009 we first need to prepare an opening statement of affairs to calculate the capital at 31 December 2008 – this is the same as the capital at 1 January 2009.

## Hurst Hat Tricks

Statement of affairs at 31 December 2008

<b>Assets</b>	<b>£</b>
Premises at cost	86,000
Fixtures at valuation	10,800
Motor vehicles at valuation	12,560
Stock	3,654
Trade debtors	865
Insurance paid in advance	1,200
Bank	2,564
	<hr/>
	117,643
	<hr/>
<b>Liabilities</b>	
Trade creditors	7,892
Wages in arrears	80
	<hr/>
	7,972
	<hr/>
<b>Capital</b>	<hr/>
	109,671
	<hr/>

### Activity 3

Now prepare the statement of affairs at 31 December 2009 and calculate the profit or loss for Hurst Hat Tricks for the year ended 31 December 2009.



## Activity

# 4



Alan Ball has provided the following information relating to his business, Ballponds.

### Ballponds

Calculate the net profit for the year ended 31 October 2009

Assets and liabilities at	1 November 2008	31 October 2009
	£	£
Fixtures and fittings	14,560	18,650
Motor vehicles	6,452	14,862
Stock	865	1,465
Debtors (trade receivables)	2,689	1,898
Creditors (trade payables)	4,782	3,984
Bank	256	246 overdrawn
Rent paid in advance	480	360
Wages in arrears	140	328
Drawings for year	18,000	21,500

### Tip

Be careful with accruals and prepayments – remember accruals are liabilities and prepayments are assets – also look carefully at the bank. There is money in the bank at the beginning of the year – an asset. At the end of the year it is overdrawn – a liability.

# Activity 5

Jervaise has been giving haircuts for people at their homes, but has not kept any record of takings or expenditure. He has received a demand from the Revenue and Customs for income tax on his profits. Jervaise provides you with the following information at 6 April 2008 and 5 April 2009:



## Jervaise

	6 April 2008	5 April 2009
	£	£
Equipment	1,000	1,200
Stock of hair styling goods	70	45
Amounts owing from clients	60	72
Insurance paid in advance	100	80
Balance at bank	265	180
Amounts owing to suppliers	40	22
Motor expenses owing	20	35

Jervaise has taken £80 a week from the business for his own use.  
Calculate the profit or loss for the year ended 6 April 2009.

## Is it a good idea not to keep records?

You will probably think that the answer is no! But there are some advantages:

- You do not need any **expertise** – as you know keeping accounting records, particularly double entry is not easy – so not keeping records is easy!
- You do not waste any **time** – the time you use keeping records could be spent on your business earning you money.
- You can work out your profit.

However there are clearly disadvantages:

The major disadvantage is **the lack of information**. For instance you don't know your sales or expenses. This could lead to poor **decision making**, for instance you may be wasting money on advertising which is not bringing in any sales.

You are also likely to have to pay more to an accountant to work out your profit.

### Activity

## 6



Jervaise does not keep any accounting records for his hairdressing business. He pays an accountant each year to calculate his profit.

Evaluate this method of record keeping.

### Tip

When you are faced with a written question at A2 it is important to plan your answer.

In this case you will need to state the advantages and disadvantages of this method of record keeping. For each point you make you must give an example or develop your explanation – an example is shown in the text: the lack of information is the disadvantage and the examples are you don't know sales.

At the end you must assess the advantages and disadvantages and make a judgement – in general there is no wrong answer but you must justify your judgement.

For example you might say:

This is not a good method of record keeping (judgement) because of the lack of information (justification).

## What happens if the owner keeps some records?

### Case study

You work for an accountant and one of your clients is Sohit who owns a corner shop. Each year Sohit brings in his accounting records, they consist of:

- a bundle of invoices from his supplier – he buys on credit
- his cheque stubs
- his paying in book
- till rolls
- a few bits of paper with notes on what has happened during the year.

From this you have to prepare a trading and profit and loss account and balance sheet.

