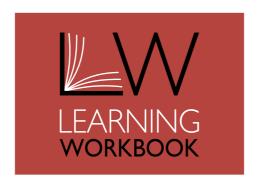
Full Answers

for

Level 2 Accounting Learning Workbook

Anne Dick





Full Answers for Level 2 Accounting Learning Workbook

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Answers

Activity 1A: Analysing transactions (page 3)

	, , ,					
1.	Bank	Α	Inventory	Α	Loan	L
	Insurance	Ex	Rent received	I	Accounts receivable	Α
	Shop wages Ex		Accounts payable	L	Advertising	Ex
	Mortgage L Sales I Interest on mortgage Ex GST payable L Bank overdraft L		Purchases	Ex	Drawings	Eq
			Vehicles	Α	Fees received	I
			Interest on term deposit	I	Depreciation on vehicles	Ex
			Furniture	Α	Accrued expenses	L
			GST receivable	Α	Accountancy fees	Ex
	Prepayments	Α	Goodwill	Α	Capital	Eq
					·	

2. a.

a.	Bank	Accounts receivable	Furniture/ Equipment	Expenses	Accounts payable	Loan	Capital	Income
i.	+3 000		+1 000				+4 000	
ii.	-276		+276					
iii.	-300			+300				
iv.	+4 600							+4 600
V.				+368	+368			
vi.	-500						-500	
vii.	-184			+184				
viii.				+92	+92			
ix.		+138						+138
х.	-600			+200		-400		
xi.	-480				-500	·		+20
xii.	+90							+90

	Account name	Element	Increase/ Decrease	Debit/ Credit	Amount \$
i.	Bank	Asset	Inc	Dr	3 000
	Furniture	Asset	Inc	Dr	1 000
	Capital	Equity	Inc	Cr	4 000
ii.	Furniture	Asset	Inc	Dr	240
11.	GST	Liability	Dec	Dr	36
	Bank	Asset	Dec	Cr	276
iii.	Wages	Expense	Inc	Dr	300
	Bank	Asset	Dec	Cr	300
iv.	Bank	Asset	Inc	Dr	4 600
	GST	Liability	Inc	Cr	600
	Fees received	Income	Inc	Cr	4 000
V.	Supplies	Expense	Inc	Dr	320
	GST	Liability	Dec	Dr	48
	Accounts payable	Liability	Inc	Cr	368
vi.	Drawings	Equity	Dec	Dr	500
	Bank	Asset	Dec	Cr	500
vii.	Electricity	Expense	Inc	Dr	160
	GST	Liability	Dec	Dr	24
	Bank	Asset	Dec	Cr	184
viii.	Telephone	Expense	Inc	Dr	80
	GST	Liability	Dec	Dr	12
	Accounts payable	Liability	Inc	Cr	92
ix.	Accounts receivable	Asset	Inc	Dr	138
	GST	Liability	Inc	Cr	18
	Fees received	Income	Inc	Cr	120
х.	Loan	Liability	Dec	Dr	400
	Interest on loan	Expense	Inc	Dr	200
	Bank	Asset	Dec	Cr	600
xi.	Accounts payable	Liability	Dec	Dr	500
AI.	Discount received	Income	Inc	Cr	20
	Bank	Asset	Dec	Cr	480
xii.	Dividends	Income	Inc	Cr	90
	Bank	Bank	Inc	Dr	90

3.	Transaction	Capital	Revenue
	Purchase new cash register	~	
	Paid for installation of cash register	~	
	Paid shop assistant's wages		~
	Painted wall to remove graffiti		V
	Paid for new shelves to display the books	~	
	Paid for monthly advertising		~
	Paid for new sign for the front of the store	~	

Activity 1B: Preparation of financial statements (page 10)

Petra's Picture Framing Income Statement for the year ended 30 June 2020					
Revenue					
Fees received			136 800		
Other income					
Discount received			<u>620</u>		
			137 420		
Less Expenses					
Framing expenses					
Advertising	1 260				
Wages – framers	35 500				
Supplies used	50 000				
Depreciation on framing equipment	9 000				
Rent – framing	<u>17 500</u>	113 260			
Administrative expenses					
General expenses	800				
Electricity	650				
Insurance	900				
Rent – office	7 500				
Stationery	3 000				
Telephone and fax	1 070				
Depreciation on office furniture	<u>1 950</u>	15 870			
Finance costs					
Interest on loan	<u>1 100</u>	<u>1 100</u>			
Takal annuana			(120.222)		
Total expenses			(130 230)		
Profit for the year	1		<u>\$7 190</u>		

Petra's Picture Framing Statement of Financial Position as at 30 June 2020					
Assets					
Current assets					
Accounts receivable		2 900			
Bank		3 000			
GST		3 218			
Supplies on hand		1 500			
Prepayments		<u>240</u>	10 858		
Non-current assets					
Intangible assets					
Goodwill		4 000			
Property, plant and equipment (Note 1)		<u>39 650</u>	43 650		
Total assets			54 508		
Less Liabilities					
Current liabilities					
Accounts payable	1 938				
Accrued expenses	500				
Income in advance	3 200	5 638			
Non-current liabilities					
Loan	<u>5 000</u>	5 000			
Total liabilities			(10 638)		
Net assets			\$ 43 870		
Equity					
Opening capital			45 680		
+ Profit for the year			7 190		
– Drawings			(9 000)		
Closing capital			\$ 43 870		

Note 1 - Property, plant and equipment

	Framing equipment	Office furniture	Total
Cost	65 000	13 000	78 000
Accumulated depreciation	(32 800)	<u>(5 550)</u>	(38 350)
Carrying amount	32 200	7 450	<u>39 650</u>

Depreciation is calculated on the straight-line basis at the following rates:

- Framing equipment \$9 000 p.a.
- Office furniture at 15% of cost p.a.

Cross Town Couriers Income Statement for the year ended 31 March 2021					
Revenue					
Fees received			164 000		
Other income					
Gain on sale of furniture		600			
Dividends		<u>420</u>	<u>1 020</u>		
			165 020		
Less Expenses					
Courier expenses					
Advertising	1 500				
Supplies used	20 000				
nsurance – vehicles	6 450				
Petrol and oil	45 360				
Wages – courier drivers	45 000				
Depreciation on vehicles	9 600	127 910			
Administrative expenses					
Electricity	1 110				
Insurance – general	2 150				
Telephone and fax	1 050				
General expenses	2 500				

1 000

800

<u>1 750</u>

150

1 100

10 360

1 250

(139 520)

\$ 25 500

Discount allowed

Finance costs

Depreciation on buildings

Interest on overdue account

Interest on mortgage

Total expenses

Profit for the year

Depreciation on furniture and fittings

Cross Town Couriers Statement of Financial Position as at 31 March 2021					
Current assets					
Accounts receivable		6 200			
Bank		4 130			
Supplies on hand		500			
Accrued income		120			
Prepayments		<u>540</u>	11 490		
Non-current assets					
Intangible assets					
Goodwill		2 000			
Property, plant and equipment (Note 1)		74 350			
Investment assets					
Shares in <i>Drivers Ltd</i>		<u>15 000</u>	91 350		
Total assets			102 840		
Less Liabilities					
Current liabilities					
Accounts payable	1 984				
Accrued expenses	1 100				
GST	<u>816</u>	3 900			
Non-current liabilities					
Mortgage	25 000	<u>25 000</u>			
Total liabilities			(28 900)		
Net assets			\$73 940		
Equity					
Opening capital			60 440		
+ Profit for the year			25 500		
– Drawings			(12 000)		
Closing capital			\$ 73 940		

Note 1 - Property, plant and equipment

	Vehicles	Furniture and fittings	Buildings	Total	
Cost	48 000	8 000	35 000	91 000	
Accumulated depreciation	(11 400)	(3 500)	<u>(1 750)</u>	(16 650)	
Carrying amount	36 600	4 500	33 250	74 350	

Depreciation is calculated on the straight-line basis at the following rates:

- Vehicles 20% p.a.
- Furniture and fittings \$800 per year
- Buildings 5% of cost per year

for the month ended	30 Septeml	ber 2023
Receipts		
Interest received	150	
Cash sales	12 000	
Cash from debtors	<u>1 850</u>	14 000
Payments		
Cash to suppliers	4 300	
Electricity	360	
Wages	1 800	
Drawings	3 000	
Van insurance	<u>180</u>	(9 640)
Net increase in cash		4 360
Opening bank balance		<u>2 700</u>
Closing bank balance		7 060
	Cash Flow of the month ended Receipts Interest received Cash sales Cash from debtors Payments Cash to suppliers Electricity Wages Drawings Van insurance Net increase in cash Opening bank balance	Interest received

Activity 2A: Accounting information (page 19)

- To communicate financial information to interested parties in order to help with decision making.
- a. Examples include: value of existing liabilities; liquid ratio; equity ratio; current value of inventory; value of security; expected profit of café.
 - b. Examples include: existing customer base; existing café competition in the area; length of time Daisy will have to close the garden store to build the café; how long it will take to build the café.
 - c. 'Security' refers to the assets the business has, in relation to existing liabilities. This information is required in case the bank needs to secure the loan so that it will have the right to sell Daisy's assets if she doesn't repay her loan on time.
- a. Non-financial information the names and phone numbers of existing suppliers have nothing to do with money.
 - b. This information will enable Coffee Beans Co. to find out whether or not Daisy's Garden Store has a good credit history and repays its debts on time. This will help it decide whether or not to give Daisy credit and what her credit limit will be.
 - Examples include: value of existing liabilities; how much profit the business made last year; current ratio.

Activity 2B: Financial statements (page 22)

	3	,	
1.	Transaction	Capital	Revenue
	Purchased new oven	~	
	Paid for installation of oven	~	
	Paid café assistants' wages		~
	Paid for advertising of the new café		~
	Paid for the ingredients and food for the café		~

- a. The purchase of the fridge is a 'one-off' type expenditure, and the
 fridge is expected to be of benefit to the café for more than the
 current accounting period, because Daisy's Garden Store will use
 the fridge for several years to store drinks which will be sold to
 customers.
 - b. Insurance is an ongoing expense that the café will need to pay every year, which does not create an asset. The benefit of the insurance premium is for the current year only.

- Current liabilities are those liabilities which Daisy's Garden Store will have to repay in the next financial year (12 months). Non-current liabilities are those liabilities that will still be outstanding beyond the next accounting period (it will take longer than the next accounting year to repay them).
- a. To calculate the profit (deficit) of Daisy's Garden Store for the accounting period – Daisy can then compare this figure with that of last year to see if the profit improved or not.
 - b. The depreciation / doubtful debts is an estimate, and therefore the profit for the period may not be accurate; or the Income Statement does not include non-financial information (e.g. quality of staff, customer base).
- a. To calculate the assets, liabilities, and equity of Daisy's Garden Store on the balance date.
 - b. The accumulated depreciation / allowance for doubtful debts is an estimate, and therefore the carrying amounts of the assets may not be accurate; or the age of the assets is not included, therefore the decision being made may not be accurate; or the values of the assets are based on historical cost, which might be out of date and not reflect the current market value of the assets.
- 6. a. To report the sources of money received, and what money was spent on during the period; the Cash Flow Statement also shows how the change in bank balance occurred during the period, and what the balance is on balance date.
 - b. The Cash Flow Statement does not show credit transactions (e.g. credit purchases) or include non-cash items (e.g. depreciation); or the Cash Flow Statement is based on past cash receipts and payments and does not show current cash obligations.
- 7. Café wages are a 'distribution cost' because they are paid to staff who are involved in the promotion and selling of the inventory of Daisy's Garden Store/Café, whereas office salaries are an administrative cost because they are paid to the employees who work in the office and perform the administrative tasks of the business.
- 8. The purpose of the Statement of Accounting Policies is to inform the users of the financial statements how the statements have been prepared and what measurement basis and assumptions have been used. The bank manager will use this information to (for example) know that the assets are based on historical cost, not market value, and the Cash Flow Statement will help the bank manager to decide whether to lend more money to Patrick's Plumbing.

Activity 2C: Depreciation (page 25)

- The systematic allocation of the depreciable amount of the asset over its useful life.
- The diminishing-value method is used when the loss of the 'future economic benefit' / economic benefit of the equipment is greater in the earlier years of its life and reduces as it ages; that is, the depreciation amount is biggest in the early years and gets progressively smaller.
- The straight-line method is used when the loss of future economic benefit of the furniture is consistent (the same) each year over the life of the furniture; that is, the depreciation amount is the same each year.
- 4. The units-of-use method is used when the loss of future economic benefit of the vehicles varies in direct proportion to how often the vehicles are used. The more they are used, the more they depreciate, which reflects the greater loss in economic benefit of the vehicles in the future.

Activity 3A: Accounting notions and assumptions (page 27)

- 1. The period reporting concept requires a business, such as Ruth's Records and Relics, to divide its trading 'life' into equal periods. This means that the profit for the year for Ruth's Records and Relics can be calculated and compared with that of previous years. This information will indicate, for example, whether the business's performance has improved.
- The period reporting concept requires a business, such as Ruth's Records and Relics, to divide its trading 'life' into equal periods. By reporting the

- business's Statement of Financial Position on the same day each year, Ruth can compare the financial position of *Ruth's Records and Relics* with its position the previous year, and see whether the value of the equity, assets or liabilities has increased or decreased.
- 3. Ruth will need to record the business insurance \$840 as a business expense that will be reported in the Income Statement of Ruth's Records and Relics. The personal insurance needs to be recorded as 'drawings' \$600, and will appear in the equity section of the Statement of Financial Position. This is because the accounting entity concept requires Ruth to keep her personal financial transactions separate from those of the business. Doing this ensures that the Income Statement reports expenses of only Ruth's Records and Relics, and not the owner's personal expenses.
- The monetary measurement concept requires Ruth to record the inventory NZ\$4 400 in New Zealand dollars, because this is the currency of Ruth's Records and Relics.
- Either: In terms of the going concern concept, because Ruth has no intention of selling Ruth's Records and Relics in the foreseeable future, the equipment should be recorded at its historical cost (that is, its original purchase price) of \$5 600.
 - *Or:* In terms of the historical cost concept, all assets are required to be recorded at their original acquisition cost, which means the equipment must be recorded at \$5 600.
- 6. The accrual basis concept requires transactions to be reported in the financial statements of the period to which they relate. The money received for the orders has not yet been earned, so the amount of 'sales' must be reduced by \$420 to report the amount actually earned in this period in the Income Statement. The amount received in advance is recorded as the current liability 'income in advance' \$420 in the Statement of Financial Position in order to report liabilities accurately on balance date.

Activity 3B: Qualitative characteristics of Accounting (page 30)

- The information may not be in a form that can be easily understood, therefore is not useful for decision making.
- 2. The concept of faithful representation has been met since the information is free from bias the shoebox of receipts provides independent verification (evidence/proof) that transactions took place (i.e. the information is neutral) and that the information in the financial statements faithfully represents the events and transactions of this financial year.
- 3. The concept of faithful representation might have been broken because your friend has provided you with the information and the friend is not independent and therefore not free from bias. Your friend might have deliberately left out information showing negative aspects of the business's performance.
- 4. The concept of relevance requires information to be useful for decision making. As the information is six months old, it is now out of date and will not be good for providing information to evaluate present or future events.
- 5. For comparability, it is important to have financial information from the previous financial year in order to identify trends and judge similarities in and differences between the business's position then and now. The business should have provided financial statements with at least two years' information.
- 6. The concept of materiality allows the desk to be recorded as an expense because the value of the desk, \$120, is small and the desk is not important in nature; therefore, how the desk is treated (recorded) will not influence the decisions being made by users of the accounting records.
- a. The van should be recorded at \$18 000 because this is the original acquisition cost of the vehicle.
 - b. For the information to be most useful for decision making, the most up-to-date value (\$3 000) should be recorded. This gives the most relevant information when evaluating present or future events.

c. The most reliable valuation for the van is \$18 000 because this is free from bias, and faithfully represents the transaction that took place when the van was purchased. The evidence for this value is provided by the invoice (or receipt) issued when the van was purchased.

Activity 3C: Elements of financial statements (page 33)

- a. Ruth's Records and Relics controls the use of the inventory and has exclusive rights to sell inventory and benefit from the proceeds.
 - b. Ruth's Records and Relics purchased and paid for the inventory at some time in the past.
 - c. Ruth's Records and Relics will sell the inventory to customers at a higher price than it paid for inventory, which generates revenue in the form of sales.
 - d. It is probable (that is, there is a greater than 50% chance) that the inventory will generate sales and that cash will flow to Ruth's Records and Relics when the customers pay for the inventory they buy.
 - e. Ruth's Records and Relics can measure the value of the inventory, because Ruth will have an invoice or receipt as proof that the amount paid for the inventory was \$12 000.
- a. The mortgage will require a future sacrifice of economic benefits in the form of decreasing the asset Bank, when the mortgage is repaid in the future.
 - Ruth's Records and Relics received the money from the mortgage in the past.
 - c. Ruth's Records and Relics is currently obliged to repay the financial institution because it has a legal obligation to do so in terms of the mortgage agreement.
 - d. It is probable (that is, there is a greater than 50% chance) that there will be an outflow of resources embodying economic benefits because *Ruth's Records and Relics* must use money in its bank account to pay off the mortgage in the future.
 - e. The amount of the mortgage can be measured with reliability because the mortgage document and bank statements will verify (prove) the amount that must be paid (currently this is \$60 000).
- a. Sales are an increase in economic benefits for Ruth's Records and Relics by increasing the asset, Bank, if they are cash sales; or increasing Accounts receivable, if the sales are made on credit.
 - Sales increase the profit of Ruth's Records and Relics for the period, which increases equity.
 - c. Sales are not a contribution made by Ruth.
 - d. The sales have taken place, either the asset, Bank, or the business's Accounts receivable has increased in this period.
 - e. The value of the sales can be measured reliably because the amount can be verified by receipts or invoices, this year totalling \$133 000.
- a. Electricity decreases economic benefits of Ruth's Records and Relics
 by decreasing the asset, Bank, when the electricity account is paid
 (or by increasing the Accounts payable liability when the account is
 received).
 - Electricity decreases the profit for the year, which in turn decreases equity.
 - c. The electricity is for Ruth's Records and Relics and is not a distribution to the owner (that is, it is not drawings).
 - d. The electricity has been used by Ruth's Records and Relics in this accounting period and this has resulted in a decrease of the asset, Bank, when the electricity is paid for (or an increase in the Accounts payable liability when the account is received).
 - e. The amount of the electricity can be proven because *Ruth's Records*and *Relics* will have copies of the electricity statements totalling
 \$8,000
- 5. a. The vehicle is an asset for Stacey's Spik 'n Span because Stacey's Spik 'n Span controls the use of the vehicle; has exclusive rights to use it, and decides how it is used. This is because Stacey's Spik 'n Span purchased and paid for the vehicle at some time in the past. Stacey's

- Spik 'n Span will use the vehicle to help provide cleaning services that customers will pay for, which generates revenue in the form of fees. It is probable (that is, there is a greater than 50% chance) that the vehicle be used to generate fees and that cash will flow to Stacey's Spik 'n Span when the customers pay for the cleaning services. Stacey's Spik 'n Span can measure the value of the vehicle because the owner, Stacey, will have an invoice or receipt as proof of the amount that was paid to purchase the vehicle.
- b. The loan is a liability because it will require a future sacrifice of economic benefits in the form of decreasing the asset, Bank, when the loan is repaid. Stacey's Spik 'n Span received the loan in the past, and it is currently obliged to repay the financial institution because the loan agreement states it must. It is probable (that is, there is a greater than 50% chance) that there will be an outflow of resources embodying economic benefits, because Stacey's Spik 'n Span must use money in its bank account to pay off the loan in the future. The amount of the loan can be measured with reliability because the loan document and bank statements will verify (prove) the amount to be paid.
- c. Fees received increase economic benefits for Stacey's Spik 'n Span by increasing the asset, Bank, if cash is paid for the cleaning jobs; or by increasing Accounts receivable, if the cleaning services are performed on credit. Fees received increase the profit of Stacey's Spik 'n Span for the period, which increases equity. Fees received are not a contribution from the owner, Stacey. The fees have in fact been received, so the asset, Bank, or Accounts receivable of Stacey's Spik 'n Span has increased in this period. The value of the fees can be measured reliably because the amount can be verified by receipts or invoices.
- d. Supplies are an expense because they decrease the economic benefits in the form of decreasing the asset, Bank, when the supplies are paid for (or increasing the Accounts payable liability when the account is received) of Stacey's Spik 'n Span. Buying supplies decreases the profit for the year, which in turn decreases equity. The supplies are for Stacey's Spik 'n Span and are not a distribution to the owner (that is, are not drawings). The supplies have been used by Stacey's Spik 'n Span in this accounting period to help generate the cleaning revenue. Purchasing supplies has decreased the asset, Bank, when the supplies were paid for (or increased the Accounts payable liability when the account was received). The amount of the supplies used this year can be proven because Stacey's Spik 'n Span will have copies of the receipts and invoices.
- 6. The equipment is an asset for Stacey's Spik 'n Span because the business purchased it in the past, online from Australia. Stacey's Spik 'n Span has exclusive rights to use and control the cleaning equipment to clean houses for customers who will pay for the service, generating future economic benefit which increases the bank account and fees received. It is probable, as a greater than 50% likelihood, that Stacey's Spik 'n Span will use the equipment to clean customers' houses, or the business would not have purchased the equipment. The value of \$NZ4 400 can be measured reliably, because the credit card statement will show this cost, and it is converted from Australian dollars into New Zealand dollars in accordance with the monetary measurement because Stacey's Spik 'n Span is based in New Zealand and NZ\$ is the common unit. The cleaning equipment will be reported as a non-current, property plant and equipment asset because Stacey's Spik 'n Span intends to operate into the foreseeable future in accordance with the going concern concept.

Activity 4: (page 37)

- a. The current and non-current liabilities as reported in the Statement
 of Financial Position show the bank's lending officer the value of
 PhotoCentre's existing liabilities both in the short term and in the
 long term. If the existing liabilities are too high, the bank might not
 lend the money as PhotoCentre is not a good risk.
 - b. The insurance paid in advance will be reported as the current asset,

- Prepayments'. This is because the insurance that hasn't been used belongs in the records of the next financial year, represented by this asset. This is to ensure that transactions are recognised when they occur, and that assets and liabilities are reported in the financial statements of the period to which they relate.
- c. Period reporting requires the life of the business to be broken up into periods of equal length for reporting purposes. The Income Statement for *PhotoCentre* illustrates this idea as it shows the life of the business is broken up into one-year lengths, ending on 31 March each year. This makes it possible for users of *PhotoCentre*'s Income Statement to calculate its profit for the year and compare it with that of the previous year. This helps users make financial decisions.
- d. i. Units-of-use method.
 - ii. 'Units of use' depreciates the developing equipment in direct proportion to how much the equipment is used. The more photos that are developed, the greater the depreciation expense will be. This is in line with the loss of future economic benefit (which is in direct relation to how many photos are developed) and is therefore the best method to use.
 - iii. Depreciation on photo developing equipment is recorded as an expense in *PhotoCentre*'s financial statements because the depreciation is a decrease in the property, plant and equipment assets of the business. The depreciation also decreases the business's profit, which in turn decreases equity. The depreciation is not a distribution to the owner, Mark.
- e. Faithful representation requires information to be free from bias, and correct and neutral; therefore, using faithful representation would record the photo frames at a value of \$2 000. This figure is reliable, as there is a source document (for example, a receipt) to prove it. Relevance requires information to help users evaluate and confirm past events and make predictions about the future. The most relevant value for decision making is the current value / net realisable value of \$500, therefore a conflict arises. In this case it is more important to record the value of the photo frames at the lower of cost or net realisable value, which is \$500.
- f. The purchase of the new display cabinet is recorded as capital expenditure in *PhotoCentre's* accounting records because the purchase is a one-off type purchase which will benefit (that is, generate income for) the entity for more than one financial year because *PhotoCentre* will use the cabinet to display cameras which customers will buy for more than one accounting period.
- g. i. Accounts payable are a liability of PhotoCentre because they represent a current obligation to repay the suppliers from whom they purchased the cameras on credit in the past. There will be a future sacrifice of economic benefits in the form of decreasing the asset, 'Bank', when the Accounts payable are repaid in the future.
 - ii. The Accounts payable are reported in the Statement of Financial Position because they meet the two recognition criteria. It is probable that an outflow of resources embodying economic benefits will result from the present obligation, because there is a contract between the two parties that *PhotoCentre* will want to meet, therefore having to 'pay' the Accounts payable in the future. The amount of the settlement can be measured with reliability because there will be invoices / a contract as evidence of how much money is outstanding.

2. Part A

- a. Karen will want to see the Income Statement to find out what the profit (or income/expenses) was for the period, to help her judge whether or not it is a good business to buy.
- b. i. Non-financial information because the information has nothing to do with money.
 - ii. This will give her an idea of the customer base that already buys from the business, and help her assess whether or not there is

room to expand or a sufficient number of customers to cover regular expenses.

Part B

- i. The roasting equipment should be recorded in New Zealand dollars, at a value of \$5 000.
 - ii. The roasting equipment will be reported in the Statement of Financial Position at the original acquisition cost to NZone Coffee Supplies, which is \$5 000.
- b. The \$6 000 for Accounts receivable after allowing for doubtful debts is relevant because it is the amount that provides the best predictive value of the amount of money that the business expects to receive from its debtors.
- c. The microwave can be written off as an expense (revenue expenditure) because the item itself (by its nature), and the amount of \$200 (by its size) are not significant enough to influence the decisions being made by the users, and therefore do not need to be disclosed separately / capitalised.
- d. i. Depreciation is the systematic allocation of the depreciable amount of the asset over its estimated useful life.
 - ii. The roasting equipment loses most of its 'future economic benefit' in the early years of its life, therefore it is most appropriate to depreciate it using the diminishing-value method, because this method depreciates assets most in their early years.

3. Part A

- a. Corporate Clothing prepares an Income Statement to measure the income, expenses and profit for the year. Due to the life of Corporate Clothing being broken into time periods of equal length, each year ending on 31 March, Caitlin and other users can use the Income Statement to make decisions. Since the Income Statement's information is for the year ended 31 March 2018, 2019, and 2020, Caitlin can compare the results. The qualitative characteristic of comparability ensures that statements are prepared in a consistent manner so that trend, similarities and differences can be established. As Corporate Clothing expanded in the recent year Caitlin can see that the decision to sell sports uniforms was successful because there was an increase in \$50 000 sales from 2019, and \$5 000 increase in profit. A non-financial reason for the increase in sales could be the large increase in advertising that was promoting the business in addition to the new uniforms and the increased customer base generated from the increased product range.
- b. The recent inventory purchase is reported in NZ\$ in accordance with the monetary measurement concept. The price of the inventory is converted from Indian rupees and reported as NZ\$12 000 in the records statements of *Corporate Clothing*. The inventory is reported in the Statement of Financial Position as at 31 March 2020 at \$18 100 in accordance with the accounting policy for inventory, because the revaluation of the obsolete inventory reduces the inventory on hand, being the lower of cost or market value. This will therefore increase the cost of goods sold in the Income Statement by \$3 000, thereby reducing the profit this year.

Part B

a. The shelving is a non-current asset for Corporate Clothing because the business will use the shelving beyond the current accounting period, and as the business will continue operating into the foreseeable future, this is the correct classification. It also meets capital expenditure by generating future economic benefit for more than the current accounting period. The shelving is an asset because it was purchased by Corporate Clothing in the past for \$18 000 and Corporate Clothing controls the shelving because only this business will benefit from the use of the shelves, which are locked inside its building. The shelving will be used to generate future economic benefit for Corporate Clothing by displaying clothes so that customers can see the uniforms easily, which increases sales and bank. It is

- probable that the shelves will generate this income because they are already being used to display clothes, and the cost of the shelving \$18 000 can be measured reliably because the historical cost of the shelves can be evidenced by the invoices provided when the shelving was purchased. The shelving is classified as a non-current asset because *Corporate Clothing* will continue to operate into the foreseeable future according to Going Concern.
- b. Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life; the shelving at \$18 000 will be depreciated at 8% every year. This straight-line method means the depreciation is the same amount every year, \$1 440. This method is the best method for shelving because the loss in future economic benefit from using the shelves is constant from year to year. The depreciation on the shelving is an expense for Corporate Clothing because it decreases the asset shelving (shop fittings) every year through increasing the accumulated depreciation every year by \$1 440. The shelving depreciation decreases the profit, which decreases the equity of Corporate Clothing this year. The depreciation is not a distribution to Caitlin the owner, and therefore is an expense for Corporate Clothing.

Part C

- a. The payment of the electricity is reported in two ways. According to the accounting entity concept, Caitlin must keep personal finances separate from those of the business. For this reason the \$120 for home electricity is reported in the Statement of Financial Position as drawings because this is a personal expense. The \$280 is reported as an expense in the Income Statement, thereby decreasing the profit for this year because it is an expense of Corporate Clothing.
- b. One possible consequence of having all credit sales pay by the 10th of each month and making all payments on the 20th is that Corporate Clothing might be missing out on discounts, especially as electricity has a discount if paid within 10 days, therefore Corporate Clothing might be paying more than it needs to. A second consequence could be that it is likely that some debtors will not pay by the 10th, especially if they have the 20th for their own payments, in the same way as Corporate Clothing. This might mean that Corporate Clothing does not have enough money to meet its own payments, and thereby misses out on discounts or is not allowed credit because of a poor payment history.
- c. The accrual basis concept states that transactions must be recognised when they occur, and reported in the financial statements of the period to which the transaction relates, regardless of whether or not cash has changed hands. The wages for the 11 days worked this year must be reported in this year's Income Statement because the workers did the work this period and the amount therefore belongs to this year. Corporate Clothing must increase the wages in the trial balance by \$1 650 to be reported in this year's Income Statement. In the Statement of Financial Position, the current liability 'accrued expenses' is created, totalling \$1 650, because the employees will be paid in the next financial year, specifically 20 April, therefore that is a current liability.

4. Part A

a. The Statement of Financial Position reports Eat Pasifika's assets, liabilities and equity at a point in time, in this case 31 March 2020. This is important to the bank manager, because the manager can see that the equity is greater than the debt and therefore this is encouraging for an increase in the loan. The manager can also see the security of \$1 240 000 in property, plant and equipment assets and the existing mortgage of \$600 000. The bank manager should give losefa the \$40 000 loan because the capital will still be greater than liabilities (\$646 500 compared with \$643 500) / the business is very successful because losefa has increased his capital by more than six times the original amount in 10 years.

(You could give a 'no' answer but would need evidence.)

- In addition to this financial information, the bank manager will also want to know the income and expenses from the past two years to establish the likelihood of covering the increase in the loan. One piece of non-financial information would be the expected customer base in Christchurch / competition in Christchurch to establish whether the loan can be serviced. It is important for the bank manager that the information is timely and up-to-date. The most recent Statement of Financial Position meets this requirement and therefore helps increase the accuracy of the manager's decision making.
- b. The loan is a liability for Eat Pasifika because it received the \$40 000 loan to expand. Eat Pasifika is presently obliged to repay the loan over the next five years as stated in the loan agreement. Eat Pasifika must sacrifice the asset bank in the future to meet the loan repayments as required. It is probable that the loan will be repaid, as Eat Pasifika will not want to pay default fees and will want to retain a good credit history; and the amount of \$40 000 is measured reliably as it is the amount stated on the loan agreement, and will be decreased as principal payments are made. Because it is clear that Eat Pasifika will continue to operate into the foreseeable future, the loan due in 5 years / 2025 is a non-current liability. In accordance with Historical Cost, the loan of \$40 000 is the original amount borrowed and does not include the interest owed.