How will you do this?

### Use the accountant's toolkit!

Preparing the final accounts is a bit like putting together flat pack furniture – we know what the end product will look like, from the diagrams and picture on the instructions – in our case this is the layout of the trading and profit and loss account and balance sheet. We also need some tools – in the case of furniture this is the screwdriver and allen keys – for us it is our toolbox. So what have we got in our toolbox?

#### The accountant's toolbox:

- Cash accounts
- Bank accounts
- Control (total) accounts
- Ratios (gross profit mark-up and margin).

What we need to do is to see what information we have got and what we need to find out. If we think about Sohit's shop:

#### Information

Till rolls  
Invoices from suppliers  
Paying in book + cheque stubs

#### Final accounts

so we should know the sales figure  
purchases and creditors (trade payables)  
receipts and payments and bank balance

So what might be missing?

How much has Sohit taken out of his business? Has Sohit made any payments from cash before banking his takings?

## Cash accounts

We will use cash accounts to find missing figures. For example:

Before banking takings from his shop, Mushtaq has paid wages of £7,140 and taken drawings of £1,385. The total of cash banked for the year is £51,273. Mushtaq maintains a cash float of £50.

We need to work out the sales figure.

First we enter the transactions in the cash account.

Mushtaq Cash account			
	£		£
Balance b/d	50	Wages	7,140
		Drawings	1,385
		Cash banked	51,273
		Balance c/d	50

We can now work out the sales by balancing the account and inserting the missing figure e.g. Sales.

Mushtaq Cash account			
	£		£
Balance b/d	50	Wages	7,140
		Drawings	1,385
Sales (missing figure)	59,798	Cash banked	51,273
		Balance c/d	50
	<hr/>		<hr/>
	59,848		59,848
Balance b/d	50		



Look at the worksheet – CASH/CONTROL accounts for a further explanation.

### Activity

## 7

The owner of a business banks all cash sales except for wages and drawings. Wages for the year are £10,000. Cash sales were £50,000 and cash banked £25,750.

Prepare a cash account to find the owner's drawings.

## Tip

In the exam you may be asked to calculate the missing figure, in which case you can do this as a calculation e.g. adding and taking away the numbers.

However if you are asked to prepare an account you must prepare a T account – otherwise you will not earn all the marks.



## Activity

### 8

Yeuk Chan owns a shop selling Chinese medicines. A thief stole the cash from the till. She can provide you with the following information:

Cash sales amounted to £78,625. She has paid wages of £8,625 and taken drawings of £18,000 from the till. Cash banked during the year amounted to £50,750.

Prepare a cash account to find how much cash was stolen.



## Bank accounts

We can use bank accounts in a similar way to find missing figures. For example in the situation below we have been given details of receipts and payments but do not know how much the owner has withdrawn for their own use.

### Activity 9



Complete the bank account to find the amount of drawings.

Receipts	£	Payments	£
Takings	51,723	Balance b/d	648
		Payments to creditors	38,361
		Rent	3,400
		Rates	940
		Insurance	822
Balance c/d	6,287		

## Control (total) accounts – case study

Dave Mellor is a self employed builder, He has not kept a record of all the work done during the year. However, he does know how much he has received from customers and how much he is owed at the beginning and end of the year.

We can use a debtors control or total account to find the missing figure.

For example Dave provides the following information:

	Dave Mellor	
	At 1 Jan 1999	At 31 Dec 1999
	£	£
Trade debtors (trade receivables)	2,220	2,600
For the year to 31 December 1999:		
Cash sales	5,600	
Cash received from trade debtors	25,800	

We need to put the information we have into the total account.

Dave Mellor Debtors total account			
	£		£
Balance b/d	2,220	Cash received from debtors	25,800
		Balance c/d	2,600

Now we can calculate the sales figure by balancing the account.