Part R

- a. The shop signage is capital expenditure because it is a one-off type payment that will benefit *Eat Pasifika* beyond the current accounting period. That is why it is recorded as 'Fittings \$12 000' in the Statement of Financial Position. The monthly advertising is revenue expenditure because it is a regular payment of \$529 including GST (\$460 for the advertising) and it will benefit *Eat Pasifika* this year and be an expense in this year's Income Statement. Faithful representation requires information to be free from error, neutral and complete. By reporting the signage as fittings and the advertising as an expense, the asset and expenses will be complete and free from bias because the amounts are recorded on the suppliers' independent invoices. Materiality requires that information that will influence decisions be disclosed separately. The signage at \$12 000 is of significant value and therefore must be disclosed as an asset; writing it off as an expense would mislead users concerning the value of profit
- b. The accrual basis states that transactions must be recognised when they occur, and reported in the financial statements of the period to which the transaction relates, regardless of whether or not cash has changed hands. The advertising invoice will be reported in the Income Statement of Eat Pasifika by increasing the Advertising expense by \$460, which reduces this year's profit. Because the advertising has taken place this year it must be reported in this year's Income Statement, even though it has not yet been paid. In the Statement of Financial Position, the GST liability will decrease by \$69 and the current liability accounts payable \$529 will be created, because this account will be paid in the next financial year.

Part 0

a. Food sales are an income for Eat Pasifika because it increases the asset bank when customers eat in the restaurant and pay for their meals. The food sales increase profit, which increases equity for the year. The food sales are not a contribution by losefa the owner, but by customers eating in the restaurant. The food sales can be measured reliably, because there will be receipts as evidence of how much money was received from customers. It is more than probable that the food sales have been received because the receipts are proof, and food will continue to generate sales. The table breaking down the income for Eat Pasifika is a good example of understandability as it reports the two main incomes, food and bar sales, and states other income for three years. It is easy to understand and can be used to make decisions.

b. The concept of materiality states that information that will influence the decisions of users should be disclosed, and this depends on the size and the nature of the item. In this case, losefa deems 'food sales' and 'bar sales' as being important to disclose separately (e.g. in 2020, \$190 000 in food sales, and \$180 000 in bar sales). This helps him make decisions regarding the success of each section. For example, bar sales have increased more than food sales – in fact food sales decreased this year though total sales increased. If the information were not separate he would not know this. (Another decision example is possible.) The 'other income' can be lumped together because the nature of dividends and tips is not important and the amount of \$1 000 is small in relation to the total income of \$371 000 in 2020.

5. Part A

- a. Dave will report the business electricity as an expense of \$65 000 in the Income Statement in accordance with the definition of an expense. The cost of business electricity would have decreased *Toptronics*' assets when the electricity was paid for because the bank account would have decreased by \$65 000. The cost of business electricity decreased equity by decreasing profit for the year, and was not a distribution to Dave the owner. The cost of personal electricity cannot be a business expense as it was a payment for Dave's personal use, and must therefore be recorded in the Statement of Financial Position as drawings of \$3 000. This is in accordance with the Accounting Entity concept that states that the financial affairs of Dave the owner must be separate from those of the business *Toptronics*.
- b. The shop shelves are an asset for *Toptronics* because they were purchased by *Toptronics* in the past. *Toptronics* has present control over how the shop shelves are used by keeping them locked in its building and deciding how they are used; and the shop shelves will generate future economic benefit by attracting more customers into the shop by displaying the tablets and televisions so that customers can see them easily, which will increase sales and the bank account. The value of the shop shelves can be measured with reliability in the Statement of Financial Position because *Toptronics* will have an invoice to give evidence of the value. It is also probable that the shelves will generate income as there is more than a 50% likelihood that customers will buy the electronics displayed on the shelves. The shelves are a non-current asset as they will generate future economic benefit for *Toptronics* for more than the next financial year / there is no intention to sell them this year.

Part B

a. The Cash Flow Statement will show Toptronics' cash receipts (where receipts came from and their value) and cash payments (what money was spent on and how much was spent) for the year, and the resulting increase or decrease in cash for the year and the resulting bank balance.

Toptronics' decision to expand online was successful as there was an increase in cash receipts from sales, from \$650 000 to \$820 000 including \$120 000 from online sales. As a result, the cash payments to suppliers increased from \$400 000 to \$500 000 because Toptronics needed to buy more inventory (iPads™, televisions and so on) to sell to the increased customer base. Overall, the increase of receipts was \$70 000, largely as a result of the online sales which increased the closing bank balance. Having the online sales appears to have increased shop sales as well, as more people are aware of the Toptronics business.

The full success of the introduction of the online store would be more evident when looking at the full Cash Flow Statement because many cash expenses would have increased with the online store. *Toptronics* might have had to employ more staff to fill the orders, and also to set up and operate the online website. This resulting increase or decrease in cash for the year would give a true judgement on the

overall success of the online store – if the increase led to a greater value of receipts than the result for 2018 then the online store was definitely a cash success, but if there was a deficit then the increased costs outweighed the receipts and would not be a good thing for *Toptronics*.

b. The historical cost concept states that assets must be reported at their original acquisition cost. *Toptronics* is meeting this concept as the shares in *Telco Ltd* are reported at \$20 000 in the main body of the Statement of Financial Position.

The concept of relevance requires *Toptronics* to disclose information that will influence the users' decision and should help predict future events or confirm past ones. The current market value might influence the users because in this case the shares have increased in value by \$4 000. This current market value of \$24 000 is reported to the users in the notes to the financial statements, providing users of the information with a more relevant figure for decisions if *Toptronics* decided to sell the shares.

Both figures are verifiable as there would be a receipt for \$20 000, which was the price paid for the shares; and the \$24 000 is verifiable as it is an independent valuation of the shares' current value on the stock exchange and the value is published publicly.

Part C

- a. The going concern concept states that *Toptronics* will continue to operate into the foreseeable future, which means it currently has no intention to close. This is important for the employees as it indicates that there should be reasonable job security, especially when considering the increase in sales growth over the past three years. The growth in sales over the past three years indicates that the business is in a strong financial position with future sales expected to continue and therefore the management has no intention to close the business as there is no need to since the business is more profitable than in previous years.
- b. i. The purchase of the new delivery van is capital expenditure because it was a one-off type of purchase that created a new non-current asset when *Toptronics* purchased it, and the firm intends to use the vehicle to benefit the business for more than the current financial year. The sign writing is also capital expenditure as it is a one-off cost related to getting the van ready for use by *Toptronics*. The vehicle is reported as an asset of \$84 000 in the Statement of Financial Position, not an expense, therefore it is capital expenditure.
 - ii. The diesel spent to fuel the vehicle is a revenue expenditure as it is recurring in nature / daily expenditure – it is likely that Toptronics will have to spend approximately \$300 every month on diesel to operate the vehicle. This diesel will be reported in the Income Statement as an expense which decreases profit, as it affects only the current year.

Activity 5A: Journal entries (page 54)

1. a. Depreciation on equipment \$800 each year

31/3/20XX	Depreciation on equipment	800	
	Accumulated depreciation on equipment		800
	(Depreciation on equipment \$800 straight line)		

b. Wages owing on balance day \$900

31/3/20XX	Wages	900	
	Accrued expenses		900
	(Wages owing on balance day)		

c. Sales received in advance \$2900 excluding GST

31/3/2	0XX	Sales	2 900	
		Income in advance		2 900
		(Sales received in advance on balance day)		

d. Insurance paid in advance \$380 excluding GST

31/3/20XX	Prepayments	380	
	Insurance		380
	(Insurance paid in advance on balance day)		

e. Interest on term deposit owing \$240

31/3/20XX	Accrued income	240	
	Interest received		240
	(Interest on term deposit owing on balance day)		

Invoices issued for fees received before balance day total \$7 360 including GST

31/3/20XX	Accounts receivable	7 360	
	GST		960
	Fees received		6 400
	(Fees received owing on balance day)		

g. Invoice received for furniture purchased on credit \$2 760 including GST

31/3/20XX	Furniture	2 400	
	GST	360	
	Accounts payable		2 760
	(Furniture purchased on credit on balance day)		

h. Invoice received for electricity dated 29 March \$184 including GST

31/3/20XX	Electricity	160	
	GST	24	
	Accounts payable		184
	(Electricity invoice owing on balance day)		

2. a. 31/3/20XX Depreciation on furniture 1 008

Accumulated depreciation on furniture 1 008

Depreciation on furniture 8% p.a. straight line

b.	31/3/20XX	Prepayments	300	
		Rates		300
		Rates paid in advance \$300		

c.	31/3/20XX	Accrued income	240	
		Dividends		240
		Dividends owing \$240		

d.	31/3/20XX	Accounts receivable	9 200	
		GST		1 200
		Sales		8 000
		Invoices issued for sales before balance day total \$9 200 including GST		

			T	1	ı
		31/3/20XX	Cost of goods sold	3 000	
			Inventory		3 000
			Recording cost price \$3 000 inventory sold on credit.		
	e.	31/3/20XX	Interest on loan	750	
			Accrued expenses		750
			Interest on loan owing on balance day \$750		
	f.	31/3/20XX	Rent received	400	
			Income in advance	1	400
			Rent received in advance \$400	1	
	g.	31/3/20XX	Furniture	560	
	3.		GST	84	
			Accounts payable		644
			Invoice received for display table	+	
			purchased \$644 including GST		
	h.	31/3/20XX	Telephone	120	
			GST	18	
			Accounts payable		138
			Invoice received for telephone dated 26 March \$138 including GST		
	i.	31/3/20XX	Depreciation on delivery van	1 920	
			Accumulated depreciation on delivery van		1 920
			Depreciation on delivery van 12% p.a. straight line		
3.	a.	31/3/2022	Wages	290	
			Accrued expenses		290
	b.	31/3/2022	Prepayments	520	
			Advertising		520
	c.	31/3/2022	Depreciation on shop fittings	500	
	0.	0 110/2022	Accumulated depreciation on shop fittings	000	500
		24/2/2022		1,000	
	d.	31/3/2022	Sales Income in advance	1 900	1 900
			Income in advance		1 900
	e.	31/3/2022	Depreciation on buildings	6 300	
			Accumulated depreciation on buildings		6 300
	f.	31/3/2022	Electricity	240	
			GST	36	
			Accounts payable		276
	g.	31/3/2022	Interest on mortgage	1 700	
	-		Accrued expenses		1 700
	h.	31/3/2022	Accounts receivable	2 300	
			GST		300
			Sales		2 000
			I		

	31/3/2022	Cost of goods sold	720	
		Inventory		720
i.	31/3/2022	Accrued income	230	
		Interest received		230

Activity 5B: Preparing financial statements (page 62)

Leigh's L Income for the year en	ittle Gifts 40 Statement ded 31 Marc		
	\$	\$	\$
Revenue			
Sales			260 000
Less Sales returns			(3 000)
Net sales			257 000
Less Cost of goods sold			(135 000)
Gross profit			122 000
Add Other income			
Dividends			<u>420</u>
			122 420
Less Expenses			
Distribution costs			
Advertising	2 770		
Shop wages	56 600		
Depreciation on shop equipment	1 000		
Insurance (Inventory)	<u>560</u>	60 930	
Administrative expenses			
Accountancy fees	1 200		
Bad debts	200		
Doubtful debts	90		
General expenses	9 760		
Rates	1 500		
Depreciation on buildings	<u>4 000</u>	16 750	
Finance costs			
Interest on mortgage	8 800	<u>8 800</u>	
Total expenses			(86 480)
Profit for the year			\$35 940

Leigh's Little Gifts 4U Statement of Financial Position as at 31 March 2024			
	\$	\$	\$
Current assets			
Accounts receivable (Note 1)		4 260	
Bank		3 600	
Inventory		39 700	
Prepayments		230	
Accrued income		300	48 09
Non-current assets			
Investments (Note 2)			
Shares in Telestar Ltd		10 000	
Property, plant and equipment (Note 3)			
Total carrying amount		201 550	211 55
Total assets			259 64
Less Liabilities			
Current liabilities			
Accounts payable	2 584		
GST	3 476		
Accrued expenses	4 600	10 660	
Non-current liabilities (Note 4)			
Mortgage		120 000	
Total liabilities			(130 6
Net assets			\$128 9
Equity			
Opening capital			96 54
Plus Profit for the year			35 94
Less Drawings			(3 50
Closing capital			\$128 9

Notes to the Statement of Financial Position

1. Accounts receivable

Accounts receivable	4 500
Less Allowance for doubtful debts	240
	\$4 260

2. Investments

Investments comprise shares in *Telestar Ltd*. The current fair value of the shares is \$11 200, which is their market value on balance date.

4. Loan / Mortgage

The mortgage has an interest rate of 8% and a maturity date of 31 March 2030.

2. a. General journal entries

31/3/2022 Prepayments 45	
Shop rent	450

31/3/2022	Interest on loan	200	
	Accrued expenses		200
31/3/2022	Advertising	320	
	GST	48	
	Accounts payable		368
	Г	1	
31/3/2022	Depreciation on vehicles	3 200	
	Accumulated depreciation on vehicles		3 200
		_	
31/3/2022	Depreciation on shop fittings	1 400	
	Accumulated depreciation on shop fittings		1 400
31/3/2022	Prepayments	70	
	Telephone		70

Steven's Stereos and Extras Income Statement for the year ended 31 March 2022				
	\$	\$	\$	
Revenue				
Sales			465 00	
Less Sales returns			(1 00	
Net Sales			464 00	
			/	
Less Cost of goods sold			(225 00	
Gross profit			239 00	
Add Other income				
Discount received			34	
			239 34	
Less Expenses				
Distribution costs				
Advertising	4 820			
Shop rent	23 550			
Stereo assistant wages	28 000			
Depreciation on shop fittings	1 400			
Depreciation on vehicle	3 200	60 970		
Administrative expenses				
Telephone	1 130			
Bad debts	540			
Doubtful debts	90			
Electricity	1 600			
Stationery	700			
Insurance	<u>560</u>	4 620		
Finance costs				
Interest on loan	4 800	<u>4 800</u>		
Tatal ayraanaa			(70.00	
Total expenses Profit for the year			(70 39 \$168 9	

Depreciation is calculated on the following property plant and equipment assets as follows:

- · Vehicles 20% p.a., straight-line method.
- Shop fittings 5% p.a., straight-line method.

4. Loan / Mortgage

c.

The mortgage has an interest rate of 12% and a maturity date of 31 October 2025.

Steven's Stereos and Extras Statement of Financial Position as at 31 March 2022				
	\$	\$	\$	
Current assets				
Accounts receivable (Note 1)		3 640		
GST		1 348		
Inventory		178 200		
Prepayments		<u>520</u>	183 708	
Non-current assets				
Property, plant and equipment (Note 2)				
Total carrying amount		35 950		
Intangible assets				
Goodwill		<u>3 000</u>	<u>38 950</u>	
			222 / 52	
Total assets			222 658	
Less Liabilities			1	
Current Liabilities			1	
Accounts payable	2 768		1	
Bank	4 500		1	
Accrued expenses	200	7 468		
Non-current liabilities (Note 3)				
Loan		40 000		
Total liabilities			(47.440)	
Total liabilities			(47 468) \$175 190	
Net assets			\$175 19U	
Equity				
Opening capital			36 240	
Plus Profit for the year			168 950	
Less Drawings			(30 000)	
Closing capital			\$175 190	

Notes to the Statement of Financial Position

1. Accounts receivable

Accounts receivable	3 800
Less Allowance for doubtful debts	(160)
	3 640

2. Property, plant and equipment

	Vehicles	Shop fittings	Total
	\$	\$	\$
For year ended 31 March 2022			
Opening carrying amount	13 700	26 850	40 550
Plus Additions	0	0	0
Less Disposals	0	0	0
Less Depreciation	(3 200)	(1 400)	(4 600)
Closing carrying amount	\$10 500	\$25 450	\$35 950
As at 31 March 2022			
Cost	16 000	28 000	44 000
Accumulated depreciation	(5 500)	(2 550)	(8 050)
Carrying amount	\$10 500	\$25 450	\$35 950

Activity 6A: Depreciation (page 68)

1.	Method	Working	Depreciation \$	Working	Accumulated depreciation \$
	a.	(16 000 <u>-2 000</u>) × 20%	2 800	2 300 + 2 800	5 100
	b.	(16 000 – 2 300) × 20%	2 740	2 300 + 2 740	5 040
	c.	$\frac{(16\ 000-2\ 000)}{80\ 000}\times 20\ 000$	3 500	2 300 + 3 500	5 800

2.	Method	Working	Depreciation \$	Working	Accumulated depreciation \$
	a.	(24 000 – 4 000) × 8%	1 600	6 000 + 1 600	7 600
	b.	(24 000 – 6 000) × 12%	2 160	6 000 + 2 160	8 160
	c.	$\frac{(24\ 000-4\ 000)}{20\ 000}\times 1\ 600$	1 600	6 000 + 1 600	7 600

Activity 6B: Bad and doubtful debts (page 70)

1. a. Bad debts = \$600

200 + 400 excluding GST.

b. Allowance for doubtful debts = \$257 (5 600 – 460) \times 5% = 257 Doubtful debts = \$107

\$257 – 150.

c. Note 1: Accounts receivable

Accounts receivable	5 140
Less Allowance for doubtful debts	(257)
	4 883

2. a. Bad debts = \$160

\$184 excluding GST.

b. Allowance for doubtful debts = $$180 (7380 - 184) \times 2.5\% = 180 Doubtful debts = \$50

180 - 130 = \$50

c. Note 1: Accounts receivable

Accounts receivable	7 200
Less Allowance for doubtful debts	(180)
	7 020

3. a. Bad debts = \$120

\$80 + \$40 excluding GST.

b. Allowance for doubtful debts = \$25 (1 296 – 46) \times 2% = \$25Doubtful debts = -\$75

(\$25 - 100) = -\$75

c. Note 1. Accounts receivable

Accounts receivable	1 250
Less Allowance for doubtful debts	(25)
	1 225

Activity 6C: Inventory revaluation (page 72)

1.	Date	Particulars	Dr	Cr
	31/3/24	Cost of goods sold	1 800	
		Inventory		1 800

2. a. \$9 100

b.	Date	Particulars	Dr	Cr
	31/3/24	Cost of goods sold	4 300	
		Inventory		4 300

Activity 6D: Putting it all together (page 73)

Income	a's Plumbin Statement October 20)		
	\$	\$	\$
Revenue			
Fees received			236 540
Add Other income			
Dividends received			<u>360</u>
			236 900
Less Expenses			
Plumbing expenses			
Advertising	3 600		
Plumbing wages	32 500		
Depreciation on plumbing equipment	1 400		
Cell phone expenses*	1 120		
Supplies used	75 000		
Vehicle expenses	15 740		
Depreciation on vehicles	<u>9 160</u>	138 520	
Administrative expenses			
Electricity	900		
Bad debts	476		
Doubtful debts	61		
Stationery	680		
Insurance	560		
Office rent	24 000	26 677	
Finance costs			
Interest on loan	2 200	2 200	
Total avnances			(147.207\
Total expenses			(167 397)
Profit for the year			\$69 503

Pollyanna's Plumbing Statement of Financial Position as at 31 October 20XX				
	\$	\$	\$	
Current assets				
Accounts receivable (Note 1)		5 860		
Bank		1 890		
Supplies on hand		23 000		
Prepayments		80		
Accrued income		<u>120</u>	30 950	
Non-current assets				
Investments (Note 2)				
Shares in XYZ Ltd		8 000		
Property, plant and equipment (Note 3)				
Total carrying amount		48 040		
Intangible assets				
Goodwill		10 000	66 040	
Total assets			96 990	
Less Liabilities				
Current liabilities				
Accounts payable		3 876		
GST		1 971		
Accrued expenses		200		
Loan (Note 4)		22 000		
Total liabilities			(28 047	
Net assets			\$68 943	
Equity				
Opening capital			21 440	
Plus Profit for the year			69 503	
Less Drawings			(22 000	
Closing capital			\$68 943	

d. Notes to the Statement of Financial Position

1. Accounts receivable

Accounts receivable	6 041
Less Allowance for doubtful debts	(181)
	\$5 860

2. Investments

Investments consist of shares in XYZ Ltd. The current fair value of the shares is \$9 600, which is their market value on balance date, 31 October 20XX.

^{*}Note: Cell phone expenses could be regarded as an administrative expense.

3. Property, plant and equipment

	Vehicles	Plumbing equipment	Total
	\$	\$	\$
For year ended 31 October 20XX			
Opening carrying amount	45 800	12 800	58 600
Plus Additions	0	0	0
Less Disposals	0	0	0
Less Depreciation	(9 160)	(1 400)	(10 560)
Closing carrying amount	\$36 640	\$11 400	\$48 040
As at 31 October 20XX			
Cost	56 000	14 000	70 000
Accumulated depreciation	(19 360)	(2 600)	(21 960)
Carrying amount	\$36 640	\$11 400	\$48 040

Depreciation is calculated on the following property, plant and equipment assets as follows:

- Vehicles 20% p.a., diminishing-value method.
- Plumbing equipment 10% p.a., straight-line method.

4. Loan / Mortgage

The mortgage has an interest rate of 10% and a maturity date of 31 July 2027.

c. Additional information (8)

31/3/20XX	Bad debts	160	
	GST	24	
	Accounts receivable		184

Additional information (9)

	31/3/20XX	Doubtful debts	61	
ſ		Allowance for doubtful debts		61

Income Statem for the year en			
Revenue			
Sales			89 08
Less Sales returns			(3 00
Net sales			86 08
Less Cost of goods sold			(23 60
Gross profit			62 48
Other income			
Rent received			19 40
Less expenses			81 88
Distribution costs			
Advertising	4 500		
Wages	36 800		
Depreciation on shop	6 000		
Depreciation on shop fittings	2 220	49 520	
Administration expenses			
Bad debts	170		
General expenses	16 282		
Insurance	3 500		
Power and lighting	4 080		
Rates	2 600		
Stationery	2 760		
Telephone	2 030		
Doubtful debts	<u>12</u>	31 434	
Finance costs			
Interest on mortgage	<u>6 120</u>	<u>6 120</u>	
Total expenses			<u>87 0</u> 7
Loss for the year			(5 19

Statement of Financial Position for <i>Lucy's Looks</i> as at 31 March 20XX				
Current assets				
Bank		7 305		
Accounts receivable (1)		2 058		
Inventory		13 700		
Prepayments		50	23 113	
Non-current assets				
Intangibles				
Goodwill		8 700		
Property, plant and equipment (2)		109 780		
			118 480	
Total assets			141 593	
Current liabilities				
Accounts payable	4 576			
Accrued expenses	1 220			
Income in advance	1 050			
GST	2 731	9 577		
Non-current liabilities				
Mortgage		68 000		
Total liabilities			(775 77)	
			\$ 64 016	
EQUITY				
Capital			105 410	
Loss for the year			(5 194)	
Drawings			(36 200)	
Closing capital			\$ 64 016	

Notes to the Statement of Financial Position

1. Accounts receivable

Accounts receivable	2 100	
Less allowance for doubtful debts	(42)	2 058

2. Property, plant and equipment

	Shop	Shop fittings	Total
	\$	\$	\$
For the year ended 31 March 20XX			
Opening carrying amount	95 800	22 200	118 000
Depreciation expense	(6 000)	(2 220)	8 220
Closing carrying amount	89 800	19 980	109 780
As at 31 March 20XX			
Historical cost	120 000	26 400	146 400
Accumulated depreciation	(30 200)	(6 420)	(36 620)
Closing carrying amount	89 800	19 980	109 780

Depreciation in charged on the following assets at the following rates:

- Shop at 5% p.a. straight-line method
- Shop fittings 10% p.a. diminishing-value method

3. Mortgage

The mortgage is secured over the shop and has a maturity date of August 2038. It has an interest rate of 9% per year.

Activity 7A: Balance-date adjustment journals (page 78)

1. a.	Date	Particulars	Dr	Cr
	31/3/20XX	Wages	600	
		Accrued expenses		600

b.	Date	Particulars	Dr	Cr
	31/3/ 20XX	Prepayments	230	
		Advertising		230

c.	Date	Particulars	Dr	Cr
	31/3/ 20XX	General expenses	160	
		GST	24	
		Accounts payable		184

d.	Date	Particulars	Dr	Cr
	31/3/20XX	Depreciation on buildings	4 500	
		Accumulated depreciation on buildings		4 500

e.	Date	Particulars	Dr	Cr
	31/3/20XX	Depreciation on shop fittings	3 800	
		Accumulated depreciation on shop fittings		3 800

f.	Date	Particulars	Dr	Cr
	31/3/20XX	Accrued income	300	
		Dividends		300

g.	Date	Particulars	Dr	Cr
	31/3/20XX	Interest on mortgage	4 000	
		Accrued expenses		4 000

h.	Date	Particulars	Dr	Cr
	31/3/20XX	Cost of goods sold	5 000	
		Inventory		5 000

i.	Date	Particulars	Dr	Cr
	31/3/20XX	Bad debts	400	
		GST	60	
		Accounts receivable		460

j.	Date	Particulars	Dr	Cr
	31/3/20XX	Doubtful debts	20	
		Allowance for doubtful debts		20

ζ.	Date	Particulars	Dr	Cr
	31/3/20XX	Accounts receivable	2 300	
		GST		300
		Fees received		2 000

2. a.	Date	Particulars	Dr	Cr
	31/3/20XX	Prepayments	80	
		Telephone		80

b.	Date	Particulars	Dr	Cr
	31/3/20XX	Interest on loan	800	
		Accrued expenses		800

C.	Date	Particulars	Dr	Cr
	31/3/20XX	Advertising	320	
		GST	48	
		Accounts payable		368

d.	Date	Particulars	Dr	Cr
	31/3/20XX	Depreciation on vehicles	6 000	
		Accumulated depreciation on vehicles		6 000

e.	Date	Particulars	Dr	Cr
	31/3/20XX	Depreciation on shop fittings	1 345	
		Accumulated depreciation on shop fittings		1 345

f.	Date	Particulars	Dr	Cr
	31/3/20XX	Sales	540	
		Income in advance		540

g.	Date	Particulars	Dr	Cr
	31/3/20XX	Bad debts	160	
		GST	24	
		Accounts receivable		184

h.	Date	Particulars	Dr	Cr
	31/3/20XX	Allowance for doubtful debts	130	
		Doubtful debts (recovered)		130

i.	Date	Particulars	Dr	Cr
	31/3/20XX	Cost of goods sold	3 600	
		Inventory		3 600

Activity 7B: Closing entries (page 81)

1. b.	Date	Particulars	Dr	Cr
	31/10/2022	Income summary	3 600	
		Advertising		3 600
		(Closing advertising on balance day)		

c.	Date	Particulars	Dr	Cr
	31/10/2022	Dividends received	360	
		Income summary		360
		(Closing dividends received on balance day)		

d.	Date	Particulars	Dr	Cr
	31/10/2022	Income summary	920	
		Stationery		920
		(Closing stationery on balance		
		day)		

e.	Date	Particulars	Dr	Cr
	31/10/2022	Income summary	1 400	
		Depreciation on office equipment		1 400
		(Closing depreciation on office equipment on balance day)		

f.	Date	Particulars	Dr	Cr
	31/10/2022	Fees received	236 000	
		Income summary		236 000
		(Closing fees received on balance day)		

g.	Date	Particulars	Dr	Cr
	31/10/2022	Income summary	1 120	
		Telephone expense		1 120
		(Closing telephone expense on balance day)		

h.	Date	Particulars	Dr	Cr
	31/10/2022	Income summary	36 500	
		Capital		36 500
		(Closing profit for the year on balance day)		

Date	Particulars	Dr	Cr
31/10/2022	Capital	22 000	
	Drawings		22 000
	(Closing drawings on balance day)		

Businesses still control the assets and are obliged to repay their liabilities at the start of the next financial year, therefore these accounts are not closed back to zero.

Activity 7C: Ledger accounts (page 86)

1. Interest on loan

Date	Particulars	Dr	Cr	Bal
31/10/2022	Balance			2 000 dr
	Accrued expenses	200		2 200 dr
	Income summary		2 200	0

Accrued expense

Date	Particulars	Dr	Cr	Bal
31/10/2022	Interest on loan		200	200 cr

Telephone expense

Date	Particulars	Dr	Cr	Bal
31/10/2022	Balance			1 200 dr
	Prepayment		80	1 120 dr
	Income summary		1 120	0

Prepayments

Date	Particulars	Dr	Cr	Bal
31/10/2022	Telephone	80		80 dr

Depreciation on furniture

Date	Particulars	Dr	Cr	Bal
31/10/2022	Accumulated depreciation on furniture	5 580		5 580 dr
	Income summary		5 580	0

Bad debts

Date	Particulars	Dr	Cr	Bal
31/10/2022	Balance			320 dr
	Accounts receivable	160		480 dr
	Income summary		480	0

Allowance for doubtful debts

Date	Particulars	Dr	Cr	Bal
31/10/2022	Balance			120.00 cr
	Doubtful debts		42.60	162.60 cr

Drawings

Date	Particulars	Dr	Cr	B al
31/10/2022	Balance			22 000 dr
	Capital		22 000	0

Capital

Date	Particulars	Dr	Cr	Bal
31/10/2022	Balance			21 560 cr
	Income summary		36 500	58 060 cr
	Drawings	22 000		36 060 cr

2. a. Additional information (1)

Date	Particulars	Dr	Cr
31/10/20XX	Prepayments	80	
	Cellphone expense		80

Additional information (2)

Date	Particulars	Dr	Cr
31/10/20XX	Interest on loan	640	
	Accrued expenses		640

Additional information (5)

Date	Particulars	Dr	Cr
31/10/20XX	Vehicle expenses	240	
	GST	36	
	Accounts payable		276

Additional information (7)

Date	Particulars	Dr	Cr
31/10/20XX	Bad debts	160	
	GST	24	
	Accounts receivable		184

Additional information (8)

Date	Particulars	Dr	Cr
31/10/20XX	Allowance for doubtful debts	155	
	Doubtful debts (recovered)		155

b. i.	Date	Particulars	Dr	Cr
	31/10/2XX	Fees received	258 000	
		Income summary		258 000

ii.	Date	Particulars	Dr	Cr
	31/10/2XX	Income summary	24 000	
		Office rent		24 000

iii.	Date	Particulars	Dr	Cr
	31/10/2XX	Income summary	2 640	
		Interest on loan		2 640

iv.	Date	Particulars	Dr	Cr
	31/10/2XX	Income summary	1 120	
		Cellphone expense		1 120

V.	Date	Particulars	Dr	Cr
	31/10/2XX	Income summary	11 160	
		Depreciation on vehicles		11 160

vi.	Date	Particulars	Dr	Cr
	31/10/2XX	Capital	42 000	
		Drawings		42 000

c. Dividends received

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Balance			240 cr
	Accrued income		120	360 cr
	Income summary	360		0

Accrued income

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Dividends received	120		120 dr

Bad debts

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Balance			320 dr
	Accounts receivable	160		480 dr
	Income summary		480	0

Accounts receivable

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Balance			5 684 dr
	Bad debts and GST		184	5 500 dr

Prepayments

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Cellphone expense	80		80 dr

Accumulated depreciation on vehicles

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Balance			10 200 cr
	Depreciation on vehicles		11 160	21 360 cr

Advertising

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Balance			3 600 dr
	Income summary		3 600	0

Allowance for doubtful debts

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Balance			320 cr
	Doubtful debts	155		165 cr

Drawings

Date	Particulars	Dr	Cr	Bal
31/10/20XX	Balance			42 000 dr
	Capital		42 000	0

Date	Particulars	Dr	Cr
31/3/XX	Dry-cleaning wages	560	
	Accrued expenses		560

Date	Particulars	Dr	Cr
31/3/XX	Prepayments	2 000	
	Shop rent		2 000

Date	Particulars	Dr	Cr
31/3/XX	Accrued income	135	
	Dividend received		135

Date	Particulars	Dr	Cr
31/3/XX	Interest on loan	3 100	
	Accrued expenses		3 100

Date	Particulars	Dr	Cr
31/3/XX	Bad debts	160	
	GST	24	
	Accounts receivable		184

Date	Particulars	Dr	Cr
31/3/XX	Doubtful debts	20	
	Allowance for doubtful debts		20

Date	Particulars	Dr	Cr
31/3/XX	Electricity	120	
	GST	18	
	Accounts payable		138

Date	Particulars	Dr	Cr
31/3/XX	Depreciation on vehicles	3 250	
	Accumulated depreciation on vehicles		3 250

Date	Particulars	Dr	Cr
31/3/XX	Depreciation on dry-cleaning equipment	7 920	
	Accumulated depreciation on dry-cleaning equipment		7 920

b.	Date	Particulars	Dr	Cr
	31/3/XX	Income summary	3 200	
		Taxation advice expense		3 200

Date	Particulars	Dr	Cr
31/3/XX	Fees received	196 400	
	Income summary		196 400

Date	Particulars	Dr	Cr
31/3/XX	Dividends received	375	
	Income summary		375

Date	Particulars	Dr	Cr
31/3/XX	Capital	22 000	
	Drawings		22 000

Date	Particulars	Dr	Cr
31/3/XX	Income summary	1 829	
	Capital		1 829

Date	Particulars	Dr	Cr
31/3/XX	Income summary	20	
	Doubtful debts		20

Date	Particulars	Dr	Cr
31/3/XX	Income summary	43 060	
	Dry-cleaning wages		43 060

d.