Dave Mellor Debtors total account			
	£		£
Balance b/d	2,220	Cash received from debtors	25,800
Sales missing figure	26,180		
		Balance c/d	2,600
	<u>28,400</u>		<u>28,400</u>
Balance b/d	2,600		



Look at the worksheet – CASH/CONTROL accounts – for a further explanation.

## Activity 10

From the following information calculate the credit sales and credit purchases figures for the year ending 31 March 2009.

	At 1.4.08	At 31.03.09
	£	£
Trade debtors	14,640	16,100
Trade creditors	19,730	21,150
For the year to 31.3.09:		
Cheques sent to suppliers	168,000	
Discounts received	6,400	
Cash received from trade debtors	199,700	
Discounts allowed	4,820	

### Tip

If you are asked to calculate sales or purchases you do not have to prepare total accounts – you can calculate e.g:

Credit sales = Cash received from debtors + closing debtors – opening debtors.

Credit purchases = Cash paid to suppliers + closing creditors – opening creditors.

However, if you are asked to prepare a total account you must prepare a ledger account or you will lose marks.

# Activity

# 11



From the following information prepare debtors total account and creditors total account to find the credit sales and credit purchases for the year ended 30 September 2009.

	At 1.10.08	At 30.9.09
	£	£
Trade debtors	18,230	12,830
Trade creditors	15,640	16,540
For the year to 31.3.09:		
Cheques sent to suppliers	25,480	
Discounts received	720	
Cash banked from trade debtors	8,170	
Discounts allowed	420	
Bad debt during year	240	

## Ratios

### Case study

Martin Peters has a market stall selling fruit and vegetables. He buys the fruit and vegetables from a wholesaler and adds a mark-up of 20% to ensure he makes a profit. Many businesses operate with a standard mark-up, e.g. they add a fixed percentage to the cost of the product. We can use this information together with the trading account to find missing figures.

For instance if Martin has kept a record of his purchases and knows how much stock he has at the beginning of the year and end then we can work out his sales for the year.

Martin is able to give provide the stock and purchases figures – so we can put the information in to the trading account.

<b>Martin Peters</b>		Ratio	Mark-up 20%
		<u>Gross profit</u>	
Trading account		Cost of sales	
	<b>£</b>	<b>£</b>	
<b>SALES</b>			
Opening stock	50		
Purchases	15,890		
Closing stock	<u>75</u>		
<b>COST OF SALES</b>		15,865	100%
<b>GROSS PROFIT</b>		<u>          </u>	20%



Look at the worksheet –RATIOS – for an example.

Because we know the gross profit mark-up, we can work out the gross profit.

### Tip

Gross profit mark-up is:

$$\frac{\text{GROSS PROFIT}}{\text{COST OF SALES}} \times 100$$

**Martin Peters**

Ratio Mark-up 20%

			Gross profit ----- Cost of sales
	£	£	
Trading account			
SALES		19,038	
Opening stock	50		
Purchases	15,890		
Closing stock	75		
		-----	
COST OF SALES		15,865	100%
		-----	
GROSS PROFIT		3,173	20%
		-----	

The gross profit is 15,865 × 20%

Using the trading account we can then calculate the sales figure.

**Martin Peters**

Ratio Mark-up 50%

			Gross profit ----- Cost of sales
	£	£	
Trading account			
SALES		19,038	120%
Opening stock	50		
Purchases	15,890		
Closing stock	75		
		-----	
COST OF SALES		15,865	100%
		-----	
GROSS PROFIT		3,173	20%
		-----	

Sales = cost of sales + gross profit  
15,865 + 3,173

We can use the ratio percentages to work out the sales figure if we need.  
Because sales = cost of sales + gross profit.  
For example in this case sales = 120% of cost of sales (GP 20% + CoS 100%)



## Activity 12



- 1 Amr operates with a standard mark-up of 25%, his cost of sales is £10,000. Calculate his sales figure.

- 2 Bernard operates with a standard mark-up of  $33\frac{1}{3}\%$ , his cost of sales is £72,000. Calculate his sales figure.