Dry-cleaning by David Income Statement for the year ended 31 March 20XX				
Revenue	\$	\$	\$	
Fees received			196 40	
Add Other income				
Dividend received			37	
Less Expenses			196 77	
Dry-cleaning expenses				
Advertising	8 600			
Dry-cleaning wages	43 060			
Depreciation on dry-cleaning equipment	7 920			
Supplies used	75 000			
Insurance – dry-cleaning	448			
Shop rent	26 000			
Vehicle expenses	15 000			
Depreciation on vehicles	3 250	179 278		
Administrative expenses				
Taxation advice expense	3 200			
Electricity	4 010			
Insurance (general)	112			
Telephone and internet	1 886			
Stationery	680			
Bad debts	160			
Doubtful debts	20	10 068		
Financial costs				
Interest on loan	<u>5 600</u>	<u>5 600</u>		
Total expenses			(194 94	
Profit for the year			\$1 82	

Dry-cleaning by David Statement of Financial Position as at 31 March 20XX				
	\$	\$	\$	
Current assets				
Accounts receivable (Note 1)		5 390		
GST		6 242		
Accrued income		135		
Supplies on hand		23 120		
Prepayments		2 000	36 887	
Non-current assets				
Investments (Note 2)				
Shares in MNOP Ltd		8 000		
Property, plant and equipment (Note 3)				
Total carrying amount		55 430		
Intangible assets				
Goodwill		10 000	73 430	
Total assets			110 317	
Less Liabilities				
Current liabilities				
Accounts payable	5 818			
Bank	1 950			
Accrued expenses	<u>3 660</u>	11 428		
Non-current liabilities				
Loan		<u>56 000</u>		
Total liabilities			(67 428)	
Net assets			\$42 889	
Equity				
Opening capital			63 060	
Plus Profit for the year			1 829	
Less Drawings			(22 000)	
Closing capital			<u>\$42 889</u>	

Notes to the Statement of Financial Position

1. Accounts receivable

Accounts receivable	5 500
Less Allowance for doubtful debts	(110)
	5 390

2. Investments

Investments comprise shares in MNOP Ltd. The current fair value of the shares is \$9 200, which is current market value on balance date.

3. Property, plant and equipment

	Vehicles	Dry-cleaning equipment	Total
	\$	\$	\$
For year ended 31 October 20XX			
Opening carrying amount	13 800	52 800	66 600
Plus Additions	0	0	0
Less Disposals	0	0	0
Less Depreciation	(3 250)	(7 920)	(11 170)
Closing carrying amount	10 550	44 880	55 430
As at 31 October 20XX			
Cost	24 000	54 000	78 000
Accumulated depreciation	(13 450)	(9 120)	(22 570)
Carrying amount	10 550	44 880	55 430

Depreciation is calculated on the following property plant and equipment assets as follows:

- Vehicles: 50c per km using the units-of-use method.
- Dry-cleaning equipment: 15% p.a. using the diminishingvalue method.

4. Loan / Mortgage

The loan has an interest rate of 10% and a maturity date of 31 October 2035.

e. Fees received

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			196 400 cr
	Income summary	196 400		0

Dry-cleaning wages

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			42 500 dr
	Accrued expenses	560		43 060 dr
	Income summary		43 060	0

Accrued income

Date	Particulars	Dr	Cr	Bal
31/3/XX	Dividend received	135		135 dr

Shop rent

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			28 000 dr
	Prepayments		2 000	26 000 dr
	Income summary		26 000	0

Prepayments

Date	Particulars	Dr	Cr	Bal
31/3/XX	Shop rent	2 000		2 000 dr

Bad debts

Date	Particulars	Dr	Cr	Bal
31/3/XX	Accounts receivable	160		160 dr
	Income summary		160	0

Drawings

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			22 000 dr
	Capital		22 000	0

Activity 8: Property, plant and equipment note to the Statement of Financial Position (page 95)

1. Property, plant and equipment

	Land and buildings	Delivery vehicle	Fixtures and fittings	Total
	\$	\$	\$	\$
For year ended 31 March 2022				
Opening carrying amount	264 000	15 800	10 900	290 700
Plus Additions	0	16 000	0	16 000
Less Disposals	0	0	(800)	(800)
Less Depreciation	(9 600)	(9 000)	(1 010)	(19 610)
Closing carrying amount	254 400	22 800	9 090	286 290
As at 31 March 2022				
Cost	320 000	64 000	18 000	402 000
Accumulated depreciation	(65 600)	(41 200)	(8 910)	(115 710)
Carrying amount	254 400	22 800	9 090	286 290

- Land and buildings: 3% p.a., straight-line method.
- Delivery van: 45 cents per kilometre using units-of-use method.
- Fixtures and fittings: 10% p.a., diminishing-value method.

2. Property, plant and equipment

	Buildings	Vehicle	Furniture and fittings	Land	Total
	\$	\$	\$	\$	\$
For year ended 31 December 20XX					
Opening carrying amount	71 200	19 200	6 100	65 000	161 500
Plus Additions	20 000	0	0	0	20 000
Less Disposals	0	0	(500)	0	(500)
Less Depreciation	(4 800)	(2 880)	(700)	0	(8 380)
Closing carrying amount	86 400	16 320	4 900	65 000	172 620
As at 31 December 20XX					
Cost	120 000	32 000	9 000	65 000	226 000
Less Accumulated depreciation	(33 600)	(15 680)	(4 100)	0	(53 380)
Carrying amount	86 400	16 320	4 900	65 000	172 620

- Buildings: 4% p.a., straight-line method.
- · Vehicle: 15% p.a., diminishing-value method.
- Furniture and fittings: straight-line method, at \$700 p.a.

3. Property, plant and equipment

	Computer	Machinery	Shop furniture	Total
	\$	\$	\$	\$
For year ended 31 March 20XX				
Opening carrying amount	0	13 000	15 000	28 000
Plus Additions	8 000	17 500	0	25 500
Less Disposals	0	(2 000)	0	(2 000)
Less Depreciation	(2 000)	(4400)	(1 500)	(7 900)
Closing carrying amount	6 000	24 100	13 500	43 600
As at 31 March 20XX				
Cost	8 000	45 000	18 000	71 000
Less Accumulated depreciation	(2 000)	(20 900)	(4 500)	(27 400)
Carrying amount	6 000	24 100	13 500	43 600

- · Shop furniture: 10% p.a., diminishing-value method.
- · Computer: 25% p.a., straight-line method.
- Machinery: 40 cents per hour using the units-of-use method.

4. Property, plant and equipment

	Furniture	Delivery vehicle	Office equipment	Total
	\$	\$	\$	\$
For year ended 31 March 2023				
Opening carrying amount	10 870	6 000	8 400	25 270
Plus Additions	630	0	4 000	4 630
Less Disposals	0	0	(1 200)	(1 200)
Less Depreciation	(575)	(4 500)	(1 440)	(6 515)
Closing carrying amount	10 925	1 500	9 760	22 185
As at 31 March 2023				
Cost	18 000	9 000	12 000	39 000
Less Accumulated depreciation	(7 075)	(7 500)	(2 240)	(16 815)
Carrying amount	10 925	1 500	9 760	22 185

- Delivery vehicle: 50 cents per kilometre using the units-of-use method.
- · Depreciation on office equipment: 12% p.a., straight-line method.
- · Shop furniture: 5% p.a., diminishing-value method.

5. Sportszone – Property, plant and equipment note

	Office equipment	Shop equipment	Total
	\$	\$	\$
For year ended 31 March 2020			
Opening carrying amount	40 000	44 500	84 500
Additions	0	4 500	4 500
Disposals	0	(4 000)	(4 000)
Depreciation	(10 000)	(2 000)	(12 000)
Closing carrying amount	30 000	43 000	73 000
As at 31 March 2020			
Cost	60 000	55 000	115 000
Accumulated depreciation	(30 000)	(12 000)	(42 000)
Closing carrying amount	30 000	43 000	73 000

Depreciation is calculated on the following property, plant and equipment assets at the following rates:

- Depreciation on shop equipment, \$2 000 p.a.
- Depreciation on office equipment is straight-line based on a residual value of \$10 000.
- 6. Casey's Catering Property, plant and equipment note

	Kitchen equipment	Vehicles	Total
	\$	\$	\$
For year ended 31 March 2020			
Opening carrying amount	27 000	80 000	107 000
Additions	12 000	44 000	56 000
Disposals	0	(5 000)	(5 000)
Depreciation	(5 850)	(9 360)	(15 210)
Closing carrying amount	33 150	109 640	142 790
As at 31 March 2020			
Cost	57 000	133 000	190 000
Accumulated depreciation	(23 850)	(23 360)	47 210
Closing carrying amount	33 150	109 640	142 790

Depreciation is calculated on the following property, plant and equipment assets at the following rates:

- Depreciation on vehicles is 52 cents per kilometre per annum using units-of-use method.
- Depreciation on kitchen equipment 15% diminishing-value method on closing historical cost balance.

Activity 9A: Calculating cash received from Accounts receivable and cash paid to Accounts payable (page 102)

- 1. a. \$230 950 6 900 + 235 000 4 500 800 250 5 400 = 230 950 b. \$63 310 2 300 + 65 000 - 1 200 - 240 - 110 + 360 - 2 800 =
- 2. a. \$26 420 1 300 + 28 000 1 600 180 1 100 = 26 420

63 310

b. \$159 270 4 600 + 165 000 - 5 300 - 480 + 450 - 5 000 = 159 270

3. a. Accounts receivable \$183 040 2 600 + 186 000 - 2 100 - 400 - 160 - 2 900 = 183 040

Accounts payable 111 250 1850 + 115000 - 3300 - 350 + 250 - 2200 = 111250

b. Accounts receivable \$24 140 5 550 + 24 000 - 40 - 110 - 5 260 = 24 140

Accounts payable \$18 150 3 880 + 18 000 - 400 - 380 - 2 950 = 18 150

Activity 9B: Preparing the Cash Flow Statement (page 104)

Workings:

Jenny's Junk U Want Cash Flow Statement for the year ended 30 June 2022					
Receipts					
Cash sales	65 000				
Accounts receivable	2 500				
Dividends	<u>120</u>				
Total receipts		67 620			
Payments					
Cash purchases	37 350				
Accounts payable	790				
Van deposit	4 000				
Wages	12 000				
Drawings	8 000				
General expenses	30 000				
Interest on loan	500				
Shares in Telestar Ltd	8 000				
Loan	<u>5 000</u>				
Total payments		(105 640)			
Net decrease in cash		(38 020)			
Opening bank balance		46 000			
Closing bank balance		\$7 980			

2. Workings:

Accounts receivable \$7 570 500 + 8000 - 180 - 750 = 7570Accounts payable \$12 200 1200 + 12000 - 1000 = 12200

Tim's Toy Barn Cash Flow Statement for the month ended 30 September 2018					
Receipts					
Cash sales	36 000				
Accounts receivable	7 570				
Capital	10 000				
Dividends	<u>360</u>				
		53 930			
Payments					
Accounts payable	12 200				
Wages	2 000				
Drawings	580				
Electricity	150				
Computer instalment	1 250				
Cash purchases	5 600				
Telephone	100				
Insurance	65				
Mortgage	<u>1 200</u>				
		(23 145)			
Net increase in cash		30 785			
Opening bank balance		2 300			
Closing bank balance		\$33 085			

Workings:

Spering bank balance \$30 000 overdrait 5 300 - 42 300 = -30				
Dylan's Dentist Cash Flow Statement for the year ended 31 March 2018				
Receipts				
Loan	6000			
Interest received	300			
(Cash) fees received	220 000			
Accounts receivable	<u>67 620</u>	293 920		
Payments				
Shares in Colgleans Ltd	6 000			
Drawings	2 500			
Wages	80 000			
Advertising	4 500			
Insurance	890			
Electricity	2 800			
General expenses	60 000			
Drill purchase	35 000			
Bank fees	120			
Rent	15 000			
Accounts payable	44 750			
		(251 560)		
Net increase in cash		42 360		
Opening bank balance		(38 860) OD		
Closing bank balance		\$3 500		

Activity 10A: Reinforcement (page 108)

1. a.	Date	Particulars	Dr	Cr
	31/3/23	Shop wages	960	
		Accrued expenses		960

Date	Particulars	Dr	Cr
31/3/23	Prepayments	250	
	Rates		250

Date	Particulars	Dr	Cr
31/3/23	Advertising	240	
	GST	36	
	Accounts payable		276

Date	Particulars	Dr	Cr
31/3/23	Bad debts	320	
	GST	48	
	Accounts receivable		368

Date	Particulars	Dr	Cr
31/3/23	Doubtful debts	40	
	Allowance for doubtful debts		40

Date	Particulars	Dr	Cr
31/3/23	Depreciation on buildings	6 500	
	Accumulated depreciation on buildings		6 500

Date	Particulars	Dr	Cr
31/3/23	Depreciation on shop equipment	860	
	Accumulated depreciation on shop equipment		860

Date	Particulars	Dr	Cr
31/3/23	Accrued income	90	
	Dividends		90

Date	Particulars	Dr	Cr
31/3/23	Interest on mortgage	1 790	
	Accrued expenses		1 790

b.	Date	Particulars	Dr	Cr
	31/3/23	Income summary	6 240	
		Advertising		6 240

Date	Particulars	Dr	Cr
31/3/23	Sales	315 200	
	Income summary		315 200

Date	Particulars	Dr	Cr
31/3/23	Income summary	235 000	
	Cost of goods sold		235 000

Date	Particulars	Dr	Cr
31/3/23	Capital	15 400	
	Drawings		15 400

Emma's Emporium Income Statement for year ended 31 March 2023				
Revenue	\$	\$	\$	
Sales			315 200	
Less Sales returns			(1 000)	
			314 200	
Less Cost of goods sold			(235 000)	
Gross profit			79 200	
Add Other income				
Dividends			410	
			79 610	
Less expenses				
Distribution costs				
Advertising	6 240			
Shop wages	82 960			
Depreciation on shop equipment	860	90 060		
Administrative expenses				
Accountancy fees	1 100			
General expenses	15 690			
Insurance (general)	760			
Rates	2 250			
Depreciation on buildings	6 500			
Bad debts	720			
Doubtful debts	<u>40</u>	27 060		
Finance costs				
Interest on mortgage	11 790	11 790		
Total expenses			128 910	
LOSS for the year			\$ (49 300	

Statement of I	Emporium Financial P March 202	osition	
	\$	\$	\$
Current assets			
Accounts receivable (Note 1)		6 720	
Bank		3 200	
Inventory		36 200	
Prepayments		250	
Accrued income		90	46 4
Non-current assets			
Investments (Note 2)			
Shares in Flightways Ltd		7 000	
Property, plant and equipment (Note 3)			
Total carrying amount		177 590	
Intangible assets			
Goodwill		8 000	192 5
Total assets			239 0
Less Liabilities			
Current liabilities			
Accounts payable	6 036		
GST	1 116		
Accrued expenses	2 750	9 902	
Non-current liabilities			
Mortgage		131 000	
Total liabilities			<u>(140 °</u>
Net assets			\$98 1
Equity			
Opening capital			162 8
Less LOSS for the year			(49 3
Less Drawings			(15 4
Closing capital			\$98 1

Notes to the Statement of Financial Position

1. Accounts receivable

Accounts receivable	7 000
Less Allowance for doubtful debts	(280)
	6 720

2. Investments

Investments consist of Shares in *Flightways Ltd*. The current fair value of the shares is \$6 400, which is the current market value on balance date.

3. Property, plant and equipment

	Shop equipment	Buildings	Land	Total
	\$	\$	\$	\$
For year ended 31 March 2023				
Opening carrying amount	7 250	117 700	60 000	184 950
Plus Additions	0	0	0	0
Less Disposals	0	0	0	0
Less Depreciation	(860)	(6 500)	0	(7 360)
Closing carrying amount	6 390	111 200	60 000	177 590
As at 31 March 2023				
Cost	8 600	130 000	60 000	198 600
Accumulated depreciation	(2 210)	(18 800)	0	(21 010)
Carrying amount	6 390	111 200	60 000	177 590

Depreciation is calculated on the following property, plant and equipment assets as follows:

- Building: 5% p.a. of cost, using the straight-line method.
- Shop equipment: 10% p.a. of cost, using the straight-line method.

4. Loan / Mortgage

The mortgage has an interest rate of 9% and a maturity date of 31 March 2030.

e. Sales

Date	Particulars	Dr	Cr	Bal
31/3/23	Balance			315 200 cr
	Income summary	315 200		0

Shop wages

Date	Particulars	Dr	Cr	Bal
31/3/23	Balance			82 000 dr
	Accrued expenses	960		82 960 dr
	Income summary		82 960	0

Accrued expense

Date	Particulars	Dr	Cr	Bal
31/3/23	Shop wages		960	960 cr
	Interest on mortgage		1 790	2 750 cr

Rates

Date	Particulars	Dr	Cr	Bal
31/3/23	Balance			2 500 dr
	Prepayments		250	2 250 dr
	Income summary		2 250	0

Prepayments

Date	Particulars	Dr	Cr	Bal
31/3/23	Rates	250		250 dr

Bad debts

Date	Particulars	Dr	Cr	Bal
31/3/23	Balance			400 dr
	Accounts receivable	320		720 dr
	Income summary		720	0

Allowance for doubtful debts

Date	Particulars	Dr	Cr	Bal
31/3/23	Balance			240 cr
	Doubtful debts		40	280 cr

Accumulated depreciation on buildings

Date	Particulars	Dr	Cr	Bal
31/3/23	Balance			12 300 cr
	Depreciation on buildings		6 500	18 800 cr

Capital

Date	Particulars	Dr	Cr	Bal
31/3/23	Balance			162 848 cr
	Income summary	49 300		113 548 cr
	Drawings	15 400		98 148 cr

2. a.

	Date	Particulars	Dr	Cr
	31/3/XX	Prepayments	250	
ſ		Advertising		250

Date	Particulars	Dr	Cr
31/3/XX	Accounts receivable	736	
	GST		96
	Sales		640

Date	Particulars	Dr	Cr
31/3/XX	Cost of goods sold	300	
	Inventory		300

Date	Particulars	Dr	Cr
31/3/XX	Bad debts	400	
	GST	60	
	Account receivable		460

Date	Particulars	Dr	Cr
31/3/XX	Allowance for doubtful debts	90	
	Doubtful debts		90

Date	Particulars	Dr	Cr
31/3/XX	Interest on mortgage	1 600	
	Accrued expenses		1 600

Date	Particulars	Dr	Cr
31/3/XX	Rent received	500	
	Income in advance		500

Date	Particulars	Dr	Cr
31/3/XX	Depreciation on buildings	1 800	
	Accumulated depreciation on buildings		1 800

Date	Particulars	Dr	Cr
31/3/XX	Depreciation on shop equipment	885	
	Accumulated depreciation on shop equipment		885

b.	Date	Particulars	Dr	Cr
	31/3/XX	Income summary	9 600	
		General expenses		9 600

Date	Particulars	Dr	Cr
31/3/XX	Income summary	1 200	
	Bad debts		1 200

Date	Particulars	Dr	Cr
31/3/XX	Income summary	7 600	
	Interest on mortgage		7 600

Date	Particulars	Dr	Cr
31/3/XX	Capital	6 500	
	Drawings		6 500

Date	Particulars	Dr	Cr
31/3/XX	Rent received	6 000	
	Income summary		6 000

Da	te	Particulars	Dr	Cr
31/3	/XX	Income summary	80 845	
		Capital		80 845

Anureet's Asian Supermarket Income Statement for the year ended 31 March 20XX				
Revenue	\$	\$	\$	
Sales			205 640	
Less Cost of goods sold			(65 300)	
Gross profit			140 340	
Add Other income				
Rent received		6 000		
Gain on sale of shop equipment		350	<u>6 350</u>	
			146 690	
Less Expenses				
Distribution costs				
Advertising	3 250			
Wages	32 600			
Depreciation on shop equipment	<u>885</u>	36 735		
Administrative expenses				
Accountancy fees	1 200			
General expenses	9 600			
Insurance (general)	560			
Rates	1 800			
Postage and stationery	5 000			
Discount allowed	440			
Depreciation on buildings	1 800			
Bad debts	1 200			
Doubtful debts	(90)	21 510		
Financial costs				
Interest on mortgage	<u>7 600</u>	<u>7 600</u>		
Total expenses			65 845	
Profit for the year			\$80 845	

Anureet's Asian Supermarket **Statement of Financial Position** as at 20XX \$ \$ \$ **Current assets** Accounts receivable (Note 1) 3 430 Bank 6 956 Inventory 23 300 Prepayments 33 936 250 Non-current assets Property, plant and equipment (Note 2) 183 865 Total carrying amount 183 865 **Total assets** 217 801 **Less** Liabilities **Current liabilities** Accounts payable 2 240 GST 3 536 Income in advance 500 Accrued expenses 1 600 7 876 Non-current liabilities Mortgage (3) 95 000 **Total liabilities** (102 876) Net assets \$114 925 **Equity** Opening capital 40 580 Plus Profit for the year 80 845 (6 500) Less Drawings \$114 925 Closing capital

Notes to the Statement of Financial Position

1. Accounts receivable

d.

Accounts receivable	3 500
Less Allowance for doubtful debts	(70)
	3 430

2. Property, plant and equipment

	Shop equipment	Buildings	Land	Total
	\$	\$	\$	\$
For year ended 31 March 20XX				
Opening carrying amount	10 850	57 700	120 000	188 550
Plus Additions	0	0	0	0
Less Disposals	(2 000)	0	0	(2 000)
Less Depreciation	(885)	(1 800)	0	(2 685)
Closing carrying amount	7 965	55 900	120 000	183 865
As at 31 March 20XX				
Cost	10 000	60 000	120 000	190 000
Accumulated depreciation	(2 035)	(4 100)	0	(6 135)
Carrying amount	7 965	55 900	120 000	183 865

Depreciation is calculated on the following property, plant and equipment assets as follows:

- Building: 3% p.a. of cost using the straight-line method.
- Shop equipment: 10% p.a. using the diminishing-value method.

3. Loan / Mortgage

The mortgage has an interest rate of 8% and a maturity date of 31 March 2030.

e. Gain on sale of shop equipment

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			350 cr
	Income summary	350		0

Interest on mortgage

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			6 000 dr
	Accrued expenses	1 600		7 600 dr
	Income summary		7 600	0

Accrued expense

Date	Particulars	Dr	Cr	Bal
31/3/XX	Interest on mortgage		1 600	1 600 cr

Sales

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			205 000 cr
	Accounts receivable		640	205 640 cr
	Income summary	205 640		0

Prepayments

Date	Particulars	Dr	Cr	Bal
31/3/XX	Advertising	250		250 dr

Allowance for doubtful debts

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			160 cr
	Doubtful debts	90		70 cr

Depreciation on buildings

Date	Particulars	Dr	Cr	Bal
31/3/XX	Accumulated depreciation on buildings	1 800		1 800 dr
	Income summary		1 800	0

Inventory

	Date	Particulars	Dr	Cr	Bal
	31/3/XX	Balance			23 600 dr
ſ		Cost of goods sold		300	23 300 dr

Capital

Date	Particulars	Dr	Cr	Bal
31/3/XX	Balance			40 580 cr
	Income summary		80 845	121 425 cr
	Drawings	6 500		114 925 cr

3. a. Date Particulars Dr Cr 31/3/25 Office salaries 320 Accrued expenses 320

Date	Particulars	Dr	Cr
31/3/25	Prepayments	120	
	Insurance		120

	Date	Particulars	Dr	Cr
3	31/3/25	Accrued income	80	
		Dividends received		80

Date	Particulars	Dr	Cr
31/3/25	Interest on loan	220	
	Accrued expenses		220

Date	Particulars	Dr	Cr
31/3/25	Vans	12 000	
	GST	1 800	
	Accounts payable		13 800

Date	Particulars	Dr	Cr
31/3/25	Bad debts	240	
	GST	36	
	Accounts receivable		276

Date	Particulars	Dr	Cr
31/3/25	Doubtful debts	48	
	Allowance for doubtful debts		48

Date	Particulars	Dr	Cr
31/3/25	Depreciation on vans	4 700	
	Accumulated depreciation on vans		4 700

Date	Particulars	Dr	Cr
31/3/25	Depreciation on office furniture	2 000	
	Accumulated depreciation on office furniture		2 000

c.

Date	Particulars	Dr	Cr
31/3/25	Cost of goods sold	1 140	
	Inventory		1 140

 Date
 Particulars
 Dr
 Cr

 31/3/25
 Income summary
 2 300

 Advertising
 2 300

Date	Particulars	Dr	Cr
31/3/25	Sales	320 600	
	Income summary		320 600

Date	Particulars	Dr	Cr
31/3/25	Gain on sale of office furniture	300	
	Income summary		300

Date	Particulars	Dr	Cr
31/3/25	Dividends received	400	
	Income summary		400

Date	Particulars	Dr	Cr
31/3/25	Capital	8 500	
	Drawings		8 500

Date	Particulars	Dr	Cr
31/3/25	Income summary	48 462	
	Capital		48 462

Date	Particulars	Dr	Cr
31/3/25	Income summary	480	
	Bad debts		480

Date	Particulars	Dr	Cr
31/3/25	Income summary	18 820	
·	Office salaries		18 820

Tane's Top-Notch Furniture Income Statement for the year ended 31 March 2025			
Revenue	\$	\$	\$
Sales			320 600
Less Cost of goods sold			(169 140)
Gross profit			151 460
Add Other income			
Dividends received		400	
Gain on sale of office furniture		300	700
			152 160
Less Expenses			
Distribution costs			
Advertising	2 300		
Sales assistant wages	45 000		
Depreciation on vans	4 700		
Shop rent	21 000		
Shop power and lighting	2 400	75 400	
Administrative expenses			
Office salaries	18 820		
Telephone	1 130		
Insurance	3 780		
Postage and stationery	1 200		
Discount allowed	120		
Depreciation on office furniture	2 000		
Bad debts	480		
Doubtful debts	<u>48</u>	27 578	
Financial costs			
Interest on loan	<u>720</u>	<u>720</u>	
Total expenses			103 698
Profit for the year			\$48 462

d.

Tane's Top-Notch Furniture **Statement of Financial Position** as at 31 March 2025 \$ \$ \$ **Current assets** 5 432 Accounts receivable (Note 1) **GST** 2 036 Inventory 33 300 Accrued income 80 Prepayments 120 40 968 Non-current assets Investments (Note 2) Shares in HIJ Ltd 10 000 Property, plant and equipment (Note 3) Total carrying amount 40 800 50 800 Total assets 91 768 **Less** Liabilities **Current liabilities** Accounts payable 17 480 Bank 1 106 Accrued expenses 540 Loan (4) 6 000 <u>25 126</u> **Total liabilities** (25 126)\$66 642 Net assets Equity Opening capital 26 680 Plus Profit for the year 48 462 Less Drawings (8 500) Closing capital \$66 642

Notes to the Statement of Financial Position

1. Accounts receivable

Accounts receivable	5 600
Less Allowance for doubtful debts	(168)
	5 432

2. Investments

Investments consist of shares in *HIJ Ltd*. The current fair value of the shares is \$11 200, which is the current market value on balance date, 31 March 2025.

3. Property, plant and equipment

	Vans	Office furniture	Total
	\$	\$	\$
For year ended 31 October 2025			
Opening carrying amount	23 500	14 000	37 500
Plus Additions	12 000	0	12 000
Less Disposals	0	(2 000)	(2 000)
Less Depreciation	(4 700)	(2 000)	(6 700)
Closing carrying amount	30 800	10 000	40 800
As at 31 October 2025			
Cost	48 000	15 000	63 000
Accumulated depreciation	(17 200)	(5 000)	(22 200)
Carrying amount	30 800	10 000	40 800

Depreciation is calculated on the following property, plant and equipment assets as follows:

- Vans: 20% p.a. of cost, using the diminishing-value method.
- Office furniture: \$2 000 p.a., using the straight-line method.

4. Loan / Mortgage

The loan has an interest rate of 12% and a maturity date of 31 October 2035.

e. Cost of goods sold

Date	Particulars	Dr	Cr	Bal
31/3/25	Balance			168 000 dr
	Cost of goods sold	1 140		169 140 dr
	Income summary		169 140	0

Interest on loan

Date	Particulars	Dr	Cr	Bal
31/3/25	Balance			500 dr
	Accrued expenses	220		720 dr
	Income summary		720	0

Accrued expenses

Date	Particulars	Dr	Cr	Bal
31/3/25	Interest on loan		220	220 cr
	Office salaries		320	540 cr

Insurance

Date	Particulars	Dr	Cr	Bal
31/3/25	Balance			3 900 dr
	Prepayments		120	3 780 dr
	Income summary		3 780	0

Accounts payable

Date	Particulars	Dr	Cr	Bal
31/3/25	Balance			3 680 cr
	Van and GST		13 800	17 480 cr

Doubtful debts

Date	Particulars	Dr	Cr	Bal
31/3/25	Allowance for doubtful debts	48		48 dr
	Income summary		48	0

Capital

Date	Particulars	Dr	Cr	Bal
31/3/25	Balance			26 680 cr
	Income summary		48 462	75 142 cr
	Drawings	8 500		66 642 cr

Inventory

Date	Particulars	Dr	Cr	Bal
31/3/25	Balance			34 440 dr
	Cost of goods sold		1 140	33 300 dr

4. Part A

Ella's Electrics **Cash Flow Statement** for the year ended 31 March 2020 \$ \$ Receipts Accounts receivable 44 780 Cash sales 210 000 Capital 10 000 Commission received 3 000 Sale of shop fittings 1 700 Sale of computer 100 269 580 Total receipts **Payments** Accounts payable 81 400 Rent 36 000 Insurance 5 250 General expenses 3 250 Loan 9 600 Interest on mortgage 1 100 Distribution costs 29 400 55 000 Wages Drawings 28 950 Computer 2 300 9 200 Shop fittings Total payments 261 450 8 130 Increase in cash for the year Opening bank balance 160 Closing bank balance 8 290

Workings

Accounts receivable: $4\ 200\ +\ 46\ 000\ -\ 1\ 600\ -\ 420\ -\ 3\ 400\ =\ 44\ 780$

Accounts payable: $7\,800 + 81\,000 - 1\,800 - 5\,600 = 81\,400$

Drawings: $32\ 000 - 3\ 050 = 28\ 950$

Shop fittings: Receipt 900 + 800 = 1700, Payment 9200 - 5000= 4200

Computer: Receipt 600 – 500 = 100 b. Close the commission received account

31/3/2020	Commission received	3 000	
	Income summary		3 000
	(Closing commission received)		

Bank

1/4/2019	Balance			160 cr
	Total receipts	269 580		269 740 dr
	Total payments		261 450	8 290 dr

Part B

	* =			
a.	Ella's I Property, plant and ed	E <i>lectrics</i> quipment N	lote (extra	ct)
		Vehicles	Shop fittings	Office computer
		\$	\$	\$
	For the year ended 31 March 2020			
	Opening carrying amount	26 160	7 700	740
	Additions	0	8 000	2 000
	Disposals	0	(900)	(600)
	Depreciation	(5096)	(1 332)	(700)
	Closing carrying amount	21 064	13 468	1 440
	As at 31 March 2020			
	Cost	62 000	18 600	2 000
	Accumulated depreciation	(40 936)	(5 132)	(560)
	Closing carrying amount	21 064	13 468	1 440

Depreciation is calculated on the following property, plant and equipment assets at the following rates:

- Depreciation on vehicles is calculated using units-of-use method at a rate of 26 c/km.
- Depreciation on shop fittings is 9% diminishing value (based on closing balance).
- · Depreciation on office computer is 28% straight line.

b. i.	31/3/2020	Depreciation on shop fittings	1 332	
		Accumulated depreciation shop fittings		1 332
		(Recording depreciation on shop fittings)		

ii.	31/3/2020	Wages	920	
		Accrued expenses		920
		(Recording wages owing on balance day)		

iii. Wages

31/3/2020	Balance			55 000 dr
	Accrued expenses	920		55 920 dr
	Income summary		55 920 dr	0

iv. Accumulated depreciation on vehicles

1/4/2020	Balance		38 840 cr
	Depreciation on vehicles	5 096	40 936 cr

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Activity 10B: NCEA revision questions (page 122)

1. a. Gifts for Living Income Statement (extract) for the year ended 31 March 2018 Distribution expenses Advertising 4 120 Electricity – shop 5 400 Sales wages 36 750 Depreciation on shop fixtures and equipment 2 000 48 270

b.	Gifts for Living Statement of Financial Position as at 31 March 2018			
	Current assets			
	Inventory		24 000	
	Accounts receivable (1)		<u>12 250</u>	36 250
	Non-current assets			
	Property, plant and equipment			
	Total carrying amount (2)			140 000
	Total assets			176 250
	Liabilities			
	Current liabilities			
	Accounts payable	10 868		
	Bank	2 500		
	GST	2 916		
	Accrued expenses	<u>1 350</u>	17 634	
	Non-current liabilities			
	Mortgage (3)		<u>74 000</u>	(91 634)
	Net assets			<u>\$84 616</u>
	Equity			
	Opening capital			88 600
	Profit for the year			31 016
	Drawings			(35 000)
	Closing capital			<u>\$84 616</u>

Notes to the Statement of Financial Position:

1. Accounts receivable

Accounts receivable	12 500
Allowance for doubtful debts	(250)
	12 250

2. Mortgage

The mortgage has an interest rate of 9%, and a maturity date of 30 June 2025.

2. a. Cash received from customers:

Accounts receivable + invoices issued - bad debts - closing Accounts receivable

\$42 000 + \$265 000 - \$200 - \$46 000 = \$260 800

ο.	Landscape Visions Statement of Cash Flows (extract) for the year ended 31 March 2018				
	Cash receipts				
	Cash from Accounts receivable / customers	260 800			
	Loan from BNZ	35 000			
	Sale of delivery van	2 000			
	Total receipts		297 800		

3. a. i.

Date	Particulars	Dr	Cr
31/3/20	Accrued income	1 800	
	Dividends received		1 800

ii.	Date	Particulars	Dr	Cr
	31/3/20	Interest on loan	600	
		Accrued expenses		600

iii.	Date	Particulars	Dr	Cr
	31/3/20	Prepayments	1 000	
		Insurance		1 000

iv.	Date	Particulars	Dr	Cr
	31/3/20	Depreciation on clinic vehicle	1 920	
		Accumulated depreciation on clinic vehicle		1 920

V.	Date	Particulars	Dr	Cr
	31/3/20	Bad debts	80	
		GST	12	
		Accounts receivable		92

vi.	Date	Particulars	Dr	Cr
	31/3/20	Doubtful debts	230	
		Allowance for doubtful debts		230

vii.	Date	Particulars	Dr	Cr
	31/3/20	Income summary	680	
		Bad debts		680

viii.	Date	Particulars	Dr	Cr
	31/3/20	Capital	16 000	
		Drawings		16 000

b. Dividends received

Date	Particulars	Dr	Cr	Bal
31/3/20	Balance			600 cr
	Accrued income		1 800	2 400 cr
	Income summary	2 400		0

Accrued expenses

Date	Particulars	Dr	Cr	Bal
31/3/20	Interest on loan		600	600 cr

Allowance for doubtful debts

Date	Particulars	Dr	Cr	Bal
31/3/20	Balance			500 cr
	Doubtful debts		230	730 cr

4. Working

Cash from Accounts receivable: $12\ 000\ +\ 42\ 000\ -\ 1\ 200\ -\ 13\ 600\ =$

\$39 200

Cash paid to Accounts payable: $3\ 400\ +\ 54\ 000\ -\ 3\ 900\ =\ \$53\ 500$

Quickshift Removals Statement of Cash Flows for the year ended 31 December 2022			
Cash flows in			
Cash from Accounts receivable	39 200		
Cash fees received / Removal fees	86 200		
Sale of delivery van	13 000		
Loan	40 000		
Dividend from Van Lines Ltd	<u>1 750</u>	180 150	
Less Cash flows out			
Cash paid to suppliers / Accounts payable	53 500		
Delivery van purchase	55 000		
Advertising	4 500		
Insurance	6 200		
Wages	27 000		
Loan repayment	31 000		
Interest	8 900		
Donation	200	(186 300)	
Net decrease in cash		(6 150)	
Plus opening bank balance 1/1/22		10 000	
Closing bank balance 31/12/22	\$3 850		

5. a.	Date	Particulars	Dr	Cr
	31/3/20	Prepayments	80	
		Insurance		80

b.	Date	Particulars	Dr	Cr
	31/3/20	Accounts receivable	2 760	
		Tour revenue received		2 400
		GST		360

C.	Date	Particulars	Dr	Cr
	31/3/20	Bad debts	800	
		GST	120	
		Accounts receivable		920

d.	Date	Particulars	Dr	Cr
	31/3/20	Allowance for doubtful debts	40	
		Doubtful debts		40

e. Accumulated depreciation on tour vans

Date	Particulars	Dr	Cr	Bal
1/04/19	Balance			13 000 cr
31/3/20	Depreciation on tour vans		5 400	18 400 cr

f. Interest on loan

Date	Particulars	Dr	Cr	Bal
31/3/20	Balance			720 dr
	Accrued expenses	240		960 dr
	Income summary		960	0

g. Tour revenue received

Date	Particulars	Dr	Cr	Bal
31/3/20	Balance			78 800 cr
	Accounts receivable		2 400	81 200 cr
	Income summary	81 200		0

6. Part A

Martha's Vehi Income Statement for the ye	•		2019
	\$	\$	
Revenue			
Repair income		351 200	
Other income			
Interest received		<u>1 250</u>	
TOTAL INCOME			352 45
Less Expenses			
Workshop and repair expenses			
Mechanics' wages	100 000		
Workshop expenses	75 000		
Workshop rent	32 000		
Depreciation on workshop equipment	20 000		
Electricity	<u>36 000</u>		
		263 000	
Administrative expenses			
Accountancy fees	12 000		
Bad debts	2 000		
Electricity	9 000		
Office insurance	4 000		
Depreciation on office equipment	2 000		
Doubtful debts	<u>294</u>	29 294	
Finance costs			
Interest on loan	<u>4 500</u>	<u>4 500</u>	
TOTAL EXPENSES			296 79
Profit (loss) for the year			\$55 65

b. i.	31/03/19	Accounts receivable	1 380	
		Repair income		1 200
		GST		180

31/03/19	Income summary	294		ı
	Doubtful debts		294	ı

ii.		Capital					
	1/04/18	Balance			176 500 cr		
		Drawings	40 000		136 500 cr		
		Income summary		55 656	192 156 cr		

Part B

a. i. Cash paid to suppliers:

Opening accounts payable \$30 000 + invoices received \$920 000 - discount received \$8 000 - closing accounts payable \$25 000 = \$917 000

ii.	Flash Furniture Cash Flow Statement (extract) for the year ended 31 March 2019					
	\$ \$					
	Less Payments					
	Cash to suppliers	917 000				
	Business expenses	65 000				
	Wages	120 000				
	Drawings	33 500				
	Delivery van	69 000				
	Total cash payments		1 204 500			

Property, plant and equipme	Property, plant and equipment Note (extract)					
	Deliver y vans	Shop equipment				
	\$	\$				
For the year ended 31 March 2019						
Opening carrying amount	55 000	60 000				
Plus Additions	60 000	0				
Less Disposals	(15 000)	0				
Less Depreciation	(12 000)	(6 000)				
Closing carrying amount	88 000	54 000				
As at 31 March 2019						
Cost	140 000	80 000				
Less Accumulated depreciation	(52 000)	(26 000)				
Closing carrying amount	88 000	54 000				

Part C

Best Fash Statement of Financial as at 31 Marc	Position (extra	act)
Current liabilities		
Accounts payable	48 300	
Accrued expenses	2 500	
Income in advance	3 000	
Loan	12 000	
Bank	20 000	
Total current liabilities		85 800
Non-current liabilities		
Mortgage (due October 2030)	180 000	
Total non-current liabilities		<u>180 000</u>
Total liabilities		265 800
Net assets		205 000
Equity		
Opening capital	200 000	
Plus profit for the year	65 000	
Less Drawings	(60 000)	
Closing capital		205 000

b. i.	30/03/19	Wages	2 500	
		Accrued expenses		2 500
	30/03/19	Prepayments	600	
		Insurance		600

30/03/19	Cost of goods sold	6 000			
	Inventory		6 000		
	5				

Depreciation office equipment						
30/03/19	Accumulated depreciation on office equipment	3 000		3 000	Dr	
	Income Summary		3 000	0		

Office equipment					
1/04/18	Balance			50 000	Dr
31/03/19	Accounts payable	22 000		72 000	Dr

7. Part A

Stationery Pad Income Statement for the year ending 31 March 2018							
	\$	\$	\$				
Revenue							
Sales			990 000				
Less Cost of goods sold			(586 000)				
Gross profit			404 000				
Other income							
Rent received			24 000				
			428 000				
Less Expenses							
Distribution expenses							
Advertising	11 000						
Electricity	15 400						
Insurance	3 500						
Sales staff salaries	126 000						
Depreciation on buildings	9 200						
Depreciation on shop fittings	<u>4 100</u>	169 200					
Administrative expenses							
Accountancy fees	3 000						
Bad debts	2 000						
Electricity - Office	6 600						
Insurance – Office	1 500						
Office expenses	33 600						
Depreciation on office equipment	2 000						
Doubtful debts	(200)	48 500					
Finance costs							
Interest on mortgage	<u>6 875</u>	<u>6 875</u>					
Total expenses			224 575				
Total expenses Profit(loss) for the year			\$203 425				

Part B

Garden Life Statement of Financial Position (extract) as at 31 March 2018									
Note \$ \$									
Current assets									
Accounts receivable	1	9 155							
Bank		20 000							
Inventory		74 000							
Accrued income		1 500							
Prepayments		3 000							
Total current assets			107 655						

Current liabilities		
Accounts payable	20 299	
GST	5 916	
Accrued expenses	2 000	
Total current liabilities		28 215

Note 1 – Accounts receivable

	\$	\$
Accounts receivable	9 655	
Less Allowance for doubtful debts	(500)	
		9 155

b. i.	30/3/18	Prepayments	3 000	
		Insurance		3 000

ii.	30/3/18	Depreciation on trailers	4 000	
		Accumulated depreciation		4 000
		on trailers		4 000

iii.	30/3/18	Dividends received	2 000	
		Income summary		2 000

iv.	Bad debts								
	30/3/18	Balance			1 600 dr				
		Accounts receivable	300		1 900 dr				
		Income summary		1 900	0				

V.	Acc	umulated depreciation	– Deliv	ery veh	icles
	30/3/18 Balance				20 000 cr
		Depreciation on delivery vehicle		25 000	45 000 cr

Part C

a. Cash from credit customers:

Opening accounts receivable \$1500 + invoices issued \$3000 - credit notes issued \$200 - bad debts \$100 - closing accounts receivable 2000 = 2200

b. Cash paid to fuel suppliers:

Opening accounts payable \$900 + invoices received \$1 200 - discount received \$50 - closing accounts payable 750 = 1300

C.

<i>Jetboat Fun</i> Cash Flow Statement (extract) for the month ended 31 December 2018						
	\$	\$				
Receipts						
Cash from accounts receivable	2 200					
Cash from cash customers	4 000					
Interest received	150					
Sale of office equipment	<u>500</u>					
Total receipts		6 850				
Less Payments						
Accounts payable / Fuel suppliers	1 300					
Advertising	400					
Rent	1 000					
Wages	1 800					
Business expenses	<u>2 300</u>					
Total payments		(6 800)				
Net increase (decrease)		50				
Opening bank balance		2 000 in funds				
Closing bank balance		\$2 050				

(Note: Sale of equipment \$600 is a foreign item.)

Chapter 11

The answers provided are examples only. They indicate the depth of knowledge required from students. Other responses are possible.

Activity 11: Generic internal controls (page 144)

- a. Separation of duties is important to ensure that a person cannot order books for him- or herself and get the bookshop to pay for the order. Separation of duties would involve having one employee put in orders for stock, and another deal with paying the invoices for the stock purchases. This means that the orders are checked and that the bookshop receives the stock ordered.
 - b. Authorisation means that someone in a position of responsibility has the final say over whether stock is ordered. It is important that one person is in charge of ordering books (or at least checking and approving the orders) because this will prevent staff members from ordering books for themselves – each order will be checked to ensure that the bookshop needs the items. Having an authorisation system in place also avoids the problem of double-ordering books, which could arise if two different staff members order the same item.
 - c. By using the till roll on the cash register, adequate documentary evidence is created and kept of every 'cash received' transaction. This ensures that there is adequate documentation of money received. This will enable accurate journals to be prepared and ensure a check against the money banked. It will also mean that at the end of the day the manager can count the money in the till and check it against the till roll, to identify theft or inaccurate recording of transactions.
 - d. Checking the bank statement against the cash journals is an important control because the bank statement provides an independent check on money received and paid by the bookshop, and verifies the accuracy of this information. Discrepancies between the journals and bank statement could indicate that theft has taken place.
- 2. Examples include (but are not limited to) the following.
 - All items are scanned and a receipt is produced for each transaction.
 A copy of each receipt is kept in the cash register so the supermarket can check the money received against the cash register tape at the end of the day.

- When check-out operators change over, a new till drawer is used so
 that each employee is responsible for his or her own drawer. In this
 way, any errors can be accounted for, and discrepancies can be traced
 back to the person responsible.
- The money in the cash drawer is checked at the end of the shift to see if the amount matches the amount on the cash register printout.
- Any refunds given or the correction of an incorrect ringing on the till
 have to be authorised by the supervisor. This prevents the possible
 problem of the check-out operator giving friends 'refunds'.
- 3. Examples, which will vary depending on school canteen set-up, include (but are not limited to) the following.
 - a. Inventory strength
 - There is no inventory that is accessible to the students it is all kept behind a counter/screen. This prevents theft by customers.
 - The canteen staff ensure that all new stock is put at the back
 of the fridges/shelves, so that the oldest stock is sold first. This
 avoids the problem of stock becoming obsolete and having to be
 discarded because it has passed its 'best before' date.
 - b. Cash receipt weakness
 - No receipts are issued. This means there is no proof of how much money the canteen has received for the day. This could mean that the staff might be undercharging, or possibly stealing money, and there would be no documentation to help prove this.
- 4. If the employee who receives the money is also the person who prepares the cash receipts and banks the money, that employee could easily steal some of the money before it is deposited into the bank, then change the records to cover this theft, by making the cash receipts journal match the amount of money actually banked. The employee wouldn't get caught, because no one else is involved in the process and so the error would remain undetected.
- 5. If the employee who receives the inventory when it is delivered is the same person who ordered the inventory, he or she could easily order stock for him- or herself, have the business pay for it, and take it home when it arrives.

Chapter 12

The answers provided are examples only. They indicate the depth of knowledge required from students. Other responses are possible.

Activity 12A: Inventory controls (page 148)

- The purchase order form provides evidence of, and ensures adequate documentation for all the business's orders. It means Campbell's Camping Supplies Store knows exactly what it has ordered and can later check this against the packing slip and invoice to make sure the business is receiving what it ordered.
- 2. Having purchases authorised by one person prevents different members of staff ordering the same stock, thus having overstocking of items in some areas. This could lead to losses through stock becoming obsolete. If one person authorises all purchases, it should prevent this problem and it will also prevent staff members from ordering goods for their personal use and getting the business to pay for the goods.
- 3. a. Inventory objectives not being met:
 - · Adequate records of inventory on hand are kept.
 - Inventory is kept secure and safe from theft and fraud.
 - Minimum stock levels are maintained.
 - b. Two 'easy fixes' need to be implemented. Firstly, my parents need to change the combination lock. Only my parents and one or two other employees should know the combination. This will help ensure the stock is safe from employee theft, and narrow down suspects if some stock does go missing. There also need to be inventory records in the storeroom, where all inventory entering and leaving the store is recorded. The employee taking the stock must also sign for it. This will help ensure that the inventory on hand is known, thus avoiding running out of stock. It will also help ensure that inventory records are accurate, and can be checked by a stock-take.

- 4. a. Separation of duties is important to help lessen the opportunity for employees to steal from the business and cover their tracks. Separation of duties is lacking in Nicholson and Company because Sam orders the inventory, checks the inventory off when it arrives and signs the packing slip for payment by Sue. Sam could easily order inventory for himself, keep it when it arrives and then get the business to pay for it. Someone else should check the inventory off when it arrives and put it on the shelves to make it harder for Sam to steal it.
 - b. It is important for businesses to keep adequate documentation, ideally consecutively pre-numbered. *Nicholson and Company* uses a range of documents (order forms, invoices, packing slips and so on) but does not keep enough of them. The order form is thrown out, so the business relies only on Sam's signed packing slip to update the inventory records. When Tane makes the payment he does not have a copy of the order or packing slip, so there is no proof that the goods were ordered or received. (Could also discuss invoices and receipts at point of sale, which is good.)
 - c. Authorisation is important so that only some people may do a task, therefore they are able to check for approval, and it also makes it easier to discover who is responsible if there is a problem. Sam has the authority to order the inventory. This is a good example of authorisation and prevents several people from ordering the same inventory and over-stocking. However, Jack should authorise all payments and not just leave signed cheques. Leaving signed cheques means that Tane could write cheques out for himself or others, effectively stealing from *Nicholson and Company*.

Activity 12B: Elements of an inventory subsystem (page 153)

- 1. The perpetual inventory system keeps a 'theoretical' running record of all inventory that should be on hand. The system requires the use of inventory cards (or other ledger accounts) that record whenever inventory is bought or sold, to keep a record of the inventory the business should have by increasing or decreasing the inventory account. In addition, it keeps a running record of cost of goods sold, sales, and sales returns.
- 2. Advantages include the following.
 - The business can trace missing or stolen inventory. This is done
 by comparing the theoretical record of inventory on hand on the
 inventory card with the total calculated after completing a stock-take.
 The difference identifies missing or unaccounted-for inventory.
 - The business can prepare regular financial statements without having to do a stock-take each time, which saves the business money. Doing so is possible because the perpetual system keeps a running record of inventory on hand, sales, and cost of goods sold.
 - The business can set reorder points and quantity so the business
 does not run out of stock or carry too much stock. This is good
 because it should help maximise sales and profit since the customers
 are kept happy by having sufficient inventory, and it minimises
 obsolete inventory.
- 3. A stock-take is the process of physically counting every item of stock on a particular day. This often requires businesses to shut early or open late in order for staff to complete this process. Normally all stock is counted twice (by two different people) as a double check. A stock-take is needed to verify the actual amount of inventory on hand and must be completed at the end of each financial year.
- 4. a. On 26 July 2020 Betty's Boutique ordered on credit from Clothing Galore 20 coats at \$120 excluding GST and 10 dresses at \$32 excluding GST each, totalling \$3 128 including GST. Purchase order number 2938426. This order was authorised by Betty, the owner.
 - b. The use of the purchase order, which required an authorising signature, is a key internal control. The purchase order helps to ensure the inventory is needed by Betty's Boutique and helps to

- prevent an employee being able to order clothes for themselves. This protects the business from having to pay for goods the business does not receive. Another internal control is having the pre-printed purchase order number. The number helps the business file the document, and check that all have been used and filed numerically. This allows the business to identify whether the business is missing any order forms, which could indicate a staff member has tried to purchase inventory for themself.
- 5. The use of the payment voucher, which required two authorising signatures, is a key internal control. It shows that two people agree that this account (for Clothing Galore) should be paid, and that it is a legitimate business payment. The payment voucher has reference identification of the original purchase order, packing slip and invoice so the auditor (or owner, or anyone) can check the details to ensure they match and are legitimate. Having these references also helps confirm that the business is paying only for goods it ordered and received, which helps protect the business's money.
- 6. The amount of stolen inventory can be identified by comparing the amount of inventory that is actually on hand, as established by a stock-take, against the inventory cards, which show the amount of inventory the business thinks it should have (theoretical amount on hand). The difference is the amount that is missing, possibly stolen.
- 7. Ensuring that inventory purchases are authorised is an important control to ensure that the inventory is needed, and a legitimate business purchase. Having someone in authority approve the purchase helps prevent employees purchasing inventory for personal use (fraud), which protects the business's cash flow and profit, as the business is not paying for inventory it does not keep, and does not have obsolete stock from ordering too much inventory.
- 8. It is important that payments to Accounts payable are authorised by someone not involved with the purchasing/ordering of the inventory, otherwise it would be easy for the employee to order stock for themselves and pay the account with the business's money. When the payment is authorised, it should be checked against the order form and the packing slip to make sure the payment is legitimate.
- 9. a. It is important to have a purchase order because it helps keep a record of what has been ordered. This helps prevent ordering the same inventory twice, which is a waste of money and can lead to wastage/obsolete stock. Having an order form allows the business to have a record of what was ordered, which it can check against the inventory when it arrives to make sure that it is the correct inventory / can check against the invoice to make sure the business pays only for inventory that it ordered.
 - One internal control present on the purchase order form is the document number. This helps the business file the document, and check that all have been used and filed numerically. This allows the business to identify if the business is missing any order forms, which could indicate a staff member has tried to purchase inventory for themself. Another internal control is the requirement for the purchase order to be authorised (signed). This is to ensure the inventory is needed by *Fitness World* and to prevent employees being able to order goods for themselves. This protects the business from having to pay for goods the business does not receive.
 - b. Having a reorder point is important because it should prevent the business from running out of inventory. This means that customers are kept happy by having inventory on hand and there will be increasing sales. Having a reorder quantity helps make the ordering process easier and quicker, and it should also mean the business is avoiding over-ordering stock (leading to possible obsolescence). Having optimum inventory levels helps maximise sales and profit.
 - c. A reorder point is the level of inventory Fitness World has on hand at the time when it needs to order more. (The reorder quantity is how many items should be ordered, which is printed out by the computer.) The minimum stock level is the smallest amount of inventory Fitness

- World is prepared to have before it risks running out and therefore losing its good reputation with customers. The reorder point should be above the minimum stock level and there should be a sufficient quantity of stock to allow for more sales until the new order arrives without reaching the minimum stock level.
- d. When the inventory arrives, one of the shop assistants checks the packing slip and passes it to the office manager. The office manager receives the checked packing slip from the shop assistant and checks it against the purchase order form. This is important for Fitness World so that it does not receive unwanted goods it did not order, which would mean it would spend money paying for goods it did not need or receive. It also helps prevent Fitness World from running out of inventory if what was ordered does not arrive. That could lead to dissatisfied customers and a loss in sales, so it important to check that the goods received match the goods ordered to prevent these problems.
- e. When the inventory arrives, one of the shop assistants checks the packing slip and passes it to the office manager. The office manager receives a copy of the purchase order form and matches it against the invoice when the invoice arrives, before preparing payment. This procedure ensures Fitness World pays only for goods that were ordered. This is important because the business does not want to spend money for goods that it does not need, which would be bad for cash flow.

Activity 13A: Inventory cards (page 160)

- The purpose of preparing an Inventory card is to record whenever inventory arrives at or leaves the business. A different card is kept for each inventory type. The balance column should match the Inventory ledger account.
- 2. (240 + 240 + 420) = \$900
- 3. a. FIFO

	Inventory card									
Name: Dining table				Measurement base: FIFO						
Invent	ory number: 8	80			Location	: Shop				
			IN			OUT			BALANCE	
Date	Particulars	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$
Aug 1	Balance							15	220	3 300
3	Sales				2	220	440	13	220	2 860
5	Purchases	4	240	960				13	220	2 860
								4	240	960
8	Returns out				1	220	220	12	220	2 640
								4	240	960
14	Sales				12	220	2 640			
					3	240	720	1	240	240
15	Purchases	6	200	1 200				1	240	240
								6	200	1 200
20	Sales				1	240	240			
					2	200	400	4	200	800
25	Purchases	5	280	1 400				4	200	800
								5	280	1 400
26	Sales				4	200	800			
_					1	280	280	4	280	1 120
31	Shortage				1	280	280	3	280	840

b. Weighted average

				In	ventory c	ard				
Name: Dining table				Measurement base: Weighted average						
Invent	ory number: 8	30			Location	: Shop				
			IN			OUT			BALANCE	
Date	Particulars	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$
Aug 1	Balance							15	220.00	3 300.00
3	Sales				2	220	440	13	220.00	2 860.00
5	Purchases	4	240	960				17	224.71	3 820.00
8	Returns out				1	224.71	224.71	16	224.71	3 595.29
14	Sales				15	224.71	3 370.65	1	224.64	224.64
15	Purchases	6	200	1 200				7	203.52	1 424.64
20	Sales				3	203.52	610.56	4	203.52	814.08
25	Purchases	5	280	1 400				9	246.01	2 214.08
26	Sales				5	246.01	1 230.05	4	246.01	984.03
31	Shortage				1	246.01	246.01	3	246.01	738.02

4. a. FIFO

				In	ventory c					
Name:	Rimu Scotch	chests			Measure	ment base:	FIFO			
Invent	ory number: 2	! 5			Location	: Shop and	storage ro	om		
			IN			OUT			BALANCE	
Date	Particulars	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$
Oct 1	Balance							10	320	3 200
								5	336	1 680
3	Sales				4	320	1 280	6	320	1 920
								5	336	1 680
5	Sales				6	320	1 920			
					2	336	672	3	336	1 008
8	Purchases	5	352	1 760				3	336	1 008
								5	352	1 760
14	Sales				3	336	1 008			
					3	352	1 056	2	352	704
15	Purchases	8	368	2 944				2	352	704
								8	368	2 944
20	Sales				2	352	704			
					1	368	368	7	368	2 576
22	Returns in	3	320	960				3	320	960
								7	368	2 576
25	Purchases	5	336	1 680				3	320	960
								7	368	2 576
								5	336	1 680
26	Sales				3	320	960			
					2	368	736	5	368	1 840
								5	336	1 680
31	Drawings				2	368	736	3	368	1 104
								5	336	1 680
			1							

b. Weighted average

				In	ventory ca	ırd				
Name:	Rimu Scotch	chests			Measure	ment base:	Weighted	average		
Invent	ory number: 2	25			Location	Shop and	storage ro	om		
			IN			OUT			BALANCE	
Date	Particulars	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$
Oct 1	Balance							15	325.33	4 880.00
3	Sales				4	325.33	1 301.32	11	325.33	3 578.68
5	Sales				8	325.33	2 602.64	3	325.35	976.04
8	Purchases	5	352	1 760.00				8	342.01	2 736.04
14	Sales				6	342.01	2 052.06	2	341.99	683.98
15	Purchases	8	368	2 944.00				10	362.80	3 627.98
20	Sales				3	362.80	1 088.40	7	362.80	2 539.58
22	Returns in	3	325.33	975.99				10	351.56	3 515.57
25	Purchases	5	336	1 680.00				15	346.37	5 195.57
26	Sales				5	346.37	1 731.85	10	346.37	3 463.72
31	Drawings				2	346.37	692.74	8	346.37	2 770.98

5. a. FIFO

				Inven	tory card					
Name:	Pine sea chests				Measure	ment base:	FIFO			
Invent	ory number: 36				Location	: Shop and	storage ro	om		
			IN			OUT			BALANCE	
Date	Particulars	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$
Jun 1	Balance							12	40	480
								4	48	192
								8	56	448
4	Sales				12	40	480			
					3	48	144	1	48	48
								8	56	448
6	Purchases	8	40	320				1	48	48
								8	56	448
								8	40	320
10	Sales				1	48	48			
					7	56	392	1	56	56
								8	40	320
18	Purchases	5	48	240				1	56	56
								8	40	320
								5	48	240
20	Sales				1	56	56			
					8	40	320			
					3	48	144	2	48	96
25	Drawings				2	48	96	0	0	0
27	Returns in	2	40	80				2	40	80
28	Purchases	5	56	280				2	40	80
								5	56	280
29	Returns out				2	40	80	5	56	280
30	Shortage				2	56	112	3	56	168
30	Error – Scotch chests	4	52	208				3	56	168
								4	52	208

b. Weighted average

Invent	ory card										
Name:	Pine sea chests				Measure	ment base:	Weighted	average			
Invent	ory number: 36				Location:	Shop and	storage ro	om			
			IN			OUT			BALANCE		
			Unit			Unit			Unit		
Date	Particulars	Qty	price \$	Total \$	Qty	price \$	Total \$	Qty	price \$	Total \$	
Jun 1	Balance							24	46.67	1 120	
4	Sales				15	46.67	700.05	9	46.66	419.95	
6	Purchases	8	40	320				17	43.53	739.95	
10	Sales				8	43.53	348.24	9	43.52	391.71	
18	Purchases	5	48	240				14	45.12	631.71	
20	Sales				12	45.12	541.44	2	45.14	90.27	
25	Drawings				2	45.14	90.27	0	0.00	0.00	
27	Returns In	2	40	80				2	40.00	80.00	
28	Purchases	5	56	280				7	51.43	360.00	
29	Returns Out				2	51.43	102.86	5	51.43	257.14	
30	Shortage				2	51.43	102.86	3	51.43	154.28	
30	Error	4	52	208				7	51.75	362.28	

Activity 13B: Inventory journals and ledgers (page 170)

1. March 3 Purchased inventory on credit costing \$4 600 including GST

Date	Particulars	Debit	Credit
Mar 3	Inventory	4 000	
	GST	600	
	Accounts payable		4 600
	(Buying inventory on credit)		

March 5 Sold inventory which cost $2\,000$ excluding GST for $4\,600$ including GST

Date	Particulars	Debit	Credit
Mar 5	Cost of goods sold	2 000	
	Inventory		2 000
	(Recognising inventory sold at cost price)		
	Accounts receivable	4 600	
	GST		600
	Sales		4 000
	(For sale of inventory on credit)		

March 7 Returned inventory which cost \$460 including GST, as it was faulty

Date	Particulars	Debit	Credit
Mar 7	Accounts payable	460	
	GST		60
	Inventory		400
	(Returned faulty stock on credit)		

March 12 Customer returned goods to us. They were sold for \$276 including GST, and had a cost price of \$138 including GST

Date	Particulars	Debit	Credit
Mar 12	Inventory	120	
	Cost of goods sold		120
	(Sales return at cost price)		
	Sales returns	240	
	GST	36	
	Accounts receivable		276
	(For sales return on credit)		

March 24 Some inventory has become damaged and needs to be revalued. The inventory is to be decreased by \$2 000 excluding GST.