### Tip

Be careful when calculating  $33\frac{1}{3}\%$  on your calculator – a lot of students use 0.3 to work it out (this is 30% not  $33\frac{1}{3}\%$ ). The easiest way is to divide by 3.

It is possible that a business could operate with a fixed profit margin.

### Tip

Gross profit margin is:

$$\frac{\text{GROSS PROFIT}}{\text{SALES}} \times 100$$

For example: Lan's business operates with a profit margin of 50%. Her sales for the year were £50,000. We can work out her gross profit

<b>Lan</b>		Ratio
Trading account		Gross profit margin 50%
	<b>£</b>	<b>£</b>
SALES		50,000      100%
Opening stock		
Purchases		
Closing stock		
COST OF SALES		0
GROSS PROFIT		25,000      50%

Gross profit margin is:  
 $\frac{\text{Gross profit}}{\text{Sales}} \times 100$   
 Lan's gross profit is  
 $\text{Sales} \times 50\%$   
 $5,000 \times 50\%$

If Lan does not know her purchases figure but has carried out a stock take at the beginning and end of the year, we can work out her purchases figure. The stock in last year's accounts was £1,850. The closing stock for the current year was valued at £1,950.

We can enter this information in the trading account and use it to find the purchases figure.

**Tip**  
 Last year's closing stock is this year's opening stock.

<b>Lan</b>		Ratio
Trading account		Gross profit margin 50%
	<b>£</b>	<b>£</b>
SALES		50,000      100%
Opening stock	1,850	
Purchases	25,100	
Closing stock	1,950	
COST OF SALES		25,000
GROSS PROFIT		25,000      50%

Cost of sales =  
 Opening stock  
 + purchases  
 - closing stock  
 So working backwards to find the missing purchases figure:  
 Cost of sales + closing stock  
 - opening stock  
 = purchases  
 $25,000 + 1,950 - 1,850 = 25,100$

Cost of sales = sales  
 - gross profit

## Activity 13



- 1 Cheuk operates with a fixed gross profit margin of 50%, his sales are £50,000. Calculate his gross profit.

- 2 Dale operates his business with a fixed gross profit margin of  $33\frac{1}{3}\%$ , his sales were £54,000. His opening stock was £4,580 and the closing stock was £5,480.

Calculate his gross profit.

Calculate his purchases figure.

In exams you are often given the gross profit mark-up but not enough information to work out the cost of sales. However, you know the sales figure. We can still work out the cost of sales because we can convert the mark-up to the gross profit margin and then work out the gross profit.

If we go back to the trading account and look at the relationship between Sales, Cost of sales and Gross profit and the ratios we can work out the margin.

	£	%	
Sales			Gross profit mark-up is 50%, so cost of sales = 100%
– Cost of sales		100	
= Gross profit		50	
	Mark-up	50	

	£	%	
Sales		150	Sales = cost of sales + gross profit Therefore in terms of % Sales = 100% + 50% = 150% Therefore the gross profit margin is $\frac{50}{150} = 33\frac{1}{3}\%$
– Cost of sales		100	
= Gross profit		50	
	Margin	33 $\frac{1}{3}$	

## Activity

# 14



Complete the table below converting the gross profit mark-up to the margin

	£	%	%	%	%
Sales					
– Cost of sales		100			
= Gross profit		50			
	Mark-up	50%	100%	33 $\frac{1}{3}$	25%

	£	%
Sales		150
– Cost of sales		100
= Gross profit		50
	Margin	33 $\frac{1}{3}$

Let's see how this would work in a question. Ying owns a corner shop. Her accounting year end is 31 December, during the Christmas holiday her shop was broken into and some stock stolen; Ying does not know how much was taken. She provides you with the following information:

Sales for the year: £88,668  
 Stock at 1 January 2008: £2,380  
 Purchases for the year: £59,645

She marks up all her stock by 50% to set the selling price.

She has counted the stock left in the shop and this was valued at £1,800.