Date	Particulars	Debit	Credit
Mar 24	Write down of inventory/Cost of goods sold	2 000	
	Inventory		2 000
	(Inventory revaluation)		

March 28 Owner took inventory which has a selling price of \$1 840 including GST home for personal use. The inventory originally cost \$800 excluding GST when the business purchased it.

Date	Particulars	Debit	Credit
Mar 28	Drawings	920	
	GST		120
	Inventory		800
	(Owner took stock for personal use)		

March 31 The annual stock-take revealed that some inventory has gone missing. The cost price of this inventory (excluding GST) is \$320.

Date	Particulars	Debit	Credit
Mar 31	Inventory shortage	320	
	Inventory		320
	(Recognising inventory shortage)		
	Cost of goods sold	320	
	Inventory shortage		320
	(Writing off inventory shortage to cost of goods sold)		

2. a. Journals

Jan 3 Sold 4 bookcases at \$230 including GST on credit, cost price \$120 excluding GST

Date	Particulars	Debit	Credit
Jan 3	Cost of goods sold	480	
	Inventory – bookcase		480
	Accounts receivable	920	
	GST		120
	Sales		800

Jan 5 Purchased 4 more bookcases each costing \$130 excluding GST

Date	Particulars	Debit	Credit
Jan 5	Inventory – bookcase	520	
	GST	78	
	Accounts payable		598

Jan 8 Returned 1 bookcase which cost \$120 excluding GST, because it was faulty

Date	Particulars	Debit	Credit
Jan 8	Accounts payable	138	
	GST		18
	Inventory – bookcase		120

Jan 20 The owner took one bookcase home for daughter's 21st birthday gift. The bookcase is currently being sold for \$184 including GST, and it had a cost price of \$138 including GST.

Date	Particulars	Debit	Credit
Jan 20	Drawings	138	
	GST		18
	Inventory – bookcase		120

Jan 24 One of the bookcases sold for \$184 including GST (cost price \$120 excluding GST) was returned

Date	Particulars	Debit	Credit
Jan 24	4 Inventory – bookcase		
	Cost of goods sold		120
	Sales returns	160	
	GST	24	
	Accounts receivable		184

Jan 31 Performed stock-take and found that 1 bookcase which cost \$120 excluding GST was missing.

Date	Particulars	Debit	Credit
Jan 31	Inventory shortage	120	
	Inventory – bookcase		120
	Cost of goods sold	120	
	Inventory shortage		120

Jan 31 Some of the bookcases are damaged and have lost retail value. The closing value of the inventory on hand is now \$2 230.

Date	Particulars	Debit	Credit
Jan 31	Write-down of inventory/Cost of goods sold	210	
	Inventory – bookcase		210

Jan 31 Recording error

Date	Particulars	Debit	Credit
Jan 31	Inventory – Bookcase	1 200	
	Inventory – Sea chest		1 200

b. Ledgers

Inventory - Bookcases

Jan 1	Balance			2 400 dr
3	Cost of goods sold		480	1 920 dr
5	Accounts payable	520		2 440 dr
8	Accounts payable		120	2 320 dr
14	Cost of goods sold		960	1 360 dr
15	Accounts payable	1 200		2 560 dr
20	Drawings		120	2 440 dr
24	Cost of goods sold	120		2 560 dr
31	Shortage		120	2 440 dr
31	Write-down of inventory		210	2 230 dr
31	Inventory – Sea chests	1 200		3 430 dr

Cost of goods sold

Jan 3	Inventory – bookcases	480		480 dr
14	Inventory – bookcases	960		1 440 dr
24	Inventory – bookcases		120	1 320 dr
31	Shortgage	120		1 440 dr

Sales

Jan 3	Accounts receivable	800	800 cr
14	Accounts receivable	1 280	2 080 cr

Sales returns

Jan 24 Accounts red	eivable 160	160 dr
---------------------	-------------	--------

3. a. Ledger accounts

Inventory - Gadgets

	. y Caagots			
Mar 1	Balance			11 200 dr
4	Accounts payable	1 728		12 928 dr
5	Cost of goods sold		4 480	8 448 dr
6	Cost of goods sold	560		9 008 dr
8	Accounts payable	2 240		11 248 dr
10	Cost of goods sold		1 680	9 568 dr
12	Accounts payable		576	8 992 dr
14	Accounts payable	3 504		12 496 dr
16	Shortage		560	11 936 dr
18	Write-down/COGS		2 160	9 776 dr
20	Inventory – widgets	560		10 336 dr

Cost of goods sold

Mar 5	Inventory – gadgets	4 480		4 480 dr
6	Inventory – gadgets		560	3 920 dr
10	Inventory – gadgets	1 680		5 600 dr
16	Shortage	560		6 160 dr
18	Write-down/Inventory	2 160		8 320 dr

Sales

Mar 5	Accounts receivable	13 440	13 440 cr
10	Accounts receivable	6 000	19 440 cr

Accounts payable

Mar 4	Inventory – gadgets and GST		1 987.20	1 987.20 cr
8	Inventory – gadgets and GST		2 576	4 563.20 cr
12	Inventory – gadgets and GST	662.40		3 900.80 cr
14	Inventory – gadgets and GST		4 029.60	7 930.40 cr

Accounts receivable

Mar 5	Sales and GST	15 456		15 456 dr
6	Sales returns and GST		1 932	13 524 dr
10	Sales and GST	6 900		20 424 dr

Write-down of inventory

Mar 18	Inventory – gadgets	2 160		2 160 dr
	COGS		2 160	0

D.

Date	Particulars	Debit	Credit
Mar 4	Inventory – gadgets	1 728	
	GST	259.20	
	Accounts payable		1 987.20
Mar 10	Cost of goods sold	1 680	
	Inventory – gadgets		1 680
	Accounts receivable	6 900	
	GST		900
	Sales		6 000
Mar 16	Inventory shortage	560	
	Inventory – gadgets		560
	Cost of goods sold	560	
	Inventory shortage		560
Mar 18	Write-down of inventory/COGS	2 160	
	Inventory – gadgets		2 160
Mar 20	Inventory – gadgets	560	
	Inventory – widgets		560

Note: In this topic Inventory write-down could be recorded against Cost of goods sold.

4. Examples:

The perpetual inventory system provides a theoretical running total of the inventory that should be on hand, so that interim reports can be prepared and inventory levels monitored.

The perpetual inventory system has a theoretical running total of stock, and the business can use this to maintain optimum stock levels and ensure that it does not run out of stock. It can also introduce reorder points using the data obtained from the perpetual inventory method. Missing stock can be identified by the difference between the theoretical balance for inventory that should be on hand and the amount of stock that is on hand after carrying out the stock-take.

- Missing stock can be identified as the difference between the theoretical balance for inventory that should be on hand and the amount of stock that is actually on hand after the stock-take has been carried out.
- 6. There is a continuous running balance of the inventory on hand, and this amount can be used to prepare the Statement of Financial Position. At the same time, the Cost of goods sold account is being updated continuously so that this figure can be used in the Income Statement, allowing a business to prepare interim reports.
- 7. Carrying out a physical stock-take is very important because it provides an accurate count of the inventory actually on hand on the day of the stock-take. This is the accurate figure, and the one that should be used in the end-of-year financial statements. The amount can also be compared with the running balance on the inventory card, and if there is a difference between the two figures, this indicates that theft of stock has taken place, or that the recording practices of the employees are poor.

8. a. FIFO

				Inv	entory ca	rd				
Name:	Gift boxes				Measure	ement base	: FIFO			
Invent	ory number: 18				Location	n: Shop				
			IN			OUT			BALANCE	
Date	Particulars	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$
Jan 1	Balance							500	6.00	3 000
								100	6.40	640
3	Purchases	310	5.60	1 736				500	6.00	3 000
								100	6.40	640
								310	5.60	1 736
4	Sales				150	6.00	900	350	6.00	2 100
								100	6.40	640
								310	5.60	1 736
6	Returns out				50	6.00	300	300	6.00	1 800
								100	6.40	640
								310	5.60	1 736
7	Sales				300	6.00	1 800			
					50	6.40	320	50	6.40	320
								310	5.60	1 736
8	Purchase	300	6.00	1 800				50	6.40	320
								310	5.60	1 736
								300	6.00	1 800
10	Sales				50	6.40	320			
					200	5.60	1 120	110	5.60	616
								300	6.00	1 800
11	Returns in	30	6.00	180				30	6.00	180
								110	5.60	616
								300	6.00	1 800
12	Drawings				10	6.00	60	20	6.00	120
								110	5.60	616
								300	6.00	1 800
14	Shortage				20	6.00	120	110	5.60	616
								300	6.00	1 800
16	Write-down							110	3.20	352
								300	6.00	1 800
17	Error – Baskets				10	3.20	32	100	3.20	320
								300	6.00	1 800

b. Journal entries

Date	Particulars	Debit	Credit
Jan 6	Accounts payable	345	
	GST		45
	Inventory – gift boxes #18		300
Jan 7	Cost of goods sold	2 120	
	Inventory – gift boxes #18		2 120
	Accounts receivable	4 830	
	GST		630
	Sales		4 200
Jan 8	Inventory – gift boxes #18	1 800	
	GST	270	
	Accounts payable		2 070
Jan 11	Inventory – gift boxes #18	180	
	Cost of goods sold		180
	Sales returns	360	
	GST	54	
	Accounts receivable		414
Jan 12	Drawings	69	
	GST		9
	Inventory – gift boxes #18		60

c. Weighted average

	Inventory card									
Name: Gift boxes Measurement base: Weighted average										
Invent	ory number: 18				Location	Shop				
			IN			OUT			BALANCE	
			Unit			Unit			Unit	
Date	Particulars	Qty	price \$	Total \$	Qty	price \$	Total \$	Qty	price \$	Total \$
Jan 1	Balance							600	6.07	3 640.00
3	Purchases	310	5.60	1 736.00				910	5.91	5 376.00
4	Sales				150	5.91	886.50	760	5.91	4 489.50
6	Returns out				50	5.91	295.50	710	5.91	4 194.00
7	Sales				350	5.91	2068.50	360	5.90	2 125.50
8	Purchases	300	6.00	1 800.00				660	5.95	3 925.50
10	Sales				250	5.95	1487.50	410	5.95	2 438.00
11	Returns in	30	5.91	177.30				440	5.94	2 615.30
12	Drawings				10	5.94	59.40	430	5.94	2 555.90
14	Shortage	·			20	5.94	118.80	410	5.94	2 437.10
16	Write-down*							410	5.21	2 135.70
18	Inventory – baskets				10	5.21	52.10	400	5.21	2 083.60

 $^{*(110 \}times 5.94 = 653.40) - (110 \times 3.20 = 352.00)$

^{= 301.40} decrease in total inventory

^{\$2 437.10 - \$301.40 = 2 135.70}

Activity 13C: Inventory interpretations (page 178)

- a. SWEETS 4U has a reorder quantity of 22, as shown by the ordering of 22 bags of lollipops on 6 May and 20 May. SWEETS 4U also appears to order
 every fortnight, because these purchases are two weeks apart.
 - b. The quantity of sales fluctuates a lot from none on some days, to five on 12 May and up to twelve on 30 May. This makes is difficult for SWEETS 4U to carry enough stock without overstocking bringing the risk of carrying lollipops that are past their best-before date.
 - c. Average shortage of three bags in one month is high if regular. There were two errors or mis-recordings in the month. Not at risk of running out of lollipops, as the smallest amount of inventory on hand comprised 14 bags.
 - d. The recurring errors indicate that staff members are not careful when recording purchases and sales of inventory and they mix up the quantities and items of the inventory. This can lead to over-ordering of some inventory, which is not good considering this is a short-dated item and food can date quickly. Alternative could have customers unhappy by running out of lollies they think are in stock.
 - e. The shortage is established when Lulu does a stock-take. She compares the physical stocktake against the theoretical inventory on hand, which is on the inventory card. When the card shows more stock than SWEETS 4U has and it is not a recording error, then a shortage is found. In this case on 31 May the card stated 24 bags of lollipops, but the physical count showed 21 bags, therefore three bags were missing. Missing inventory increases the cost of goods sold without providing any income, which reduces the gross profit for SWEETS 4U.
- 2. No answer provided. Discuss in class or ask teacher to mark. Use resource information and the inventory, as well as your notes from a. to e. to help you.

Activity 14A: Adapted NCEA examination questions (page 181)

Product: Hoodies DATE PARTICULARS IN OUT I 2018 No. @ \$ No. @ \$ No. 5 Sales 15 16.00 240.00 10 16.80 168.00 40	BALANCE	
2018 No. @ \$ No. @ \$ No. 5 Sales 15 16.00 240.00	BALANCE	
5 Sales 15 16.00 240.00		
	@	\$
10 16.80 168.00 40		
	16.80	672.00
8 Purchases 20 17.20 344.00 40	16.80	672.00
20	17.20	344.00
9 Returns out 3 17.20 51.60 40	16.80	672.00
17	17.20	292.40
10 Drawings 2 16.80 33.60 38	16.80	638.40
17	17.20	292.40

b.	5/7/18	Cost of goods sold	408	
		Inventory – Hoodies		408
		Accounts receivable – North Bridge Football Club	920	
		GST		120
		Sales		800

C.	31/7/18	Write-down of Inventory / COGS	360	
		Inventory – Hoodies		360

- d. Max can prepare an Income Statement without doing a stock-take because he has a ledger account for cost of goods sold which is updated after every inventory transaction. This means he can calculate the business's gross profit without a stock-take.
- e. A minimum inventory (stock) level is a quantity of different types of inventory that is the point at which more inventory is ordered, to help prevent the shop running out of inventory. Max should have a minimum stock level for his hoodies and other clothes so that *Cool Clothes* does not run out of clothes that customers want, which would result in a loss of sales.
- f. Max should make sure that there is separation of duties when ordering and receiving the inventory. One staff member should have responsibility for ordering the new stock and another for receiving it and checking it off against the packing slip. This will help prevent someone ordering inventory for themself and keeping it when it arrives.
 - Max should use a purchase order form to evidence all inventory that is ordered. The purchase order form should be authorised by Max or another senior staff member. This will help ensure that the inventory is needed and is not a personal order. The order form should be checked against the packing slip when the goods arrive.
- g. It is important that *Cool Clothes* does not over-order its inventory because it might then have too much inventory and be unable to sell it all, and might then need a discount sale, which would reduce the income from sales. In addition, clothes go out of fashion and can become obsolete within a year, so if *Cool Clothes* over-orders, it might have to sell stock for less than it paid for the stock, which will reduce profit. Another reason is that if *Cool Clothes* has too much inventory that is not selling, although the stock has been paid for the business is not receiving any money from sales, so it might struggle to have cash-flow to pay expenses.

h.	Date	Particulars	Debit	Credit
		Inventory – Hoodies	640	
		Inventory – T-shirts		640

- i. Some advantages of using the perpetual inventory system for Cool Clothes are the following.
 - Max can identify if inventory has gone missing / been stolen as he can compare the inventory cards stating how much inventory should be on hand, against the stock-take – the difference measures the value of stolen or missing inventory.
 - Max has a running record of the inventory that should be on hand and cost of goods sold from the year so far, so he can prepare interim financial statements for Cool Clothes without needing to do a stock-take.
 - Max can manage the inventory of Cool Clothes more efficiently by having reorder points and quantities so the business does not run out of
 inventory and lose sales, or carry too much inventory and end up losing profit by holding obsolete stock.

2. a. First in, first out.

b.

NZ4U – I	Inventory Card									
Product	: Paua Necklaces									
DATE PARTICULARS IN					OUT		BALANCE			
2018		No.	@	\$	No.	@	\$	No.	@	\$
May 22	Sales				30	4.24	127.20			
					5	4.40	22.00	35	4.40	154.00
May 23	Drawings				4	4.40	17.60	31	4.40	136.40
May 28	Returns in	3	4.00	12.00				3	4.00	12.00
								31	4.40	136.40
May 30	Purchases	10	5.60	56.00				3	4.00	12.00
								31	4.40	136.40
								10	5.60	56.00
May 31	Error – MoP							1	4.00	4.00
					2	4.00	8.00	31	4.40	136.40
								10	5.60	56.00

c.	NZ4U General Journal										
	20/5/18	Inventory – Paua necklaces	176.00								
		GST	26.40								
		Paua Works / Accounts payable		202.40							

- d. The perpetual inventory system can help manage inventory levels in two main ways ensuring the inventory does not run out by having a reorder point so when stock levels reach the pre-arranged quantity the business should order more inventory. It should also prevent the business having too much inventory, because staff know how much inventory (e.g. paua necklaces) they should have on hand so they do not order more just because they think they need to. They should have a set quantity to reorder that they know (from past experience) can sell in a reasonable time.
- e. The perpetual inventory system has enabled Timu to discover that scenic books have gone missing because he can compare the theoretical balance in his scenic books inventory card or ledger account against the actual amount from the physical stock-take. If the stock-take quantity is less than the theoretical balance, this indicates that some of the books have gone missing.
- f. i. Purchase order it is important to check inventory when it arrives against the purchase order form to make sure that NZ4U receives all the inventory it is supposed to and to make sure NZ4U is not sent stock (which it will have to pay for) that it did not order.
 - ii. Packing slip it is important to check the inventory against the packing slip in case the supplier missed putting some inventory in the order, but says the inventory was sent. This helps prevent NZ4U paying for inventory that it did not receive. It also helps prevent running out of inventory NZ4U thinks it should have, but has never arrived.
- g. NZ4U should complete a stock-take at least once a year. They do this by counting every item of inventory on hand on a specific date and recording this (usually two people count each item as a double check). They should then compare the counted stock against the amount that the inventory cards/ ledgers state they should have on hand. The difference will indicate stolen and missing inventory. This will indicate whether they need to tighten inventory controls or check staff and customers more carefully. Having counted inventory makes the inventory on hand in the Statement of Financial Position and the profit in the Income Statement more accurate than just relying on inventory cards.
- h. i. The office manager orders the inventory, not the shop assistants, because the shop assistants could easily order inventory for themselves and keep it when it arrives. Filling out the requisition form provides documentation of inventory requested and who requested it, and it is then approved by the manager when the order is placed.
 - ii. The purchase requisition form is used to request that more inventory is ordered. It is a good control over inventory because it provides evidence, as well as helping ensure separation of duties (so staff do not order inventory for themselves) because it is used by someone else to place the order. Internal controls that should be present on the purchase requisition form include the following.
 - Purchase requisition number so NZ4U can identify if documents have gone missing.

- Authorisation signature the person requesting the inventory has to sign the form, so they are accountable for requesting the inventory. If
 inventory goes missing or is not needed, the matter can be followed up.
- . The form will have quantity and description of the inventory being requested so there is proof if the manager is unsure later.
- i. i. Timu views each of these documents before making the payment because they each have a different purpose. He checks the purchase order to make sure he is paying for inventory NZ4U ordered. He checks the packing slip to make sure he is paying for goods that have arrived in the shop already, and he checks the invoices to make sure the totals on all three documents agree and are legitimate inventory costs for NZ4U.
 - ii. Timu makes the payment, not the office manager, to help ensure separation of duties. The office manager orders the inventory so should not pay for it as well, otherwise it would be easy for the office manager to order inventory for him- or herself, remove it from the shelves at some stage, and then pay for it from the business bank account. Having separation of duties prevents this happening.

Activity 14B: Golf Galore (page 187)

- 1. Source documents include the following.
 - Purchase requisition to evidence what stock the warehouse manager wants ordered. This provides two signatures those of the warehouse manager and the purchasing clerk – as proof of who has ordered the inventory in case there is a problem or over-ordering occurs.
 - Packing slip to evidence what goods have been delivered. This is signed by the person receiving the inventory so if the inventory does not appear on
 the shelves that staff member is accountable.
 - Purchase order to evidence what inventory has been ordered by the business. This document is pre-numbered and can be checked to see if any documents go missing. If so, it could indicate that the purchasing clerk has ordered some inventory for him- or herself.
 - Invoice to outline the amount owed for the inventory purchased on credit and to detail what inventory is being charged for. This document should
 have the purchase order number written on it so Jane can check that the invoice is for inventory that Golf Galore ordered.
- 2. a. Control strengths include the following.
 - The purchase of inventory is authorised by the purchasing officer. This is a strength because it prevents the warehouse manager ordering stock for himself and keeping it when it arrives.
 - There is separation of duties in that the person ordering the inventory is not the person who receives the inventory. This prevents the purchasing officer ordering stock for himself and keeping it when it arrives.
 - The warehouse manager checks the goods against the packing slip when they arrive. This ensures that the goods that were sent have arrived so the business does not have to pay for them later when they might not have received them.
 - The accounts clerk checks the invoice against the purchase order before authorising payment. This should prevent *Golf Galore* paying for goods it did not order or has not received, thus protecting its cash.
 - The purchase order is pre-numbered so that all orders can be traced and accounted for. If an order form was missing it would be noticed by the accounts clerk and could indicate poor records and/or theft by the purchasing officer.
 - b. Control weaknesses include the following.

The purchase requisition is not filed and is not given to the accounts clerk. This means that the purchasing manager could order different stock from what is on the requisition form, so he could order stock for himself, or leave stock out, which could lead to a shortage and loss of sales.

When the stock arrives, the packing slip is not compared against the requisition form. This means that the warehouse manager is not sure that he has received what he requested, and does not know if the purchasing clerk changed the order.

Activity 14C: Music Mania (page 188)

1.

	Inventory card												
Name:	T-shirts				Measurement base: FIFO								
Invento	ry number: 7				Location: Shop								
			IN			OUT			BALANCE				
DATE	PARTICULARS	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$			
Aug 1	Balance							15	10.00	150.00			
5	Sales				10	10.00	100.00	5	10.00	50.00			
6	Purchases	20	9.40	188.00				5	10.00	50.00			
								20	9.40	188.00			
14	Sales				5	10.00	50.00						
					7	9.40	65.80	13	9.40	122.20			
20	Drawings				2	9.40	18.80	11	9.40	103.40			
24	Sales				6	9.40	56.40	5	9.40	47.00			
25	Purchases	20	9.80	196.00				5	9.40	47.00			
								20	9.80	196.00			
28	Sales poster error				5	9.40	47.00	20	9.80	196.00			
31	Shortage				2	9.80	19.60	18	9.80	176.40			

Name:	Posters				Measurement base: FIFO							
Invento	ry number: 8				Location:	Shop						
			IN		OUT			BALANCE				
DATE	PARTICULARS	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total S		
Aug 1	Balance							22	5.00	110.00		
3	Sales				2	5.00	10.00	20	5.00	100.00		
5	Purchases	10	5.50	55.00				20	5.00	100.00		
								10	5.50	55.00		
8	Returns out				1	5.00	5.00	19	5.00	95.00		
								10	5.50	55.00		
17	Sales				19	5.00	95.00					
					6	5.50	33.00	4	5.50	22.00		
18	Purchases	26	5.70	148.20				4	5.50	22.00		
								26	5.70	148.20		
20	Sales				4	5.50	22.00					
					3	5.70	17.10	23	5.70	131.10		
22	Returns in	2	5.00	10.00				2	5.00	10.00		
								23	5.70	131.10		
25	Purchases	6	4.60	27.60				2	5.00	10.00		
								23	5.70	131.10		
								6	4.60	27.60		
26	Sales				2	5.00	10.00					
					3	5.70	17.10	20	5.70	114.00		
								6	4.60	27.60		
28	Error – T-shirts	2	5.00	10.00				2	5.00	10.00		
		3	5.70	17.10			·	23	5.70	131.10		
								6	4.60	27.60		
31	Shortage				2	5.00	10.00					
					2	5.70	11.40	21	5.70	119.70		
								6	4.60	27.60		

2. (Examples but not limited to)

One main advantage for *Music Mania* of using the perpetual inventory system is that it helps identify missing inventory. This is because the perpetual inventory system keeps a theoretical balance of the amount and cost of inventory that should be on hand. When *Music Mania* carried out the stock-take on August 31, staff identified that 4 posters and 2 T-shirts were missing. This indicates that stock control needs to be tightened to minimise future shortages because an increase in theft reduces profit in the long run.

Another main advantage is that *Music Mania* can prepare financial statements without having to do a stock-take to calculate the inventory on hand or the cost of goods sold, since running records of these amounts are kept. In this case, if it had not done the stock-take it would have recorded T-shirt inventory at \$196.00 and posters at \$168.70, which would have enabled it to prepare the Statement of Financial Position; and the Income Statement could be prepared, because the cost of goods sold is calculated at \$188.10 for posters and \$319.20 for T-shirts. Although the shortages that were found would give different results, they would be immaterial and unlikely to influence the decisions of users of the financial statements.

- 3. A minimum stock level is a quantity of inventory that Music Mania has established to be the point at which inventory is re-ordered. Often the maximum quantity of inventory is also set. This helps the business avoid running out of stock and putting off customers. It also helps to ensure the business does not carry too much stock, which can become obsolete, so profit decreases. It appears that Music Mania has a minimum stock level for T-shirts of 5 T-shirts, because every time the stock on hand reached this quantity the business ordered 20 more the next day. However, the posters do not appear to have a re-order quantity or minimum point. The difference is possibly due to which group is popular at the time. The value of this inventory is not so great, so perhaps it is not so important. Having the re-order point for T-shirts helps make ordering easier, and keeps customers happy.
- 4. Optimum stock level is the theoretical idea that a business needs to have sufficient inventory to meet customer demand while at the same time not over-stocking, which leads to a slow inventory turnover and can lead to obsolete stock. Overstocking can also mean the business has to have discount

- sales to clear the stock and get cash-flow, which decreases the mark-up and profit in the future. It appears that *Music Mania* has a good level of inventory, especially with a re-order point and quantity for T-shirts. *Music Mania* should try to implement the same concept for posters, which should help avoid having to write-down out-of-date posters and prevent ordering randomly. *Music Mania* is often carrying about 30 posters and most orders appear to be for fewer than 8 (except for the school).
- 5. During a stock-take, employees of *Music Mania* count every item of inventory to have an accurate record of the quantity and value of inventory on hand. This is important in order to prepare accurate financial statements. In addition to this a stock-take can help identify weakness in internal control possibly employee theft, poor record keeping, and other missing inventory. This allows *Music Mania* to investigate the cause of the discrepancies between the inventory card and physical stock-take. In this case, the stock-take identified 2 missing T-shirts and 4 posters. If this was for a year it would probably be acceptable, but if this is a monthly count and it happens regularly, there is a costly problem with inventory control. This will lead to a decrease in profit and puts a strain on cash-flow if not addressed.
- 6. The manager of Music Mania counts the inventory that is ordered when it arrives in the store to check that all the goods the packing slip states are in the delivery are actually there; otherwise Music Mania might be charged for inventory it did not receive. It is important that the manager did not place the order, because it would be easy to order for himself and keep the inventory when it arrives. He, or someone else, should also check that the inventory that arrives is what was ordered, to avoid receiving and paying for inventory that is not wanted.

Activity 14D: Super Sports Supplies (page 192)

				Inventory	card					
Name:	Tennis racquets			Measurement base: Weighted average						
IN				OUT		BALANCE				
DATE	PARTICULARS	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$
July 1	Balance							45	76.00	3420.00
3	Sales				5	76.00	380.00	40	76.00	3040.00
5	Purchases	10	60.00	600.00				50	72.80	3640.00
8	Returns out				2	72.80	145.60	48	72.80	3494.40
17	Sales				25	72.80	1820.00	23	72.80	1674.40
18	Purchase	20	74.00	1480.00				43	73.36	3154.40
20	Drawings				2	73.36	146.72	41	73.36	3007.68
25	Sales				15	73.36	1100.40	26	73.36	1907.28
	Purchases	20	80.00	1600.00				46	76.25	3507.28
28	Error purchase – cricket bats	4	40.00	160.00				50	73.35	3667.28
31	Shortage				1	73.35	73.35	49	73.35	3593.93

	Inventory card												
Name:	Name: Cricket bats					nent base: W	eighted ave	rage					
			IN			OUT			BALANCE				
DATE	PARTICULARS	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$	Qty	Unit price \$	Total \$			
July 1	Balance							15	40.00	600.00			
5	Sales				8	40.00	320.00	7	40.00	280.00			
14	Sales				5	40.00	200.00	2	40.00	80.00			
18	Purchase	10	44.00	440.00				12	43.33	520.00			
20	Sales				4	43.33	173.32	8	43.34	346.68			
22	Returns in	1	40.00	40.00				9	42.96	386.68			
25	Sales				4	42.96	171.84	5	42.97	214.84			
28	Error tennis racquets				4	40.00	160.00	1	54.84	54.84			

2. a. (Examples but not limited to – reason to improve integrated in answer)

It does not appear that *Super Sports Supplies* has a re-order policy for cricket bats or a minimum stock level. The cricket bat quantity was allowed to get very low, in one case with only two bats left, before the bats were re-ordered. Two bats would be sold easily before the new order arrived. The re-order amount does not seem sufficient to cover the demand for the bats, unlike the tennis racquets, which are always re-ordered after sales to maintain a good stock level. *Super Sports Supplies* needs to implement a minimum stock level of probably eight to ten bats and a reorder quantity of between 10 and 15, definitely in the spring and summer months.

Poor record keeping is another reason for *Super Sports Supplies* running out of bats. The computer inventory card said there were five bats, but in reality there was only one, because the tennis racquets' purchase had been recorded incorrectly. This gave the shop a false understanding of the

- number of bats on hand, which would be why it could not find them. It is important that inventory purchases and sales are recorded correctly; otherwise, stock levels cannot be fixed.
- b. It appears that tennis racquets are re-ordered whenever there is a sale, and that the quantity is usually 20 (although 10 were ordered once). This could lead to Super Sports Supplies holding a large number of racquets and needing to have a discount clearance sale, which would decrease profits. The current minimum quantity appears to be more than 20, which seems quite high. I recommend that this be reduced to about 12 and that the reorder quantity be 15 to 20, which should help maintain a good supply of racquets without having too much excess stock. This should meet customer demand and keep sales up, improving profits.
- c. (Examples, not limited to)
 - By changing to the perpetual inventory system Mike has a theoretical record of the amount of inventory he should have on hand. This enables him to calculate shortages and possibly identify stolen stock if there is a difference between the physical stock count and the inventory card. This happened when the tennis racquet count was one less than the card, identifying one missing racquet. The periodic system would not identify a missing item. If there is a continual trend of missing stock then Mike could investigate his employees for theft, or might need to make his record-keeping more accurate, because that could also be the problem.
 - Another advantage is that Mike can now set a re-order point and a minimum stock level for all his inventory, which should help prevent his running out of stock, or becoming over-stocked, both of which have a negative effect on the business. If he keeps running out of inventory, customers will get annoyed and go elsewhere, resulting in lost sales and a decrease in potential profits. If he carries too much stock, he has spent the money paying his suppliers but has not recovered it through sales, and will often have to reduce the price to clear the stock. The decrease in price will decrease mark-up and possibly the final profit as well.
- d. By allowing only the two full-time staff to order the inventory, Mike is implementing the internal control of authorisation. Ensuring that ordering is authorised and carried out by only those staff should avoid inventory being ordered twice, by different people, or not being ordered because the part-time staff all think the others are doing it. This will also allow for separation of duties, because when the inventory arrives it should be a part-time worker who checks it off, to prevent the person doing the ordering keeping stock for himself when the order arrives. Separation of duties does not currently take place in this way, but it should.
- e. It is very important to check the inventory against the packing slip when the inventory arrives, to make sure the order is complete and nothing is missing. Otherwise, Super Sports Supplies could be charged and pay for inventory it never received, which would be a waste of money. Currently this procedure has a strength and a weakness. It is good it is checked off and the packing slip given to the office manager to check against the order form and invoice before paying the account. However, it should not be the full-time staff who check the goods when they arrive, because they could order something for themselves, keep it, sign the packing slip and the manager will pay for it later.
- f. The reason Super Sports Supplies carries out a stock-take is to count and have an accurate record of the amount of inventory actually on hand at a point in time. By doing the stock-take the employees physically count every item of stock and record it, often being double-checked by a second worker. Once the count is complete, the office manager or Mike can check the count against what the inventory cards show Super Sports Supplies should have. This will highlight discrepancies, which could be from human recording error, or indicate a customer or employee theft problem. By doing a stock-take and using the perpetual system, discrepancies can be monitored and investigated. A stock-take also provides the business with more accurate inventory records, because the missing stock identified is adjusted against the cost of goods sold, which means the gross profit and final profit for the year are more accurate. The stock-take also gives an accurate value for the inventory for reporting in the Statement of Financial Position.

Activity 14E: Formative assessment – *Tops-n-Tees* (page 195)

Part A

				Invento	ry card – Top	s-n-Tees					
Name: \	Name: White cotton tee shirt Size 12 Inventory number: 12WCT				Measureme	Measurement Base: Weighted average				Location: Shop/ Storeroom	
			IN		OUT				BALANCE		
Date	Particulars	Qty	@\$	Total \$	Qty	@\$	Total \$	Qty	@\$	Total \$	
Aug 1	Balance							8	6.50	52.00	
3	Sales				4	6.50	26.00	4	6.50	26.00	
7	Purchases	15	6.90	103.50				19	6.82	129.50	
8	Purchase returns				2	6.82	13.64	17	6.82	115.86	
9	Sales				6	6.82	40.92	11	6.81	74.94	
10	Sales returns	1	6.50	6.50				12	6.79	81.44	
15	Sales				10	6.79	67.90	2	6.77	13.54	
16	Purchases	8	9.20	73.60				10	8.71	87.14	
21	Purchases	15	6.80	102.00				25	7.57	189.14	
22	Error (14WCT)	4	6.30	25.20				29	7.39	214.34	
26	Drawings				3	7.39	22.17	26	7.39	192.17	
30	Sales				5	7.39	36.95	21	7.39	155.22	
31	Shortages				4	7.39	29.56	17	7.39	125.66	

Part B

No answer supplied because this is a formative assessment. Your teacher will discuss in class or mark. Check that you have written about stocktakes and shortages, ordering quantities and frequency, stock levels, customer satisfaction, profit margins and impact on profit, separation of duties, authorising, checking orders, errors, and having adequate documentation. Make sure you have linked to evidence from the case study and the inventory card you prepared. Make sure you have discussed that this is about white tee shirts. Is this a clothing item that will date easily or not? Is there a risk of obsolescence?

Chapter 15

The answers provided are examples only. They indicate the depth of knowledge required from students. Other responses are possible.

Activity 15: Accounts receivable subsystem (page 201)

- The potential customer's income to establish his/her ability to repay
 the amount of credit.
 - Job to establish if the person is in stable employment, or whether the work is likely to be seasonal. This helps determine whether the person will be able to repay debt.
 - What other liabilities the person has is he or she overcommitted already and perhaps not able to handle any more debt?
 - Does the potential customer own or rent the house in which he/she lives – this indicates financial security and whether the person is a 'flight risk'.
 - Credit history / credit rating (names of previous creditors) to establish whether the person has been a good debtor in the past and has a good history of repaying debts.
- The customer may not have paid off previous credit accounts and may have a lot of debt outstanding. The risk if they buy more on credit is that it is unlikely that the business will receive the money from them, increasing the value of their bad debt and reducing the business assets and profit.
- 3. This ensures that shop assistants in Sarah's Superstore cannot give credit to their friends. It also means that the manager will check to see if customers are up to date with their repayments before allowing them more credit. This reduces the likelihood of bad debts, or overdue accounts. It increases the likelihood that the business will receive the money owing to it from each credit sale.
- 4. This report shows how long the debt owed by each debtor has been outstanding. It allows Sarah's Superstore to stop credit if debts are outstanding over a certain period of time and can also indicate if debts are likely to become 'bad'. If credit is stopped on overdue debtors then they won't get more credit and the amount of potential bad debts should be reduced. It also signals how long debts have remained unpaid, so after a certain period, reminder letters can be sent and debt collectors can be used to recover the debt.
- 5. Processes:
 - When a customer phones through an order, the office manager takes the order and fills out a duplicate order received slip. She then passes the top copy of the order received slip to the shop assistant who fetches the goods and prepares a triplicate invoice. The shop assistant then passes the goods, with the top two copies of the invoice and order received slip to the manager. This ensures that Charlie's Cookware has accurate documents and records for Accounts receivable.
 - The manager checks that the order is correct, authorises the
 invoice, then files the second copy of the invoice and the order
 received slip together alphabetically. The manager then sends the
 goods and invoice to the customer. Authorising the credit sale should
 help minimise bad debts and prevent selling to people with bad
 credit.

- At the end of each week, the accounts clerk collects the invoice book from the shop assistant and updates the Accounts receivable ledger. At the end of each month, she prepares monthly statements and sends them to the customers. This helps ensure that all debtor records are up-to-date and accurate. Sending monthly accounts helps ensure debtors pay promptly.
- 6. Important features include the following.
 - The invoice should be pre-numbered so the business can check to make sure none have gone missing. If any are missing, it could highlight that a staff member has given credit to someone who should not have credit, or even to themselves.
 - The invoice should have a signature to authorise the credit being given. This approval of the reason for the credit being given protects the potential cash-flow of the business.
 - The invoice should have the name and contact details of the customer (possibly a customer number as well) so the business knows who and where to follow up if there are problems or the account is not paid, and is to be able to transfer the details on the document to the correct debtors ledger account.
- 7. The issuing of the credit note meets the internal control of adequate documentation, because the note provides evidence that the return has taken place, and of what was returned, why it was returned and what the value was. Because there is a signature on the credit note, there is the additional internal control of authorisation being met, because the person signing the document has approved the credit to ensure it is legitimate.
- 8. A credit limit is the maximum amount of credit that an Accounts receivable can be in debt for in total at any one time. The amount is important, since not all debtors have the same limit they have varying creditworthiness. Having a limit is important because it provides an amount that should be checked before a credit sale to ensure the customer has not exceeded their limit, in which case it would be doubtful they would be able to repay the extra amount.
- 9. A check of a customer's current credit situation is important because many debtors do not pay their accounts on time, and even if they are not at their limit, they might be at high risk of not paying. (A debtor could have a small amount outstanding from two months ago, in which case it would not be a good idea to sell to them on credit again until this amount is paid off.)
- 10. Bad debts are those debts that the business knows it will not get the money back from. Often a letter is received informing the business that the person will not be repaying the debt. Doubtful Debts are an estimation made to meet the qualitative characteristic of relevance to ensure that the amount of 'debtors' and 'profit' is not overstated. This amount is based on experience that not all debtors will pay in full and is usually a percentage of the current Accounts receivable total.
- 11. If a credit check is not done before selling on credit the debtor might not be suitable and might never pay their accounts. This could mean the business has effectively had inventory stolen (not paid for), which will reduce the business's profit. Because the business had to pay for the inventory when it bought the inventory and is not getting cash from the sale, its cash-flow will also struggle if the amounts are large, making it difficult for the business to repay its own creditors and expenses.

Activity 16A: Subsidiary ledger (page 207)

- The total of the list of Accounts receivable should equal the balance in the Accounts receivable control account in the general ledger. If these totals don't balance, it indicates that an error has been made.
- 2. If the business does not keep good control over its debtors, then it may not have enough money to pay its liabilities and other expenses. This will put the business's own credit rating at risk. / The business has sold the inventory to the debtors and must now get payment for it. If it doesn't, then the business has lost a lot of inventory and might not get the money back this will increase its bad debts and decrease its profit.

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3. a. Accounts receivable subsidiary ledger

J. Parker

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			330 dr
10	Sales and GST	414		744 dr
12	Sales returns and GST		160	584 dr
28	Sales and GST	230		814 dr
28	Bank		300	514 dr

L. Malone

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			650 dr
5	Sales and GST	736		1 386 dr
15	Bank		650	736 dr

L. Ko

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			520 dr
24	Sales and GST	515		1 035 dr
26	Sales returns and GST		230	805 dr

S. Adams

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			820 dr
12	Sales and GST	138		958 dr
14	Freight and GST	46		1 004 dr
18	Bank		560	444 dr

T. Walsh

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			710 dr
30	Bad debts and GST		710	0

V. Adams

Date	Particulars	Debit	Credit	Balance
Oct 19	Sales and GST	549		549 dr

Schedule of Accounts receivable as at 31 October 2024			
J. Parker 514			
L. Malone	736		
L. Ko	805		
S. Adams 444			
V. Adams 549			
Total 3 048			

General ledger

Accounts receivable control account

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			3 030 dr
14	Freight and GST	46		3 076 dr
30	Bad debts and GST		710	2 366 dr
31	Sales and GST	2 582		4 948 dr
31	Sales returns and GST		390	4 558 dr
31	Bank		1 510	3 048 dr

b. It is important to check the Schedule of Accounts receivable against the Accounts receivable control account in the general ledger because, although they are prepared by different people, the balance should be the same for each. If the balance is not the same, it highlights a mistake in posting or an employee making changes to the accounts, which could result in less cash being received by the business.

4. a. Accounts receivable subsidiary ledger

W Alk

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			430 dr
5	Fees received and GST	126		556 dr
10	Bank		430	126 dr
31	Bank		110	16 dr
31	Discount allowed and GST		16	0

T Ramp

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			540 dr
10	Fees received and GST	630		1 170 dr
25	Bank		700	470 dr
25	Discount allowed and GST		40	430 dr
28	Fees received and GST	630		1 060 dr

H Utt

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			120 dr
8	Bank		80	40 dr
12	Fees received and GST	428		468 dr
20	Overdue fees and GST	10		478 dr

T Rees

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			460 dr
31	Bank		120	340 dr
31	Bad debts and GST		340	0

P Ath

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			320 dr
15	Bank		320	0
19	Fees received and GST	149		149 dr
28	Fees received and GST	215		364 dr
28	Bike hire and GST	18		382 dr

Schedule of Accounts receivable as at 31 October 20XX			
T Ramp	1 060		
H Utt	478		
P Ath	382		
Total 1 920			

General ledger

Accounts receivable control account

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			1 870 dr
20	Overdue fees and GST	10		1 880 dr
28	Bike hire and GST	18		1 898 dr
31	Bad debts and GST		340	1 558 dr
31	Bank		120	1 438 dr
31	Fees received and GST	2 178		3 616 dr
31	Bank, discount and GST*		1 696	1 920 dr

^{*} or Bank credit 1 640 Discount allowed and GST 56 cr

b. Striders Tours should keep a subsidiary ledger to hold all its Accounts receivable together in one place making it easy to find the information, assist with customer inquiries, and produce debtor statements. Removing the individual debtors and having the control account in the general ledger is also a good way to reduce clutter in the general ledger. In addition, having one person prepare the control account and one the subsidiary ledger and then ensuring that the balances of the control account and the Schedule of accounts receivable are equal provides a double check on debtors' records.

Activity 16B: Processing transactions (page 215)

1. Accounts receivable subsidiary ledger

A Perry

Date	Particulars	Debit	Credit	Balance
Sept 3	Sales and GST	460		460 dr
9	T Vousden – error		92	368 dr

T Vousden

Date	Particulars	Debit	Credit	Balance
Sept 1	Balance			200 dr
1	Sales and GST	736		936 dr
8	Sales returns and GST		92	844 dr
9	A Perry – error	92		936 dr
22	Bank		200	736 dr
26	Sales and GST	345		1 081 dr
27	Freight and GST	41.40		1 122.40 dr
30	Bank		100	1 022.40 dr

R Parkin

Date	te Particulars		Credit	Balance
Sept 1	Balance			573 dr
3	Sales and GST	828		1 401 dr
4	Discount and GST		23	1 378 dr
18	Bank		550	828 dr
18	Discount allowed and GST		23	805 dr

T Tait

Date	Particulars	Debit	Credit	Balance
Sept 1	Balance			1150 dr
10	Bad debts and GST		1 150	0

B Jones

Date	Particulars	Debit	Credit	Balance
Sept 1	Balance			1 200 dr
30	Overdue fees and GST	18.40		1 218.40

K Seaward

Date	Particulars	Debit	Credit	Balance
Sept 1	Balance			260 dr
3	Bank		230	30 dr
15	Sales and GST	414		444 dr

C Harris

Date	Particulars	Debit	Credit	Balance
Sept 1	Balance			506 dr
30	Bank		460	46 dr
30	Discount allowed and GST		46	0

M Davidson

Date	Particulars	Debit	Credit	Balance
15	Sales and GST	138		138 dr
30	Sales returns and GST		23	115 dr

K Jackson

Date	Particulars	Debit	Credit	Balance
Sept 1	Balance			376 dr

Schedule of Accounts receivable as at 30 September			
A Perry	368.00		
T Vousden	1 022.40		
R Parkin	805.00		
B Jones	1 218.40		
K Seaward	444.00		
M Davidson	115.00		
K Jackson	376.00		
Total	4 348.80		

General ledger

Accounts receivable control account

Date	Particulars	Debit	Credit	Balance
Sept 1	Balance			4 265.00 dr
4	Discount and GST		23.00	4 242.00 dr
9	A Perry – error		92.00	4 150.00 dr
9	T Vousden – error	92.00		4 242.00 dr
10	Bad debts and GST		1 150.00	3 092.00 dr
27	Freight and GST	41.40		3 133.40 dr
30	Sales and GST	2 921.00		6 054.40 dr
30	Sales returns and GST		115.00	5 939.40 dr
30	Bank, discount and GST		1 609.00	4 330.40 dr
30	Overdue fees and GST	18.40		4 348.80 dr

2. Sales journal

Date	Particulars	Accounts receivable	GST	Sales
Nov 2	M Kirby	437	57	380
16	F Gull	230	30	200
	L Whale	276	36	240
23	D Loper	598	78	520
	S Swinter	506	66	440
26	H Halket	414	54	360
28	J Castle	644	84	560
	L Soper	276	36	240
		3 381	441	2 940

Sales returns journal

Date	Particulars	Accounts receivable	GST	Sales returns
Nov 8	M Kirby	92	12	80
29	J Castle	69	9	60
		161	21	140

Cash receipts journal (extract)

Date	Particulars	Discount allowed	Bank	GST	Accounts receivable	Sales
Nov 4	Sales		207	27		180
5	F Gull		184		184	
22	Sales		345	45		300
25	M Kirby		276		276	
28	W Quirter	40	640	(6)	686	
30	D Loper	20	500	(3)	523	
	E Dewer		246		246	
		60	2 398	63	1 915	480

General journal

Date	Particulars	Debit	Credit
Nov 13	Bad debts	200	
	GST	30	
	Accounts receivable – S Kirk		230
27	K McDonald – Accounts receivable	230	
	F Gull – Accounts receivable		230
27	Accounts receivable – H Halket	23	
	GST		3
	Freight received		20
30	Discount allowed	40	
	GST	6	
	Accounts receivable – L Whale		46

3. P Rabbit

Date	Particulars	Debit	Credit	Balance
Feb 1	Balance			460.00 dr
2	Sales and GST	414.00		874.00 dr
13	Sales and GST	644.00		1 518.00 dr
22	Freight and GST	27.60		1 545.60 dr
27	Sales returns and GST		92.00	1 453.60 dr
28	Bank		310	1 143.60 dr
28	Discount allowed and GST		15	1 128.60 dr

H Hare

Date	Particulars	Debit	Credit	Balance
Feb 4	Sales and GST	644.00		644.00 dr

L Lamb

Date	Particulars	Debit	Credit	Balance
Feb 1	Balance			184.00 dr
7	Bank		184.00	0
13	Sales and GST	253.00		253.00 dr
20	Error – P Cat		253.00	0

M Pie

Date	Particulars	Debit	Credit	Balance
Feb 1	Balance			414.00 dr
9	Bad debts and GST		414.00	0

L Lizard

Date	Particulars	Debit	Credit	Balance
Feb 20	Sales and GST	828.00		828.00 dr
25	Sales and GST	690.00		1 518.00 dr
28	Bank		184.00	1 334.00 dr

P Cat

Date	Particulars	Debit	Credit	Balance
Feb 20	L Lamb sales error	253.00		253.00 dr

D Dog

Date	Particulars	Debit	Credit	Balance
Feb 25	Sales and GST	230.00		230.00 dr

B Bunny

Date	Particulars	Debit	Credit	Balance
Feb 1	Balance			265.00 dr
18	Sales and GST	644.00		909.00 dr
20	Sales returns and GST		115.00	794.00 dr
24	Bank		250.00	544.00 dr
24	Discount allowed and GST		15.00	529.00 dr

K Frog

Date	Particulars	Debit	Credit	Balance
Feb 18	Sales and GST	276.00		276.00 dr
28	Discount allowed and GST		23.00	253.00 dr

S Snake

Date	Particulars	Debit	Credit	Balance
Feb 1	Balance			256.00 dr
25	Bank		200.00	56.00 dr

Accounts receivable subsidiary ledger

, ,				
Schedule of Accounts receivable as at 28 February				
P Rabbit	1 128.60			
H Hare	644.00			
L Lizard	1 334.00			
P Cat	253.00			
D Dog	230.00			
B Bunny	529.00			
K Frog	253.00			
S Snake	56.00			
Total	4 427.60			

General Journal

20/2/20xx	Accounts receivable – P Cat	253.00	
	Accounts receivable – L Lamb		253.00
	(Correction of error, sales 13 Feb)		
20/2/20xx	Discount allowed	20.00	
	GST	3.00	
	Accounts receivable – K Frog		23.00
	(Recording K Frog discount)		

4. a. Accounts receivable subsidiary ledger

U Swing

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			2 420 dr
5	Sales and GST	736		3 156 dr
8	Bank		700	2 456 dr
8	Discount allowed and GST		36	2 420 dr
24	Sales and GST	515		2 935 dr
26	Sales returns and GST		230	2 705 dr

E Conomy

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			930 dr
10	Sales and GST	1 380		2 310 dr
18	Interest	93		2 403 dr
31	Bank		1 023	1 380 dr

Н Норе

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			1 130 dr
10	Bank		500	630 dr
12	Sales and GST	138		768 dr
14	Freight and GST	19		787 dr

D Turn

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			1 840 dr
25	Bank		1 700	140 dr
25	Discount allowed and GST		140	0

D Pression

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			1 610 dr
12	Sales returns and GST		160	1 450 dr
15	Bank		1 000	450 dr
19	Sales and GST	549		999 dr

S Nurse

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			340 dr
30	Bad debts and GST		340	0

R Cession

Date	Particulars	Debit	Credit	Balance
Mar 28	Sales and GST	1 230		1 230 dr
31	Bank		1 000	230 dr
31	Discount allowed and GST		100	130 dr

Schedule of Accounts receivable as at 31 March				
U Swing	2 705			
E Conomy	1 380			
Н Норе	787			
D Pression	999			
R Cession	130			
Total	6 001			

7.

8.

General ledger

Accounts receivable control account

Date	Particulars	Debit	Credit	Balance
Mar 1	Balance			8 270 dr
14	Freight GST	19		8 289 dr
18	Interest	93		8 382 dr
30	Bad debts and GST		340	8 042 dr
31	Sales and GST	4 548		12 590 dr
31	Sales returns and GST		390	12 200 dr
31	Bank and discount and GST		6 199	6 001 dr

b. No, because E Conomy had an overdue account, which is why E Conomy was charged interest on 18 March.

Activity 16C: Aged debtors report (page 226)

- Advantage: It encourages debtors to pay their accounts quickly. This, in turn, ensures that the business has sufficient money to meet its own financial obligations.
 - Disadvantage: The discount is an expense which is increasing. This means that profit will be less than it would have been if the debtors repaid the full amount owing, without receiving a discount. It also might mean the business receives less money overall from its sales as credit customers are getting a discount that cash customers might not be receiving.
- 2. The purpose of the aged debtors report is to show the business the length of time individual debtors' accounts have been outstanding (it does NOT show how long it takes them to pay, because they haven't paid yet). Each person's debt is broken down into different time frames so that the business knows how much of the debt is current and how much has been outstanding for a longer period. It can also show if the business has sold beyond the credit limit, which should not happen. It enables the business to 'stop credit' for individual customers until the debts are cleared.
- 3. Trouble Inn's credit policy is not very good because it keeps giving credit to people who have debts outstanding for longer than three months and selling to people over their credit limit as is the case with H Harrison. This means that people can keep buying on credit and they don't have to repay Trouble Inn which is not good for the business's cash flow situation.
- 4. The owners of *Trouble Inn* can offer a discount if the clients repay the entire amount in a week, or can start charging interest on their accounts. Both of these measures would be incentives for Y Ping and S Smithson to pay their accounts quickly. The owners should also make phone calls and send reminder letters to follow up this debt.
- 5. The owners of *Trouble Inn* need to stop credit for H Harrison. This will act as an incentive for him to pay his outstanding debt if he wants to keep shopping at *Trouble Inn*. That may not be enough to collect the outstanding debt, however; so they also need to send reminder letters and perhaps look at getting a debt collector to chase up this debt, because of the value of the debt and the length of time it has been outstanding.
- 6. Yes, the advice was different, because the debt owing by Y Ping and S Smithson is smaller than that owing by H Harrison. Even more important is the fact that their debt is still quite recent. Sending a reminder or giving the customers an incentive to repay the debt should be all that is needed. On the other hand, H Harrison's debt has been outstanding for a lot longer and is a much larger amount, so recovering this debt requires more drastic measures.

a.	Serious Services Aged debtors report as at 30 November 2019							
	Name	Total	Current	1 month	2 month	3 month	4 or more months	
	XYZ Kindy	230	200	30				
	Georgia Harris	450					450	
	Best Meat	420			420			
	Franks Fitness	685				235	450	
	Bright Future	340	340					
	Ready Steady	530	450	80				
	John Jones	920	920					
	Hone Weka	176	120		56			
	Total	3 751	2 030	110	476	235	900	

b. Serious Services has a poor credit policy because it has \$900 (24%) of its Accounts receivable more than four months overdue, which is very poor. In addition, it continues to sell on credit to debtors who have debts that are outstanding (Hone Weka).

			_						
a.	Better Books Aged debtors report as at 30 June 2019								
	Name	Total	Current	1 month	2 month	3-5 month	6 or more months		
	LMNOP Preschool	980	380			600			
	Learning Works	380				380			
	First Steps	530	530						
	High Hope Learning	985	220		765				
	Bright Futures	340					340		
	High Five	1 130		1130					
	Happy Days High School	750	350	400					
	Kia Ora Welcome Preschool	1 138	1 020		118				
	Total	6 233	2 500	1530	883	980	340		

- b. Learning Works and High Five have different credit limits because they have different credit risk ratings based on their income and stability. High Five has a higher credit limit because it is less of a risk and has a high rating from being able to pay back \$2 000 each month if needed, whereas Learning Works has a lower rating and is allowed only a \$400 credit limit. In addition, Learning Works might have had its limit reduced because of the overdue account.
- c. Better Books has a very high age of Accounts receivable (62 days) because it has a large amount of money owed to it by a debtor for more than 3 months (\$1 320) and an additional \$883 over 2 months, contributing to the high age of debtors. It also does not help that Better Books continues to sell on credit when businesses have debts outstanding for more than a month (e.g. Kia Ora Welcome Preschool, LMNOP Preschool).

d. Better Books needs to stop giving credit to debtors with accounts outstanding for more than the previous month. Better Books needs to check this regularly and not keep selling on credit if accounts are unpaid. Better Books should also send out reminder letters and go door knocking to collect the outstanding debts.

9. a. **Tony's Truckstop** Aged debtors report As at 31 March 2020 more months month 3 or mor months Current Fotal Name Big Red 320 320 Tall Timber 410 90 320 290 90 70 130 Jonsee Rubber Duckie 685 175 510 Big Wheels 290 290 530 Smilie 530 Jack Knife 130 130 Total 2655 1030 680 435 510

- b. Tony's Truckstop would have carried out a credit check on Jonsee. The check would have included finding out about his job and income (whether they are reliable and stable, and what sized credit limit he could afford to repay). It would also want to know if Jonsee rents or owns his house, because this gives an indication of 'flight-risk'. It might also have asked for names and numbers of other liabilities Jonsee has, to check up on his credit history with other businesses.
- c. Tony's Truckstop needs to get the money Rubber Duckie owes it because it has been outstanding for more than three months and offering discounts is not appropriate. Tony's Truckstop needs to make phone calls and send reminder letters to encourage payment. If that does not work, it should consider a debt-collection service. In the meantime, it needs to cancel any further credit so Rubber Duckie does not become an even bigger risk.
- d. The total of 'debtors' in the report should be the same total as the closing balance of the Accounts receivable control account in the general ledger and the Schedule of Accounts receivable in the subsidiary ledger.

Activity 17A: Meli's Melting Moments (page 232)

1. a. Accounts receivable subsidiary ledger

HLP Consulting

	•			
Date	Particulars	Debit	Credit	Balance
June 1	Balance			184.00 dr
1	Sales and GST	414.00		598.00 dr
5	Bank		174.80	423.20 dr
5	Discount and GST		9.20	414.00 dr
23	Sales and GST	1 840.00		2 254.00 dr
30 Cleaning fees received and GST		230.00		2 484.00 dr

Your Fitness

Date	Particulars	Debit	Credit	Balance
June 1	Balance			230.00 dr
4	Bank		184.00	46.00 dr
9	Sales and GST			276.00 dr
25	25 Sales and GST			667.00 dr
29	Fitness First – error		230.00	437.00 dr

Mystery Getaways Ltd

Date	Particulars	Debit	Credit	Balance
June 1	Balance			828.00 dr
24	Bank		220.00	608.00 dr
30	Bank		100.00	508.00 dr

Carworld

D	DateParticularsJune 1Balance		Debit	Credit	Balance
Ju					414.00 dr
	26	Overdue fees and GST	41.40		455.40 dr

HealthWorkx

Date Particulars		Debit	Credit	Balance
June 1	Balance			460.00 dr
9	Sales and GST	207.00		667.00 dr

Realty 4U

Date	Particulars	Debit	Credit	Balance
June 1	Balance			460.00 dr
17	Sales and GST	207.00		667.00 dr
30	Bank		460.00	207.00 dr

Jackson HR

Date Particulars		Debit	Credit	Balance
June 1 Balance				276.00 dr
11	Bad debts and GST		276.00	0

Fitness First

Date	Particulars	Debit	Credit	Balance
June 29	Your Fitness – error	230.00		230.00 dr

Schedule of Accounts receivable for Meli's Melting Moments as at 30 June 20XX					
HLP Consulting	2 484.00				
Your Fitness	437.00				
Mystery Getaways Ltd	508.00				
Carworld	455.40				
HealthWorkx	667.00				
Realty 4U	207.00				
Fitness First	230.00				
Total	\$ 4 988.40				

b.

Meli's Melting Moments Aged debtors report as at 30 June							
Name	Total	Current	1 month	2 months	3 months	4 months	
HLP Consulting	2 484.00	2 484.00					
Your Fitness	437.00	391.00	46.00				
Mystery Getaways Ltd	508.00		508.00				
Carworld	455.40	41.40				414.00	
Health Workx	667.00	207.00		368.00	92.00		
Realty 4U	207.00	207.00					
Fitness First	230.00	230.00					
Total	4 988.40	3 560.40	554.00	368.00	92.00	414.00	

- c. One main advantage of keeping an Accounts receivable subsidiary ledger is that it keeps all the individual debtors accounts together, which makes it very easy to access and from it answer any enquiries debtors might have. It also means that the general ledger will be less cluttered and there will be just the one control account, which acts as a check against the Schedule of accounts receivable. This will highlight any errors in debtors' records. Meli's Melting Moments uses the subsidiary ledger to keep the accounts together, and it also facilitates the preparation of the Aged debtors report.
- d. There does not appear to be a stop-credit policy for Meli's Melting Moments, or not until an account is more than three months overdue. This is evidenced by the fact that HealthWorkx was given credit despite having an overdue payment from two months prior to the start of June. It appears that overdue fees are charged only when the account has been unpaid for more than three months, which does not provide a big incentive to pay earlier. On the whole, the stop-credit policy is not effective, because several accounts are overdue but the customers can still buy on credit. In addition to this, bad debts are written off, which decreases the profit of Meli's business.

Meli's Melting Invoice 162 Date June 23 20XX **Moments** 27 High St, Auckland **GST Number:** 11-889-425 Sold to: HLP Consulting 98 North Rd, Auckland Address **Unit Price** Total Description 1 600.00 1 600.00 Café booked for private function catering Subtotal 1 600.00 CST 240.00 **GST** 1 840 00 Inclusive Authorised by: Meli Please pay by the 20th of next month

b. The invoice is signed by Meli, which proves the credit transaction was authorised and approved by Meli. This prevents other employees issuing credit. It also means that if there are any issues with the invoice, Meli knows she approved it herself. It is important to

- approve each credit transaction to try to reduce the risk of bad debts. The invoice has an invoice number, which in this case is #162. Having invoices pre-numbered is a good control because it makes invoices easy to trace and to identify if any are missing. If there is an invoice missing, it could indicate a transaction that has not been recorded and therefore a decrease in potential cash flow and profit. It is important to have accurate records of each transaction and the invoice helps achieve this goal. Ensuring that the invoice has the debtor's name and address makes it easy to follow up payment and send reminder statements if needed. The invoice is used to accurately prepare the sales journal and update debtors' records.
- c. Before offering credit to a new personal customer, Meli needs to do a thorough credit check and then set a small credit limit. She needs to research the potential debtor's income, job, ownership or rental of home, how long the person has been in the job and house, and so on, to establish 'flight-risk' and ability to repay the debt. Once the customer has been allowed credit, Meli needs to become stricter on repayment and enforce a one-month policy, charging interest as soon as the account is overdue. This will help reduce the risk of bad debts and help increase profit. The credit situation should be checked every time a credit transaction takes place so any debtor with an overdue account is not allowed more credit.
- d. (Examples, but not limited to)
 - The debtor's name and contact details, so the debtor can check that the account is theirs and that they are not being charged for someone else's transactions. This is also important for Meli, to make sure she has sufficient details to follow up late accounts.
 - The amount owed is very important, so Meli knows how much the debtor owes her and so the debtor knows how much they owe and the date by which they have to pay. The statement might also state how much is current and how much is overdue, warning the debtor of any future penalties and of what they need to pay urgently.
 - A description of the transaction or source document references is needed so the customer can check the accuracy of the transaction on their account for the month and so that they can agree that the transactions are theirs. For example, HLP Consulting will be able to check that the payment it made was deducted and the current charges are for the private function, other sales, and as a cleaning fee. The amounts should match the amounts on the original documents.