First we will draw up a trading account and enter the information we have.

**Ying**

Trading account

	£	£
SALES		88,668
Opening stock	2,380	
Purchases	59,645	
Closing stock	_____	
COST OF SALES		_____
GROSS PROFIT		_____

Now we need to work out the gross profit margin.

**Ying**

Trading account

	£	£	
SALES		88,668	
Opening stock	2,380		
Purchases	59,645		
Closing stock	_____		
COST OF SALES		_____	100%
GROSS PROFIT		_____	50%

Mark-up is 50%  
 Gross profit = 50% of cost of sales  
 Therefore cost of sales = 100%  
 Sales = 150%  
 The gross profit margin is  
 $\frac{\text{Gross profit}}{\text{Sales}} = \frac{50}{150} = 33\frac{1}{3}\%$

We can now calculate the gross profit.

**Ying**

Trading account

	£	£	Ratio
SALES		88,668	150%
Opening stock	2,380		
Purchases	59,645		
Closing stock	_____		
COST OF SALES			
GROSS PROFIT		<u>29,556</u>	33 $\frac{1}{3}$ %

Gross profit =  
sales x 33 $\frac{1}{3}$  %  
88,668 ÷ 3 =  
29,556

We can now calculate the cost of sales.

**Ying**

Trading account

	£	£
SALES		88,668
Opening stock	2,380	
Purchases	59,645	
Closing stock	_____	
COST OF SALES		59,112
GROSS PROFIT		<u>29,556</u>

Cost of sales  
= sales – gross  
profit

Now we work out how much the closing stock should be.

**Ying**

Trading account

	£	£
SALES		88,668
Opening stock	2,380	
Purchases	59,645	
Closing stock	<u>2,913</u>	
COST OF SALES		<u>59,112</u>
GROSS PROFIT		<u>29,556</u>

The closing stock should be £2,913  
We work this out:  
Cost of sales  
– opening stock –  
purchases = closing  
stock  
59,112 – 2,380  
– 59,645 = 2,913

So, the closing stock should have been £2,913 and the actual amount in the shop was £1,800. The stolen stock amounts to £1,113.

**Activity  
15**

**1**

Sales	£100,000
Opening stock	£10,000
Purchases	£80,000
Mark-up $33\frac{1}{3}\%$	

Calculate the closing stock.



**2**

Sales	£100,000
Opening stock	£15,000
Closing stock	£10,000
Mark-up 25%	

Calculate purchases.

- 3 Jeremy owns a CD shop. During the year ending 30 October 2009 he had a break-in and some CDs were stolen – he does not know the value of the stolen stock. Jeremy operates on a standard mark-up of 100%. He provides you with the following details:

Sales	£120,000
Purchases	£60,286
Opening stock	£6,854
Closing stock	£5,954

Calculate the value of the stolen stock.

- 4 Lesley owns a shoe shop. She operates on a standard mark-up of 50%. During the year ended 30 June 2009 her basement stock room was flooded and some stock destroyed. She provides you with the following information.

Sales	£90,000
Purchases	£61,850
Opening stock	£7,561
Closing stock	£3,000

Calculate the value of the stolen stock.

- 5 Harvey owns a shop selling suits. He operates a standard mark up of 200% on cost. On Saturday night there was a fire in the storeroom and the suits in there were destroyed. He wants to claim the loss on his insurance but does not know the value of the suits lost. He provides you with the following information.

Sales	£66,000	
Purchases	£20,684	
Opening stock	£5,684	
Closing stock	£542	(on display in shop)

Calculate the value of the stock for the insurance claim.



**You should now be able to:**

- Calculate profit by comparing opening and closing capital
- Evaluate the advantages and disadvantages of this method of calculating profit
- Use a range of tools such as: cash accounts, bank accounts, total accounts, and ratios to find missing figures



Tick off each item – if you are not sure that you can do one, then note below what you will do to make sure that you can!