Activity 17B: Petra's Petstore (page 237)

1. Accounts receivable subsidiary ledger

Monique Mouse

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			430.00 dr
5	Bank		110.00	320.00 dr
6	Lucy Lizard – sales and GST – error		110.00	210.00 dr
17	Sales and GST	276.00		486.00 dr

Suzie Stalk

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			720.00 dr
1	Sale and GST	414.00		1 134.00 dr
11	Sales returns and GST		80.50	1 053.50 dr
17	Sales and GST	207.00		1 260.50 dr
19	Bank		684.00	576.50 dr
19	Discount allowed and GST		36.00	540.50 dr

Barry Bear

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			490.00 dr
4	Sales and GST	230.00		720.00 dr
17	Bank		100.00	620.00 dr
29	Sales returns and GST		46.00	574.00 dr

Lucy Lizard

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			530.00 dr
6	Monique Mouse – sales error	110.00		640.00 dr

Caylee Cat

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			575.00 dr
4	Sales and GST	828.00		1 403.00 dr
19	Bank		200.00	1 203.00 dr

Darryl Dog

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			290.00 dr
25	Bank		290.00	0

George Guinea

Date	Particulars	Debit	Credit	Balance
Oct 1	Balance			330.00 dr
26	Bad Debts and GST		330.00	0

Katie Kitten

Date	Particulars	Debit	Credit	Balance
Oct 25	Sales and GST	391.00		391.00 dr
22	Cartage and GST	23.00		414.00 dr
30	Sales returns and GST		23.00	391.00 dr

Schedule of Accounts receivable for Petra's Petstore as at 31 October 20XX				
Monique Mouse	486.00			
Suzie Stalk	540.50			
Barry Bear	574.00			
Lucy Lizard	640.00			
Caylee Cat	1 203.00			
Katie Kitten	391.00			
Total	\$ 3 834.50			

2.	Petra's Petstore Aged debtors report As at 31 October					
	Name	Total	Current	1 month	2 months	3 or more months
	Monique Mouse	486.00	276.00	210.00		
	Suzie Stalk	540.50	540.50			
	Barry Bear	574.00	184.00	290.00		100.00
	Lucy Lizard	640.00	110.00		530.00	
	Caylee Cat	1 203.00	828.00		175.00	200.00
	Katie Kitten	391.00	391.00			
	Total	3 834.50	2 329.50	500.00	705.00	300.00

Note: Sales returns are usually credited to the current month's sales, although different businesses have differing policies on this.

- 3. a. It is important to carry out a credit check before allowing a customer to buy on credit in order to assess their credit risk, and to set a realistic limit, because if Petra's Petstore sells on credit to a bad risk the business will not receive its money, which worsens cash flow and decreases profit by the writing off of bad debts. Common information includes income/payslip to assess the credit limit that can be given. Whether or not the customer's job is full time or part time and what the work is, affects the security of job and income, and has an influence on credit risk. A higher income and a full-time secure job provide less risk than does part-time work. Petra will also consider the housing situation – if someone owns their house and has lived in the town for a long time, they are less likely to leave town without paying their debts than is someone who rents. Petra should also try to find out about past credit history from previous creditors to find out if the customer is a good payer. Currently Petra either doesn't do a very good credit check or is quite lenient about the customers she gives credit to, because she has a large number of debts owed to her, and several outstanding for more than one month.
 - b. After preparing the Schedule of Accounts receivable and the Accounts receivable control account in the general ledger, Petra can check to see if the balances are the same. By ensuring that they agree, and by having different employees prepare each account, errors can be found. The accounts will also highlight any discrepancies that might have arisen.
 - c. It is important to authorise credit transactions because there can be large amounts of money tied up in Accounts receivable and Petra wants to make sure she will receive the money. Currently Petra has \$3 834.50 debtors, which is a lot, and if she has to write many off as bad debts, it will reduce her profit. Petra's current procedure is not very effective. Despite authorising the transaction, she does not check how much the debtor already has outstanding. In October, Petra sold to three debtors who already had accounts outstanding for more than two months, which is not good practice. She needs to 'stop credit' on those accounts and not allow more credit until the accounts are paid.
 - d. Keeping a Debtors subsidiary ledger for Petra's Petstore allows Petra to keep all the individual debtors together, which makes it very easy to access and from it answer any enquiries debtors might have. It also means that the general ledger will be less cluttered and just have the one control account, which acts as a check against the Schedule of Accounts receivable. This will highlight any errors in debtors' records. Petra's Petstore uses the subsidiary ledger to keep the accounts together, and it also facilitates the preparation of the Aged debtors report, and of the monthly statements.

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Activity 17C: Mickey's Mechanics (page 243)

1. Accounts receivable subsidiary ledger

Hone Harrison

Date	Particulars	Debit	Credit	Balance
April 1	Balance			460.00 dr
5	Bank		420.00	40 dr
5	Discount allowed and GST		40	0
17	Sales and GST	414.00		414.00 dr

Ted Thompson

Date	Particulars	Debit	Credit	Balance
April 1	Balance			1 380.00 dr
1	Sales and GST	460.00		1 840.00 dr
4	Sales returns and GST		41.40	1 798.60 dr
19	Bank		1 352.40	446.20 dr
19	Discount allowed and GST		27.60	418.60 dr
30	Sales and GST	460.00		878.60 dr

Ashleigh Miles

Date	Particulars	Debit	Credit	Balance
April 1	Balance			644.00 dr
8	Sales and GST	138.00		782.00 dr
17	Bank		138.00	644.00 dr
20	Error – Tayla Nguyen		138.00	506.00 dr

Kaitlin O'Connor

Date	Particulars	Debit	Credit	Balance
April 1	Balance			920.00 dr
12	Bad debts and GST		920.00	0

Terry Monk

Date	Particulars	Debit	Credit	Balance
April 1	Balance			414.00 dr
2	Sales and GST	230.00		644.00 dr
5	Sales returns and GST		18.40	625.60 dr
19	Bank		200.00	425.60 dr

Rebecca Hay

Date	Particulars	Debit	Credit	Balance
April 1	Balance			1 840.00 dr
14	Sales and GST	276.00		2 116.00 dr
15	Overdue fees and GST	46.00		2 162.00 dr
25	Bank		340.00	1 822.00 dr

Nellie Avia

Date	Particulars	Debit	Credit	Balance
April 1	Balance			230.00 dr

Tayla Nguyen

Date	Particulars	Debit	Credit	Balance
April 20	A Miles – error	138.00		138.00 dr
23	Sales and GST	621.00		759.00 dr
26	Sales returns and GST		23.00	736.00 dr

Schedule of Accounts receivable for Mickeys' Mechanics as at 30 April 20XX				
Hone Harrison	414.00			
Ted Thompson	878.60			
Ashleigh Miles	506.00			
Terry Monk	425.60			
Rebecca Hay	1 822.00			
Nellie Avia	230.00			
Tayla Nguyen	736.00			
Total	5 012.22			

2. General Journal

3.

20/4/20xx	Accounts receivable T Nguyen	138.00	
	Accounts receivable – A Miles		138.00
	(Correction of error, sales 8 April)		
5/4/20xx	Discount allowed	34.78	
	GST	5.22	
	Accounts receivable – H Harrison		40.00

(Recording H Harrison)

Mickey's Mechanics Aged debtors report as at 30 April						
Name	Total	Current	1 month	2 months	3 or more months	
Hone Harison	414.00	414.00				
Ted Thompson	878.60	878.60				
Ashleigh Miles	506.00		506.00			
Terry Monk	425.60	211.60			214.00	
Rebecca Hay	1 822.00	322.00	690.00	810.00		
Nellie Avia	230.00		230.00			
Tayla Nguren	736.00	736.00				
	5 012.20	2 562.20	1 426.00	810.00	214.00	

4. (Examples of possible answers.)

- a. Credit limits are the maximum amount of credit a debtor should have at any time. These should be different depending on the potential credit risk. *Mickey's Mechanics* has different limits; for example, Ted Thompson is deemed low risk with a \$1 500 limit while Terry Monk is a higher risk with only a \$600 limit. However, *Mickey's Mechanics* is not sticking to these limits, so there is a risk of the business incurring further bad debts, and this also indicates poor management of debtors at point of sale.
- b. It appears that Mickey's Mechanics does not check the credit limit at the time of sale, because Rebecca Hay and Kaitlin O'Connor have both been allowed to go over their limit on the opening balances, and R Hay continues to be sold to during this month. They therefore might not be able to pay the money owing. This was shown to be the case K O'Connor was declared a bad debt and because she was allowed to buy over her limit profit fell by more than it should have, which is not good. At points of sale the mechanic should check both the credit limit and how long debts have been outstanding before giving credit.

- c. Documentation is important to give proof of transactions. Mickey's Mechanics uses invoices at the time of the job, providing proof of who did the job and how much is owed. The invoice is followed up with a statement, and any returns are documented on a credit note. This is good, because it allows Mickey to check any enquiries; an example being when Ashleigh Miles complained that she had been wrongly charged on 20 April.
- d. Bad debts are an expense that lessens Mickey's Mechanics' profit. This month K O'Connor's money owing was written off as a bad debt totalling \$920 including GST; therefore \$800 was deducted from profit, \$104.35 more than would have been deducted if the business had stuck to the credit limit.
- e. Making errors is bad for customer relations. Ashleigh Miles would not be happy to be charged for someone else's job. In addition, errors can mean you sell over the limit to the correct person, in this case Tayla Nyugen. Because T Nyugen did not have the \$138 on her statement she did not pay it – and it would take at least an extra month to receive the money from her, making it more difficult for Mickey's Mechanics to pay its own expenses and suppliers.
- f. It is not very effective. Only H Harrison and T Thompson paid in time for a discount, so the incentive is not very effective. The other five did not pay in time for the discount and had outstanding amounts from a month or more.

Activity 17D: Tony's Toy Warehouse (page 247)

1. Accounts receivable subsidiary ledger

ABC Books

Date	Particulars	Debit	Credit	Balance
July 1	Balance			644.00 dr
2	Sales and GST	437.00		1 081.00 dr

Abacus Toys

Date	Particulars	Debit	Credit	Balance
July 1	Balance			460.00 dr
20	Sales and GST	276.00		736.00 dr
23	A to Z Learning – error		276.00	460.00 dr
29	Sales returns and GST		69.00	391.00 dr
30	Bank		230.00	161.00 dr

A to Z Learning

Date	Particulars	Debit	Credit	Balance
July 1	Balance			575.00 dr
5	Bank		115.00	460.00 dr
23	Abacus Toys – error	276.00		736.00 dr

Angela's Toys

Date	Particulars	Debit	Credit	Balance
July 1	Balance			420.00 dr
31	Bad debts and GST		420.00	0

Action Fun

Date	Particulars	Debit	Credit	Balance
July 1	July 1 Balance			713.00 dr
6	Bank		677.35	35.65 dr
	Discount and GST		35.65	0
8	Sales returns and GST		69.00	69.00 cr
16	Sales and GST	414.00		345.00 dr
30	Discount and GST		23.00	322.00 dr

Awesome Action Learning

Date	Particulars	Debit	Credit	Balance
July 1	Balance			368.00 dr
10	Bank		230.00	138.00 dr
21	Sales and GST	414.00		552.00 dr
24	Cartage and GST	18.40		570.40 dr

Absolute Toys and Games

Date	Particulars	Debit	Credit	Balance
July 1	Balance			276.00 dr

ACDC Toys

Date	Particulars	Debit	Credit	Balance
July 16 Sales and GST		644.00		644.00 dr
28	Sales and GST	644.00		1 288.00 dr

Schedule of Accounts receivable for Tony's Toy Warehouse as at 31 July 20XX				
ABC Books	1 081.00			
Abacus Toys	161.00			
A to Z Learning	736.00			
Action Fun	322.00			
Awesome Action Learning	570.40			
Absolute Toys and Games	276.00			
ACDC Toys	1 288.00			
Total	4 434.40			

2.	6/7/20xx	Discount allowed	31.00	
		GST	4.65	
		Accounts receivable – Action Fun		35.65
		(Recording Action Fun discount)		

23/7/20xx	Accounts receivable – A to Z Learning	276.00	
	Accounts receivable – Abacus Toys		276.00
	(Correction of error, sales 8 April)		
30/7/20xx	Discount allowed	20.00	
	GST	3.00	
	Accounts receivable – Action Fun		23.00
	(Recording Action Fun discount)		

31/7/20xx	Bad debts	365.22	
	GST	54.78	
	Accounts receivable – Angela's Toys		420.00
	(Recording H Harrison)		

3.

	Tony's Toy Warehouse Aged debtors report as at 31 July						
Name	Total	Current	1 month	2 months	3 or more months	4 or more months	
ABC Books	1 081.00	437.00	460.00		184.00		
Abacus Toys	161.00			161.00			
A to Z Learning	736.00	276.00	460.00				
Action Fun	322.00	322.00					
Awesome Action Learning	570.40	432.40	138.00				
Absolute Toys and Games	276.00		230.00	46.00			
ACDC Toys	1 288.00	1 288.00					
	4 434.40	2 755.40	1 288.00	207.00	184.00	0	

4. (Examples include, but not limited to)

- a. One reason Tony has difficulty with overdue accounts while still selling to the debtors on credit is that the existing system allows this to happen. The employee checks only whether the transaction and current balance are under the credit limit, not how long the account has been outstanding. This means the sale goes ahead even if the outstanding amount is several months old. For example, in April, ABC Books was allowed to purchase \$437 despite having \$184 that was three months overdue. One 'easy fix' is to stop credit whenever the account is more than one month overdue. The computer system could provide an alert, or the employee would need to bring up the full account or check the last month's Aged debtors report before authorising credit, which should prevent at-risk debtors from getting further in debt. This will prevent bad debts increasing and help reduce them in total, which will have a positive effect on profit. Although this might decrease sales as some customers will not purchase, that is better than selling inventory and never receiving the cash from the sales, which would reduce profit by more in the long run.
- b. A credit limit is the maximum amount of credit an individual debtor is allowed to have in total at a point in time. The limit will vary depending on the 'risk' of each person/business, which is based on their income, stability and assessed ability to repay. A credit limit is important, because without one, debtors could run up huge bills in the first month and then never pay with no ability to make them pay. By having a limit, the risk is lower. Action Fun, which has a high limit, is obviously deemed a good risk and this is confirmed by its having no outstanding accounts at the start of April. In contrast, Angela's Toys had a smaller limit of \$600, which was prudent, because that business was written off as a bad debt in April.
- c. Tony carries out a credit check, which is a useful procedure. It includes checking a potential debtor's income and job, to help assess the likelihood of the debtor paying the debts and to help work out a credit limit. In addition, Tony rings previous creditors of the potential debtors, which is a good thing to do. He can ask these businesses about the customer's current reputation, if they owe money, how quickly they repay and so on. Doing this research should minimise the risk of bad debts, although it is not a guarantee against having bad debts. Currently, Tony's policy seems to be working reasonably well, because at the end of April there were no debts owed for more

- than four months, and only \$184 over three months (and that debtor has endeavoured to repay some money during the month) reducing the risk. This indicates that Tony sells to businesses that do try to pay their debts
- d. i. Tony's Toy Warehouse staff members sign the packing slip when they package the goods as a way of authorising the credit sale and therefore being accountable for the transaction if that sale should not have proceeded. This is a good internal control, as the staff member is responsible and identifiable, and therefore is more inclined to check credit limits before sales are processed.
 - ii. The packing slip should be pre-numbered, which helps track the documents and identify if any go missing. The number aids in filing, but more importantly if any are missing it could indicate staff fraud and/or inappropriate sales. The packing slip also lists all the items being sold, which helps ensure the invoice is accurate and thus the journal, ledgers, and debtors' accounts should be accurate. This will help ensure that *Tony's Toy Warehouse* receives all the money it should from its sales, which will help cash flow and profit. It will also mean the Income Statement and Statement of Financial Position are accurate.
- e. Keeping an Accounts receivable subsidiary ledger for *Tony's Toy Warehouse* allows Tony to keep all the individual debtors' accounts together, which makes it very easy to access and from it answer any enquiries debtors might have. It also means that the general ledger is less cluttered and there will be just the one control account, which acts as a check against the Schedule of accounts receivable. This will highlight any errors in debtors' records. In this case, the accounts manager is responsible for updating debtors' accounts and preparing their statements. She should not be responsible for preparing the journals, or any of the debtors' ledgers. The subsidiary ledger should be prepared by an accounts clerk, and another person should prepare the control account. This separation of duties ensures that the accounts manager cannot change the debtors' accounts to cover up any dishonesty by her or other staff.

Activity 17E: Formative assessment – *Art Supplies* (page 252)

Part A

a. Artzworkz

4	AI LEWOI NE	II (EVI OI RE					
	Date	Particulars	Debit	Credit	Balance		
	July 1	Balance			2 500 dr		
	8	Sales and GST	630		3 130 dr		
	17	Sales and GST	460		3 590 dr		
		Delivery and GST	27		3 617 dr		
	20	Sales returns and GST		92	3 525 dr		
	28	Overdue fees and GST	42		3 567 dr		

Canvas World

Date	Particulars	Debit	Credit	Balance
July 1	Balance			1 438 dr
13	Bank		538	900 dr
24	Sales and GST	900		1 800 dr

Learning Solutions

Date	Particulars	Debit	Credit	Balance
July 1	Balance			1 980 dr
4	Bank		900	1 080 dr
8	Error – Memories 4 Ever		180	900 dr
12	Sales and GST	810		1 710 dr
14	Sales returns and GST		50	1 660 dr

Make and Mould

Date	Particulars	Debit	Credit	Balance
July 1	Balance			1 166 dr
22	Sales and GST	320		1 486 dr
23	Administration and GST	23		1 509 dr
30	Bank		850	659 dr

Memories 4 Ever

Date	Particulars	Debit	Credit	Balance
July 1	Balance			3 800 dr
8	Error – Learning Solutions	180		3 980 dr
21	Sales and GST	276		4 256 dr

Photos Forever

Date Particulars		Debit	Credit	Balance
July 1	Balance			920 dr
28	Bad debts and GST		920	0

Scrapbooking Creations

Date	Particulars	Debit	Credit	Balance
July 1	Balance			780 dr
6	Discount and GST		32	748 dr
10	Bank		741	7 dr
	Discount allowed and GST		39	32 cr
11	Sales and GST	540		508 dr

Schedule of Accounts receivable as at 31 July				
Artzworkz	3 567			
Canvas World	1 800			
Learning Solutions	1 660			
Make and Mould	659			
Memories 4 Ever	4 256			
Scrapbooking Creations	508			
	·			
Total	12 450			

b. General Journal

6/7/2018	Discount allowed	27.83	
	GST	4.17	
	Accounts receivable – Scrapbooking Creations		32.00
	(Recording Action Fun discount)		

Accounts receivable – Learning	2	180.00	Accounts receivable – Memories 4 Ever	8/7/2018	
Solutions 180.	180.00]		
(Correction of error, 28 June)			(Correction of error, 28 June)		

10/7/2018	Discount allowed	33.91	
	GST	5.09	
	Accounts receivable – Scrapbooking Creations		39.00
	(Recording Action Fun discount)		

c. Age of Accounts Receivable Report, 31 July 2018

Debtor	Credit limit	Balance	July 0-30 days	June 31-60 days	May 61–90 days	April 90+ days	Mar 120+ days
Artzworkz	3 400	3 567	1 067	240	1840		420
Canvas World	1 800	1 800	900	460	440		
Learning Solutions	3 500	1 660	760		900		
Make and Mould	1 600	659	343	316	0	0	
Memories 4 Ever	6 000	4 256	276	980	1 600	1 400	
Scrapbooking Creations	1 500	508	508				
Total		12 450	3 854	1 996	4 780	1 400	420

Part B

No answer supplied, as this is a formative assessment. Your teacher will discuss in class or mark. Check that you have written about credit checking originally and at point of sale, linking to evidence, bad debts, separation of duties, documentation, incentives, authorisation, accuracy of records, and so on. Link these ideas to the resource and your answers. Make sure you discuss the impact on Art Supplies in relation to cash flow, profit, and customer satisfaction. Discuss initial credit checking and consider that these are businesses, not people.

Activity 18A: Calculations (page 256)

	2019		2020		
Analysis measure	Working	Answer	Working	Answer	
Mark-up %	(392 000 ÷ 408 000) × 100	96.1%	(446 500 ÷ 503 500) × 100	88.7%	
Gross profit %	(392 000 ÷ 800 000) × 100	49%	(446 500 ÷ 950 000) × 100	47%	
Profit %	(128 000 ÷ 800 000) × 100	16%	(133 000 ÷ 950 000) × 100	14%	
Distribution costs %	(144 000 ÷ 800 000) × 100	18%	(190 000 ÷ 950 000) × 100	20%	
Finance cost %	(40 000 ÷ 800 000) × 100	5%	(38 000 ÷ 950 000) × 100	4%	
Percentage change in sales	(800 000 – 720 000) 720 000 × 100	11.1%	(950 000 – 800 000) × 100 800 000	18.8%	
Percentage change in profit for the year	(128 000 – 130 000) 130 000 × 100	-1.5%	(<u>133 000 – 128 000)</u> × 100	3.9%	
Return on equity	128 000 × 100 (170 000 + 370 000) ÷ 2	47.4%	133 000 × 100 (370 000 + 473 000) ÷ 2	31.6%	
Return on total assets	(128 000 + 40 000) × 100 (450 000 + 537 500) ÷ 2	34.0%	(133 000 + 38 000) × 100 (537 500 + 647 000) ÷ 2	28.9%	
Current ratio	21 000 ÷ 10 500	2:1	27 000 ÷ 45 000	0.60:1	
Liquid ratio	<u>21 000 – 12 000</u> 10 500 – 0	0.86:1	<u>27 000 – (19 250 + 750)</u> 45 000 – 37 000	0.88:1	
Equity ratio	370 000 ÷ 537 500	0.69:1	473 000 ÷ 647 000	0.73:1	
Age of Accounts receivable	(2 300 + 4 500) ÷ 2 0.3 × 800 000 × 1.15 × 365	4.5 days = 5 days	$\frac{(4500+7000)\div2}{0.3\times950000\times1.15}\times365$	6.4 days = 7 days	
Inventory turnover	408 000 (10 000 + 12 000) ÷ 2	37.1 times	503 500 (12 000 + 19 250) ÷ 2	32.2 times	

Activity 18B: Profitability (page 261)

- 1. a. Mark-up percentage in 2019 was 60%; and in 2020 it is 67%.
 - i. This means that in 2020 the business increased the cost price of its inventory by 67% of the cost price to get its selling price, which is a greater increase than in the previous year. For example, if a good cost \$100 to buy, the business will sell it for \$167.
 - ii. This is a good trend, providing the increase does not scare customers away due to too high pricing. If customers continue to buy, the business is making more profit for each item sold than it did in the previous year.
 - iii. One reason for this trend is that the business has deliberately increased the selling price of its inventory, which has caused an increase in the mark-up percentage. Another reason could be that the business has sourced cheaper inventory and kept the selling price the same, which would also cause an increase in the mark-up on inventory sold.
 - iv. If the increase in mark-up percentage is deemed too high, the best way to fix the problem is to lower the selling price. This reduces the profit margin on each item sold and therefore decreases the mark-up percentage.
 - b. Gross profit percentage in 2019 was 45%, and in 2020 it was 40%.
 - i. This means that in 2020 the business has generated a gross profit of 40 cents in every dollar of sales. This means that 40% of sales is left in the business to cover the operating expenses and make a profit.

- ii. This is a poor trend because there is a smaller percentage of sales left in the business to cover its operating expenses than there was last year.
- iii. An increase in the cost of purchasing the inventory while keeping the selling price the same could be responsible for the trend. Alternatively, deliberately reducing the selling price to attract more customers and increase the market share could be the cause. These would increase sales and increase gross profit.
- iv. To improve this percentage, the business must increase its markup percentage either by finding a cheaper inventory supplier while keeping the selling price the same, or by increasing the selling price of the inventory, which would increase the gross profit and gross profit percentage.
- c. Administration costs percentage in 2019 was 18%, and in 2020 it is 22%
 - This means that in 2020 the business spent 22% of its sales (or 22 cents in every dollar of sales) on administration expenses, such as electricity used in the office, and rates.
 - ii. This is a poor trend because the business has spent a larger proportion of sales on administration expenses than it did last year, indicating poor management of expenses in the past year.
 - iii. One possible reason for this trend is that the business has had to spend more on office electricity due to the increase in electricity prices over the past year, which increased administrative expenses and their percentage.
 - iv. To improve this percentage the business needs to reduce its spending on administration expenses. For example, it could find a cheaper insurance supplier, or switch from printing and posting monthly invoices to emailing them, thus reducing the administration expenses which in turn will decrease (improve) the administration expenses percentage.
- d. Finance cost percentage in 2019 was 6%, and in 2020 it is 4%.
 - This means that in 2020 the business has spent 4% of its sales on interest (finance costs), which is an improvement on the same figure from last year.
 - This is a good trend because it leaves a greater amount in the business as profit.
 - iii. One reason for this trend could be that the business repaid large amounts of loans or its mortgage which would reduce the amount of interest that had to be paid this year. Alternatively, the interest rates at the bank may have fallen, which has resulted in less interest being paid, which reduced finance cost percentage.
- Distribution cost percentage in 2019 was 22%, and in 2020 it is 25%.
 - i. This means that in 2020 the business spent 25 cents for every dollar of sales on distribution expenses, such as petrol and advertising, which was a greater percentage than was spent on distribution in 2019
 - This is a poor trend because a smaller percentage of sales remains as profit in the business.
 - iii. One reason for this trend is that the business increased its spending on items such as advertising/petrol/wages, which resulted in increased distribution expenses. (Perhaps the business opened another store.)
 - iv. This trend can be improved by cutting back on some of the distribution expenses, for example by reducing the number of deliveries the business makes, or changing from colour to blackand-white advertising, which is less expensive. This will reduce the distribution costs and in turn improve the distribution cost percentage.
- f. Profit percentage in 2019 was 12%, and in 2020 it is 16%.
 - i. This means that in 2020 the business has 16% of sales left in the business as profit after accounting for all expenses. This is higher than the same figure for last year, which is pleasing.

- ii. This is a good trend because a greater percentage of sales remains in the business as profit.
- iii. One possible reason for this trend is that the business might have increased its mark-up percentage, resulting in an increase in profit margin and profit for the year. Alternatively, the business might have found ways to better manage its expenses, and this has resulted in a fall in expense percentages and an increase in the profit percentage.
- g. Percentage change in profit in 2019 was 8%, and in 2020 it is 12%.
 - This means that in 2020 the profit increased by 12% over the profit from 2019.
 - This is a good trend because the business has generated more profit in dollars than it did last year.
 - iii. One reason for this trend is that the business might have increased its mark-up percentage, and this has resulted in an increase in profit margin and profit. Alternatively, the business might have found ways to manage its expenses better, resulting in a fall in expense percentages and an increase in the net profit percentage.
- h. Percentage change in sales in 2019 was 25%, and in 2020 it is 23%.
 - This means that in 2020 the business increased the sales it made last year by 23%.
 - ii. This is a good trend as the business has generated nearly a quarter more sales dollars than it did in the previous year. This trend means that the business should also make a greater profit.
 - iii. One reason for this trend might be that the business increased its mark-up percentage, resulting in an increase in sales dollars, OR it might have decreased its selling price to attract more customers and therefore increase sales. Alternatively, the business might have increased its advertising, attracting more customers and increasing the number of sales made.
- a. Best Meat spent 11% of its sales on administration expenses, such as rent. This is an improvement in the figure over that of last year.
 - b. The business made sure not to increase its administration expenses very much (\$63 000 in 2020 compared with \$66 000 in 2021). Because sales increased by so much (43%), the administration expenses percentage decreased. Although the business might have cut back on some expenses, such as stationery, overall there was an increase in administration expenses.
 - c. In 2021, 7% of sales remained as profit in *Best Meat*, after all expenses were accounted for. This figure was down from that of the previous year.
 - d. The main reason for this trend is the increase in Cost of goods sold expenses, indicating that inventory is more expensive to buy and that the business hasn't increased its selling prices to account for this. This has resulted in a smaller gross profit and therefore smaller profit for the year. There was also a large increase in distribution costs, which led to a decrease in profit for the year.
 - e. 2020: Cost of goods sold = 60%, then gross profit must = 40%.
 2021: Cost of goods sold = 65%, then gross profit must = 35%.
 - f. This means that 35% of every sales dollar remains in *Best Meat* as gross profit, after accounting for cost of goods sold. This is to cover the business's operating expenses and, it is hoped, to make a profit.
 - g. Best Meat should try to decrease its distribution costs by, for example, using less shop electricity. It could also change from advertising on the radio, which is really expensive, to advertising in the newspaper providing that this change will not have detrimental effects on customer numbers. This will decrease distribution costs and the distribution cost percentage.
 - h. This means that Best Meat has generated a return of 4% on the money and other assets that Baxter has invested into the business. This figure is quite low, and currently he would be better off investing his money in the bank at 5% interest, which is less risky.

- No, because this figure is quite low, and currently Baxter would be better off investing his money in the bank (at 5% interest).
- j. Best Meat should try to increase its profit for the year. The business could do this by increasing the mark-up percentage, or by decreasing expenses (for example, using less stationery or electricity) which would increase the profit. This would, in turn, lead to an increase in the return on equity percentage.