**Actions:**



## Exam-style questions

### 1

Kath Phillips does not maintain a complete accounting system. She provides the following information.

	As at 1 April 2002	As at 31 March 2003
	£	£
Trade debtors (trade receivables)	4763	4680
Trade creditors (trade payables)	3100	3450
Stock (inventory)	2460	5710

Additional information:

The following occurred during the year ended 31 March 2003.

- (i) All purchases and sales were on credit.
- (ii) Cash paid to suppliers was £21,080. Receipts from customers were £67,350.
- (iii) Two customers who owed a total of £130 went into liquidation and the balances on their accounts were written off as bad debts. In the light of this, Kath decided to create a provision for doubtful debts of 5% based on the debtors outstanding at the year end.

#### REQUIRED:

Prepare the trading account for the year ended 31 March 2003.

(11 marks)

### AQA Acc5 June 2003 Question 2

### 2

Sharon Segg started a woodworking business on 1 December 2001 with net assets valued at £87,000.

She has been so busy she did not keep any financial records during the year. However, Sharon is able to give you the following information as at 30 November 2002.

	£
Premises at valuation	47,000
Machinery at net book value	21,600
Van at net book value	12,000
Money owed by customers	1,090
Money owed to suppliers	7,450
Stocks of timber etc	5,700
Bank overdraft	640

During the year Sharon withdrew £9,450 in cash from the business for her own private use. She also used timber valued at £1,000 to make improvements to her home.

**REQUIRED:**

(a) Calculate her net profit for the year ended 30 November 2002.

*(8 marks)*

(b) Evaluate the advantages and disadvantages of the method that you used to determine net profit.

*(6 marks)*

**AQA Acc5 January 2003 Question 2**

**3**

Tom Stoddart set up an office cleaning business on 1 March 2003.

He did not keep a full set of bookkeeping records. He was, however, able to supply the following information which related to the financial year ended 29 February 2004.

A bank overdraft of £42 was shown on the business bank statement at 29 February 2004.

At 29 February 2004 there was an unpresented cheque for £38.

Cheques totalling £720 paid into the bank on 29 February did not appear on the bank statement.

**REQUIRED:**

(a) Prepare a bank reconciliation statement at 29 February 2004 to determine Tom's bank balance at that date.

*(5 marks)*

(b) Advise Tom on the benefits of preparing a bank reconciliation statement on a regular basis.

*(6 marks)*

Tom's opening capital on 1 March 2003 was £32,000.

His assets and liabilities at 29 February 2004 were:

	£
Machinery at valuation	46,000
Two vehicles at valuation	34,000
Loan from Eliza, a friend	20,000
Stock of cleaning materials	380
Amounts outstanding for the purchase of cleaning materials	180
Amounts owed by customers	1,870
Bank balance	?

During the year, Tom:

- took £14,184 cash from the business for his private use;
- took cleaning materials to the value of £96 for use in his home;
- received a gift of £15,000 from his mother, which he paid into the business bank account.

**REQUIRED:**

(c) Calculate Tom's net profit for the year ended 29 February 2004.

(Note: a profit and loss account is **not** required.)

*(10 marks)*

(d) (i) Calculate Tom's return on capital employed.

*(2 marks)*

(ii) Comment on your result.

*(3 marks)*

**AQA Acc5 June 2005 Question 3**

**4**

Pat Parker is a butcher. She marks up all goods sold in her shop by 100%. All takings are banked each evening after the shop is closed.

During the year ended 31 December 2004, £93,322 was banked. Par believes that some cash is missing from the till on 31 December 2004. She is unable to determine the exact amount but provides the following information.

	£
Stock at 1 January 2004	890
Stock at 31 December 2004	950
Purchases	46,753
Debtors at 1 January 2004	2,786
Debtors at 31 December 2004	2,640

**REQUIRED:**

Calculate the amount of cash missing from the till on 31 December 2004.

*(9 marks)*

**AQA Acc5 January 2005 Question 2**