Activity 18C: Liquidity (page 269)

- 1. a. Current ratio in 2020 was 2.46:1; and in 2021 it is 1.89:1.
 - i. This means that in 2021 the business has \$1.89 of current assets to repay every \$1 of current liabilities. This is a good result, as it means that it should be able to repay its short-term debts in the normal course of business as they fall due in the next accounting period.
 - ii. Although the result is good, the trend is poor, since the amount of current assets to repay every \$1 of current liabilities has fallen. Therefore the business has less ability to repay these short-term debts than it did last year.
 - iii. One possible reason for the trend could be a large decrease in the cash at bank, caused by the purchasing of new equipment, or the repayment of a loan. Alternatively, the owner might have taken a large amount of cash drawings this year. The decrease in bank decreased current assets and the current ratio.
 - iv. If the owner ever needs to improve this ratio, he/she should invest more money in the business. This means that the cash at bank will increase, which increases the current assets and therefore increases the current ratio. Alternatively, the business could borrow money in the form of a long-term loan (however, this option would worsen the equity ratio – usually this is not ideal)
 - b. Liquid ratio in 2020 was 0.96:1 and in 2021 it is 1.25:1.
 - i. This means that in 2021 the business has \$1.25 of liquid assets to repay every \$1 of liquid liabilities. This is a good result as it should be able to repay its immediate debts in the normal course of business, as they fall due.
 - ii. This is a good trend, as the amount of liquid assets to repay every \$1 of liquid liabilities has increased. Therefore the business now has the ability to repay its immediate debts as they fall due.
 - iii. One possible reason for the trend is that the business might have repaid some of its Accounts payable. This would have been possible if the business got a loan, or the owner invested more money in the business. This would have decreased liquid liabilities and the liquid ratio. Alternatively, the Accounts receivable or bank account might have increased greatly due to increased sales, which increased current assets and liquid ratio.
 - iv. If the owner ever needs to improve this ratio, he/she should invest more money in the business. This means that the cash at bank will increase, which will increase the liquid assets and therefore also the liquid ratio. Alternatively, the business could borrow money as a long-term loan (but this would worsen the equity ratio, which is usually not ideal).
- The business might have high inventory, as this would help contribute to high current assets and therefore a high current ratio, but the inventory is excluded from the liquid assets meaning the value of liquid assets is very low.
- The business might have high Accounts receivable and/or a high bank account, meaning that both its current and its liquid assets are high enough for it comfortably to be able to cover the current liabilities.
- 4. This could be because of a high secured bank overdraft. This increases the current liabilities which causes the low current ratio. However, it is excluded from the liquid ratio, thus ensuring that the liquid assets are comfortably able to cover the low liquid liabilities.

- The business must have reasonably high current and liquid liabilities, such as an unsecured bank overdraft and Accounts payable, and possibly low current and liquid assets, such as bank and inventory.
- 6. 1. The business might have to borrow money from the bank to ensure that it has enough money to repay its creditors and expenses as they fall due. This will result in increased interest payments in the future.
 - If the business is unable to meet its liquid debts it will develop a poor credit rating and the Accounts payable might stop giving the business credit. This would mean that it might not be able to buy enough inventory to sell and therefore struggle to keep making a profit.

Activity 18D: Financial stability (page 271)

- 1. a. Equity ratio in 2020 was 0.62:1, and in 2021 it is 0.75:1.
 - i. This means that in 2021 the owner has financed (funded/invested) 75 cents for every \$1 of total assets (or 75% of total assets) in the business. The business is financially stable, since the owner has contributed well over half the assets, and there is room to borrow if necessary.
 - ii. This is a good trend.
 - iii. One reason for this trend is that the owner might have contributed more cash or assets into the business during 2021, or alternatively the business might have repaid a large amount of its non-current liabilities.
 - iv. The owner should always invest money into the business to improve this ratio (providing he or she wants to keep the business). By increasing his or her cash investment in the business, the owner is increasing the assets and the capital – which increases proportion of assets the owner has funded. Alternatively, if possible, the owner should repay liabilities such as loans. To do this, however, the owner will often have to contribute the money first. (The owner could also try to increase profit, but this would not be as reliable a method as contributing money.)
 - b. Equity ratio in 2020 was 0.62:1 and in 2021 it is 0.48:1.
 - This means that in 2021 the owner has financed (funded/ invested) 48 cents for every \$1 of total assets in the business.
 This means the business is financially unstable as the owner has funded far less than half of the business's assets.
 - ii. This is a poor trend because the figure has decreased since the previous year and is now below half of total equity.
 - iii. One reason for this trend is that the owner might have taken out large amounts of drawings this year, thus reducing the proportion of assets his or her capital has funded. Alternatively, the business might have purchased large property, plant and equipment assets and funded this by borrowing more money from the bank – for example, by increasing its loan or mortgage.
 - iv. The owner should always invest money in the business to improve this ratio (providing he or she wants to keep the business). By increasing their cash investment in the business, the owner is increasing the assets and the capital, which increases the proportion of assets the owner has funded. Alternatively, if possible, the owner should repay liabilities such as loans. To do this, however, the owner will often have to contribute the money first.
- The business must be paying a large amount of interest because of the large proportion of assets being funded by liabilities, which in turn will reduce the business's profit.
 - The business will be unable to borrow more money if it needs to. It will have to repay the debts each year, which will put strain on its cash flow

Activity 18E: Management effectiveness (page 274)

- a. Age of Accounts receivable in 2020 was 42 days, and in 2021 it is 36 days.
 - In 2021 it took the Accounts receivable, on average, 36 days to repay their debts, which is an improvement on the situation in 2020.
 - This is a good trend as the business is receiving its money faster from Accounts receivable.
 - iii. The business might have tightened its credit policy by reducing the amount of credit people are allowed. Alternatively, it might have sent reminder letters and started to charge interest on overdue accounts which has resulted in debtors paying more quickly.
 - iv. The business could offer discounts for early payment which should encourage debtors to pay their accounts faster. Alternatively, it could charge penalty interest on overdue accounts.
 - b. Inventory turnover in 2020 was 5 times, and in 2021 it is 3.5 times.
 - This means that in 2021 the inventory on hand was sold, on average, 3.5 times, which is a deterioration from last year.
 - This is a poor trend, because inventory is being sold more slowly this year than it sold last year.
 - iii. One reason for this is that the business might have increased the mark-up percentage too much, by increasing the selling price and making it too expensive for customers to buy its inventory. Alternatively, it might have purchased a lot more inventory this year because it wasn't carrying enough last year. This would mean that the business has more inventory which makes it logical that inventory turnover will take longer.
 - iv. Decrease the selling price by having a sale to clear the excess stock – especially that which is at risk of becoming obsolete. This will decrease the stock on hand and therefore increase the turnover. It is important also to check the purchasing policies to ensure the business is buying the stock that customers want, and not too much of it
- The business is not receiving the money its debtors owe it, therefore it might not have enough money itself to repay its Accounts payable and other monthly expenses, resulting in a poor credit reputation or incurring late fees.
 - The business will face having to write Accounts receivable off as bad and doubtful debts. This will reduce profit.
- 3. This means that the business is not making as many sales as it should be. It could indicate that it has large amounts of obsolete stock or is carrying far too much stock which could lead to obsolescence in the future if not currently. It might indicate that its inventory is too expensive and that for this reason the business is missing out on sales and therefore profit.
- 4. This indicates that the business is either selling its goods too cheaply or, alternatively, that it is missing out on sales because it is not carrying enough stock. Both of these situations would have a negative impact on the business's prospective profit.

Activity 18F: Linkages (page 276)

- a. Equity ratio the equity ratio should increase/improve because there
 will be an increase in capital, which increases equity and equity ratio.
 - b. Current ratio the current ratio will improve/increase because the loan will cause an increase in Sarah's Sofas' bank account, which will increase current assets and the current ratio.
 - c. Liquid ratio the liquid ratio will improve/increase because the loan will cause an increase in Sarah's Sofas' bank account, which will increase the liquid assets and the liquid ratio.

- a. Current ratio the current ratio will now decrease back to what it was before the cash investment, because the money in the bank will decrease, which decreases current assets and the current ratio.
 - b. Finance cost percentage the finance cost percentage should improve, because repaying the loan should decrease the amount of interest being paid by Sarah's Sofas. This will decrease the finance cost and the finance cost percentage.
 - c. Equity ratio this will improve the equity ratio further because the repayment of the loan decreases liabilities, which increases the proportion of total assets funded by the owner, which increases the equity ratio.
- a. Age of Accounts receivable the loosening of the credit policy is likely to lead to an increase in credit sales and possibly debtors taking longer to pay their debts. This will increase the age of Accounts receivable, which is a poor trend.
 - b. Liquid ratio the liquid ratio is likely to increase/improve because the Accounts receivable balance will be higher, which increases the liquid assets and the liquid ratio.
 - c. Bank balance / liquidity this is likely to worsen because, although the Accounts receivable are not paying as quickly as previously, Sarah's Sofas still has to pay its expenses and other debts so its bank balance will decrease.
- a. Mark-up percentage mark-up percentage will increase, because the increase in selling price will increase the difference between sale and cost price of inventory.
 - b. Gross profit percentage due to the increase in selling price, and therefore increase in mark-up percentage, the profit margin has increased, which leads to an increase in gross profit, which increases gross profit percentage.
 - c. Percentage change in sales the percentage change in sales should increase, because Sarah's Sofas does not need to sell as many sofas to get the same sales dollars as last year. However if the price increase scares off many customers, it might fall.
 - d. Inventory turnover generally an increase in selling price will lead to a decrease in the number sofas being sold, which will decrease/worsen the inventory turnover. Because the sofas are more expensive, fewer are sold.
 - e. Current ratio this is likely to cause an increase in inventory since fewer sofas are sold, which will lead to an increase in current assets and the current ratio. Alternatively, for each sofa sold, the Accounts receivable or bank is increasing by more than it would have last year, which also increases current assets and the current ratio.

b.

Activity 19: Analysis and interpretation (page 279)

1. a.		2019	2020	
	Analysis measure	Answer	Working	Answer
	Mark-up %	114.3%	(319 500 ÷ 360 500) × 100	88.6%
	Gross profit %	53.3%	(319 500 ÷ 680 000) × 100	47.0%
	Profit for year %	18.3%	(52 000 ÷ 680 000) × 100	7.6%
	Distribution costs %	20%	(155 000 ÷ 680 000) × 100	22.8%
	Finance cost %	3.3%	(37 000 ÷ 680 000) × 100	5.4%
	Percentage change in sales	7.1%	((680 000 – 600 000) ÷ 600 000) × 100	13.3%
	Percentage change in profit for the year	22.2%	((52 000 – 110 000) ÷ 110 000) × 100	-52.7%
	Return on equity	20.3%	(52 000 ÷ ((583 800 + 691 000) ÷ 2)) × 100	8.2%
	Return on total assets	19.7%	((52 000 + 37 000) ÷ ((722 800 + 896 000) ÷ 2)) × 100	11.0%
	Current ratio	2.73:1	56 000 ÷ 25 000	2.24:1
	Liquid ratio	0.40:1	(56 000 – 49 000) ÷ 25 000	0.28:1
	Equity ratio	0.81:1	691 000 ÷ 896 000	0.77:1
	Age of Accounts receivable	6.48 days = 7 days	((1 000 + 3 300) ÷ 2) / (0.1 x 680 000 x 1.15) × 365	10.04 days = 11 days
	Inventory turnover	8.75 times	360 500 ÷ ((28 000 + 49 000) ÷ 2)	9.36 times

Analysis measure	Meaning of the 2020 results	Trend
Mark-up %	In 2020, <i>Music Magic</i> increased the cost price of its inventory by 88.6% to calculate the selling price.	This was a poor trend because the decrease in price contributed to the decrease in gross and net profit. The reason for the trend was lowering the selling prices and having to pay increased costs for purchasing the inventory. The increases weren't passed on to the customers. This decreased the profit margin on each item sold.
Gross profit %	In 2020, <i>Music Magic</i> had 47% of its sales left in the business as gross profit to cover its operating expenses and generate a profit.	This is a poor trend because the business has generated a smaller gross profit percentage than it did last year. The main reason for this trend is the decrease in mark-up percentage which is probably caused by decreased selling prices as the inventory turnover increased.
Profit for year %	In 2020, <i>Music Magic</i> had 7.6 cents in every dollar of sales to keep in the business after accounting for all expenses.	This is a poor trend as the actual profit and profit as a percentage of sales have decreased. The main reason for this trend is the large increase in expenses, which is likely to have been caused by opening the five new stores, thus generating a lot of one-off set-up costs, and increased wages.
Distribution costs %	In 2020, <i>Music Magic</i> used 22.8% of sales on distribution expenses.	This is a poor trend because the expenses have increased and are using up a greater percentage of sales than they did last year. The main reason for this trend is opening the new shops. This would require increased staff wages to be paid as well as a large increase in advertising. These expenses would increase the distribution costs greatly.
Finance cost %	In 2020, <i>Music Magic</i> used 5.4% of sales in interest expenses.	This is a poor trend because the increase in finance costs as a percentage of sales contributes to the decrease in net profit percentage. The main reason for the trend is the increase in interest due to having to borrow more money to finance the opening of the five new shops. Non-current liabilities increased by \$53 000 which explains the increase in finance costs.
Percentage change in sales	In 2020, <i>Music Magic</i> generated 13.3% more sales than it did in 2019.	This is a good trend as the business has generated more sales to cover the operating expenses and make a profit. The reason for this trend is the opening of the new shops which attracted more customers and generated more sales. The decrease in mark-up would have also contributed to the trend as the cheaper prices encouraged the customers to buy more.
Percentage change in profit for the year	In 2020, <i>Music Magic</i> generated 52.7% less profit than it did last year.	This is a poor trend because the business should be trying to increase its profit. The main reason for the decrease is the larger increase in expenses, especially distribution and finance costs. This is to be expected as a result of opening the five new shops, increased borrowing and the increase in rent or rates, shop electricity and advertising.
Return on equity	In 2020, <i>Music Magic</i> generated a 8.2% return on the funds invested by Sam.	This is a poor trend because <i>Music Magic</i> has generated a smaller return on equity this year than it did last year. The reason for this is the decrease in profit caused by the increase in expenses, such as set-up costs. The capital that Sam invested during the year has also increased the equity and therefore reduced the return.

Return on total assets	In 2020, Music Magic generated an 11% return on total assets, which means it isn't using the asset as effectively as it did last year.	This is a poor trend because last year there was a 19.7% return which means the business is using its assets less effectively now. The reason for this is the purchase of a lot more assets to open the five new shops. Because they haven't been open for a whole year, they haven't had the opportunity to generate profit to their full capacity yet.	
Current ratio In 2020, Music Magic had \$2.24 of current assets to repay every \$1 of current liability. This means that Music Magic should be able to repay its short-term debts as they fall due.		This is a poor trend as the ability to repay short-term debts has fallen. However, it is still at a safe level. The reason for this trend is the large increase in current liabilities, especially Accounts payable, which has more than doubled. This would have possibly been a result of purchasing some equipment for the new shops on short-term credit.	
Liquid ratio	In 2020, Music Magic had 28 cents of liquid assets to repay every \$1 of liquid liability. This means that Music Magic will struggle to repay its immediate debts as they fall due.	This is a very poor trend as the ability to repay immediate debts has fallen and is now at a critical level. The reason for this trend is the large increase in liquid liabilities, especially Accounts payable, which has more than doubled. This would have been to help fund the inventory for the new shops. Also, the increase in interest payments and increased drawings would have contributed to the decrease in Bank.	
Equity ratio	In 2020, Sam has financed 77% of the total assets in <i>Music Magic</i> .	This is a good trend as the business is relying less on Sam and has increased its debt financing, thus making it possible to expand its stores, while maintaining a safe level of equity. The reason for this trend is the large increase in non-current liabilities to finance the new property, plant and equipment needed to set up the five new shops. This is despite the increase in capital by Sam during the year.	
Age of Accounts receivable	In 2020, it took <i>Music Magic</i> on average 11 days to receive money from its credit sales / Accounts receivable.	oney However, it is at such a good level in real terms that there is no reason to worry about it.	
Inventory turnover	In 2020, <i>Music Magic</i> sold its inventory on hand on average 9.4 times a year.	This is a good trend because it is selling the inventory more quickly than it did last year, meaning there is less chance of obsolete stock in the future. The main reason for this trend is the decrease in mark-up percentage which means the stock was cheaper so more people bought more music.	

- c. i. Gross profit percentage. Increase the selling price of the inventory to generate a higher mark-up percentage and therefore a higher gross profit margin on each item of inventory sold, which increases the gross profit percentage.
 - ii. Administration expenses percentage. Decrease the administration expenses by finding a cheaper electricity supplier and ensuring that lights and computers are switched off each night. This will reduce the office expenses and in turn the administration expense percentage.
 - iii. Current ratio. Sam should invest more money into Music Magic as this will increase the bank account which is a current asset. This will therefore improve the current ratio. This money could be used to repay Accounts payable which would decrease the current liabilities and therefore improve the current ratio even further.
 - iv. Equity ratio. Sam should invest more money into *Music Magic* as this will increase the capital, and then the equity as a percentage of total assets will also increase.
 - v. Inventory turnover. Sam needs to ensure that *Music Magic* carries the right amount of inventory, and inventory that the customers want to buy. This will avoid the problem of obsolete stock. In addition, the selling price can be decreased to attract more customers, but it is to be hoped that this measure will not be needed. By carrying less stock and stock people want to buy, the business can help improve its turnover. *Music Magic* also needs to reduce the stock on hand, if possible, in order to make it easier to sell the equivalent of the inventory on hand.

a	2021	2022		
Analysis measure	Answer	Working	Answer	
Profit %	31.7%	(42 500 ÷ 150 000) × 100	28.3%	
Gardening costs %	58.3%	(95 000 ÷ 150 000) × 100	63.3%	
Administration expenses %	6.7%	(9 500 ÷ 150 000) × 100	6.3%	
Finance cost %	3.3%	(3 000 ÷ 150 000) × 100	2%	
Return on equity	231.7%	(42 500 ÷ ((25 700 + 22 800) ÷ 2)) × 100	175.3%	
Return on total assets	94.6%	(42 500 + 3 000) ÷ ((54 800 + 50 200) ÷ 2) × 100	86.7%	
Current ratio	2.40:1	5 200 ÷ 2500	2.08:1	
Liquid ratio	2.40:1	(5 200 – 750) ÷ 2 500	1.78:1	
Equity ratio	0.42:1	25 700 ÷ 50 200	0.51:1	
Age of Accounts receivable	7.5 days = 8 days	((1 300 + 1 600) ÷ 2 ÷ (0.6 × 150 000 × 1.15) × 365	5.1 days = 6 days	

2.

Analysis measure	Meaning of the 2022 result	Trend
Profit for the year %	In 2022, GreenFingers Garden Services had 28.3 cents in every \$1 of fees revenue to keep in the business after accounting for all expenses.	This is a poor trend as the profit as a percentage of fees revenue has decreased The main reason for this trend is the large increase in expenses, especially gardening expenses – possibly due to the increase in petrol prices over the past year. The increase in expenses was proportionately greater that the increase in revenue, which led to a decrease in profit percentage.
Gardening costs %	In 2022, <i>GreenFingers Garden Services</i> used 63.3% of fees revenue on gardening expenses.	This is a poor trend because the gardening expenses have increased and are using up a greater percentage of fees revenue than they did last year. The main reason for this is likely to be the increase in petrol prices, and possibly more travelling that needs to be done for new customers, as fees received has increased a lot.
Administration expenses %	In 2022, GreenFingers Garden Services used 6.3% of fees revenue in administration expenses.	This is a good trend because the decrease in administration expenses as a percentage on fees revenue can contribute to an increase in profit. The main reason for the trend is that the increase in fees revenue is greater than the increase in administration expenses. Despite the increase in fees revenue, Garry has managed his administration expenses well.
Finance cost %	In 2022, <i>GreenFingers Garden Services</i> used 2% of fees revenue in interest expenses.	This is a good trend because the decrease in finance costs as a percentage of fees revenue contributes to an increase in net profit. The main reason for the trend is the decrease in interest needing to be paid because the business repaid a lot of its liabilities (for example, \$8 000 off non-current loans), which decreased finance costs.
Return on equity	In 2022, GreenFingers Garden Services generated a 175.3% return on the funds invested by Garry.	This is a poor trend because <i>GreenFingers Garden Services</i> has generated a smaller return on equity this year than it did last year. The reason for this is the increase in average equity this year, which has made it difficult to improve the return, despite the increase in profit. Nevertheless, this is a very high return on equity.
Return on total assets	In 2022, GreenFingers Garden Services generated an 86.7% return on total assets.	This is a poor trend because last year it had a 94.6% return which means the business is using its assets less efficiently now. One reason for this is the very small average total assets from 2020 to 2021, so it is expected to fall. It is still, however, a very good result.
Current ratio	In 2022, GreenFingers Garden Services had \$2.08 of current assets to repay every \$1 of current liabilities. This means that GreenFingers Garden Services should be able to repay its short-term debts as they fall due.	This is a poor trend as the ability to repay short-term debts has fallen – but it is still at a safe level. The reason for this trend is the increase in current liabilities, especially Account payable, and the decrease in the bank account caused by the large amount of drawings, and the repayment of a loan of \$8 000. This caused an increase in current liabilities and a decrease in current assets, which decreased the current ratio.
Liquid ratio	In 2022, GreenFingers Garden Services had \$1.78 of liquid assets to repay every \$1 of liquid liabilities. This means that GreenFingers Garden Services should be able to repay its immediate debts as they fall due.	This is a poor trend as the ability to repay immediate debts has fallen but it is still at a satisfactory level. The reason for this trend is the increase in current liabilities, especially Accounts payable, and the decrease in bank – caused by repaying some of the loan, which increased liquid liabilities and decreased liquid assets, overall resulting in a decrease in liquid ratio.
Equity ratio	In 2022 Garry has financed 51% of the total assets of <i>GreenFingers Garden Services</i> .	This is a good trend as the business has improved the proportion of the assets funded by Garry. This has been caused by the decrease in assets, as well as by the repayment of \$8 000 off the loan. This is still at a low level because Garry continues to take out large amounts of drawings (\$39 600).
Age of Accounts receivable	In 2022 it took <i>GreenFingers Garden Services</i> on average 6 days to receive its money from its credit sales.	This is a good trend because it is taking the business less time to receive mone from its debtors than it did last year. This is especially pleasing because there has been an increase in the Accounts receivable balance. The reason for the improvement is that the increase in debtors' balance is a smaller percentage than the increase in credit fees, indicating a tighter credit policy. Possibly the business is offering a discount for payment received within seven days.

- c. i. Net profit percentage. Increase the fees to generate more revenue by charging more for the services, or decrease administration expenses by reducing stationery expenses and using more email. Both of these will increase the profit for the year, and in turn the net profit percentage.
 - ii. Gardening cost percentage. For this business this will be difficult. If possible, find a cheaper petrol supplier or try to find mowers that are more economical to run. Perhaps advertise less or on less expensive paper to decrease the gardening expenses and in turn improve the gardening costs percentage.
 - iii. Return on equity percentage. This can be improved by increasing the profit for the year by either generating more fees or decreasing expenses. This will then increase the profit in relation to the equity in the business.
 - iv. Liquid ratio. This can be improved by increasing the cash at bank to increase the liquid assets and therefore improve the liquid ratio. This could be done if Garry invested more money in the business. (Note: NOT get a bank loan, since the equity ratio is not good enough to obtain a loan.)
 - v. Age of Accounts receivable. This can be improved by tightening the credit policy, offering discounts to encourage people to pay quickly, or charging interest on overdue accounts. These measures will encourage people to pay quickly, and in turn this will improve the age of Accounts receivable. However, this is not really an issue for this business so it is likely that it has some of these measures in place already.
- 3. a. A poor age of Accounts receivable can have a positive effect on the liquid ratio because it will have resulted in a high amount of Accounts receivable. As this is a liquid asset, it will help contribute to a good liquid ratio, as the liquid assets are greater than they would have been.
 - b. Because the liquid ratio is high, Kerry's Kingdom believes it can meet its immediate debts easily. However, since it is taking the debtors more than 6 weeks (2 months / 8 weeks) to pay, the business will not have received the money it is relying on in time to pay its liquid liabilities, therefore it might not be able to meet its immediate debts on time.
 - c. If Kerry's Kingdom does not improve its age of Accounts receivable, the business might not be able to meet its own debts and therefore incur interest penalties, get a bad credit rating, and might no longer be able to buy on credit. If the credit policy is really bad, then the business might also have to write off many bad debts which will decrease its profit.
 - d. Kerry's Kingdom needs to offer incentives to get debtors to pay their accounts faster. This should improve the Age of Accounts receivable in the long run. In the short term, it needs to make sure that it sends reminder letters to the holders of overdue accounts and makes phone calls to start getting back that money. It could also consider stopping credit so customers with overdue accounts can't buy on credit without repaying the existing debt first. The business should also look at the criteria it has for giving credit and should make it harder for people to get credit. All of these measures should encourage debtors to pay their accounts faster, which will decrease (that is, improve) the age of Accounts receivable.
- 4. a. The slow inventory turnover indicates that high amounts of inventory are being kept in the shop. This increases the value of current assets which contributes to the good current ratio. The stock remains on the shelf for longer, therefore building up the current assets value, and the current ratio.
 - b. The current ratio indicates that Kerry's Kingdom should be able to repay its short-term debts easily. However, to do this it is relying on the inventory to be sold, but as the poor inventory turnover indicates, this is not happening as quickly as it should – therefore the business has a falsely positive view of its current ability to repay

- short-term debts. If *Kerry's Kingdom* does not receive the money from inventory sold, it cannot pay its own current liabilities.
- c. If the turnover does not improve, Kerry's Kingdom might be left with a lot of money tied up in inventory. It might have to have a discount sale to clear stock, which will result in a smaller profit margin. It could also get left with a lot of stock that is obsolete and can't be sold, and needs to be written off. This will decrease the gross profit and profit for the year, both of which will have a negative impact on the business's performance. The cash flow will be insufficient to pay Accounts payable on time, as stock is being sold, thus causing the business to incur late payment fees.
- d. The business could have a discount sale to clear stock. This will mean more stock is sold, as customers will buy more when it is cheaper. Kerry's Kingdom also needs to stop buying as much stock and, if possible, have optimum stock level and reorder points to prevent overstocking in the future. These measures, when combined, will decrease inventory on hand and thus improve inventory turnover.
- 5. It appears that Kerry's Kingdom lowered its selling prices or had many discounts sales to clear its stock. This would contribute to the lower mark-up percentage since a smaller profit margin was used, and would improve the inventory turnover because more items of stock were being sold in general, people will buy more if goods are cheaper. This illustrates the link between the mark-up percentage and inventory turnover: the lower the mark-up percentage, the higher the inventory turnover.
- 6. a. Equity ratio: This would improve (increase) the equity ratio because the equity has increased as a percentage of the total assets through the increase in capital, especially as the money was used to repay some of the mortgage, as liabilities also decreased.
 - b. Finance cost percentage: This would improve (decrease) the finance cost percentage as the interest expense should fall – due to a smaller mortgage. This would require less interest to be paid, decreasing finance costs.
 - c. Liquid ratio: This would improve the liquid ratio, as some of the money is being used to repay the mortgage, and the rest is being used to increase the bank account, therefore liquid assets are increasing, which in turn increases the liquid ratio.
 - d. Profit percentage: This should improve the profit percentage because the decrease in interest expenses should result in an increase in the profit for the year, consequently increasing the profit percentage.
 - e. Return on equity percentage: The equity percentage could increase or decrease. In the current year it is likely to decrease because of the large increase in equity that the profit has to be spread over. It is unlikely that the decrease in interest costs will be greater than the \$45 000 invested by the owner.
- a. Equity ratio: The equity ratio would decrease (worsen) because there is less capital in the business, and the liabilities will now have funded a greater proportion of the business assets than the owner has funded
 - b. Return on total assets: This transaction is likely to improve the return on total assets, as the net profit is unaffected and the total assets will have decreased due to Richie taking money out of the business for his personal use, thus decreasing the bank account.
 - c. Current ratio: This transaction is likely to decrease or worsen the current ratio. Because money has been withdrawn from the business, there is less cash at bank, therefore fewer current assets to share over the current liabilities. This lowers the current ratio.
 - d. Return on equity percentage: This transaction is likely to improve the return on equity percentage. Because Richie has withdrawn a large amount of equity, the average equity will have fallen. This means that the profit for the year doesn't have to be shared over as much equity – which will improve this result. The equity ratio will be falling and the business might not be able to borrow money if it

- /4
- 8. Although this increase is a pleasing result, the reason that it occurred is not pleasing. It occurred because of large drawings. If Richie continues to take drawings, the equity ratio will fall and the business will be less stable. In addition, there will be an increase in interest payments if the business has to borrow to meet repayments and to be able to fund the owner's high level of drawings.
- 9. This high ratio indicates that the business might not be investing its funds wisely. It might have too large a percentage of its funds tied up in the cheque account when the funds could be placed more beneficially in a term investment or could be invested in more equipment. Alternatively, the ratio could be the result of a high debtors' figure which, unless the debtors are paying their accounts quickly, is not a good thing. It could be caused by too high an inventory balance which could lead to obsolete stock that has to be written off. (However, it is unlikely that there is inventory in this context.) Richie needs to determine what is contributing to the high current ratio and consider investing the business's funds more effectively.
- 10. a.

Analysis measure	Industry average	HairSprayArt	Result
Mark-up %	100%	90%	worse
Gross profit %	50%	47%	worse
Net profit %	8%	10%	better
Distribution costs %	9%	12%	worse
Finance cost %	3%	5%	worse
Administration expenses %	30%	20%	better
Return on equity %	18%	16%	worse
Return on total assets %	13%	14%	better
Current ratio	2.1:1	2.6:1	better
Liquid ratio	1.35:1	1.10:1	worse
Equity ratio	0.65:1	0.85:1	better
Age of Accounts receivable	32 days	28 days	better
Inventory turnover	7 times	5.2 times	worse

- b. HairSprayArt calculates selling price by adding 90% of the cost price to the cost price of its inventory. For example, if an item cost \$10, the business would sell it for \$19. This mark-up percentage is less than the industry average which means that the business might not be making as much profit on each item sold as it could be it might deliberately be undercutting its competition to try to sell more.
- c. HairSprayArt is selling its products at cheaper prices than the competition, and so it has a lower mark-up percentage. One reason it might want to do this is to increase sales volume and perhaps increase market share in order to try to eliminate competition. Another reason could be that it is a smaller business and therefore it costs the business more to buy its inventory, so it needs to have a lower mark-up percentage to still be able to sell the products at similar prices to those charged by the competition.
- d. The reason that HairSprayArt has a lower gross profit percentage is that its mark-up is lower than the industry average. However, HairSprayArt also has a lower expenses percentage, especially the administration expense percentage which is 10% of sales lower than the average. This means it has better control over its administration expenses than the industry average. By having a lower expense percentage of sales, the business has compensated for the slightly lower gross profit percentage, resulting in a higher profit for the year, and giving it a better-than-average net profit percentage.
- e. HairSprayArt might be a small business in comparison with other businesses in the industry. This means it can't take advantage of bulk buying and has to have a smaller mark-up percentage because of the higher cost of its purchases. A consequence of having to buy a lot of stock which isn't selling very well is that the business would

- also have a low turnover. Alternatively, the business might have purchased a lot of stock that people don't want to buy. This high inventory results in a low inventory turnover.
- f. HairSprayArt has a very good credit policy which enables it to check thoroughly whether potential debtors will be able to pay their accounts. This will allow the business to receive payment more quickly, especially if it has good incentives in place – for example, it might offer prompt-payment discounts or charge interest on overdue accounts. HairSprayArt might not have as big a proportion of its sales on credit as the industry average which would also help improve the age of debtors.
- g. On the whole, HairSprayArt's liquidity is not as good as the industry average, because its liquid ratio is worse, despite the current ratio being better. The current ratio shows that HairSprayArt has \$2.60 of current assets to repay every \$1 of current liabilities, which leaves it in a more comfortable position than the industry average at \$2.10 to repay its short-term debts. However, the liquid ratio of \$1.10 liquid assets to every \$1 liquid liability shows that HairSprayArt should be able to repay its immediate debts, but not as comfortably as others in the industry. This measure is the more important of the two, because it reflects the business's ability to repay liquid debts as they fall due in the next 4-6 weeks.
- 11. a. i. This means that, in order to calculate the selling price of his inventory, Marcus increases the cost price of his inventory by 100% (that is, he doubles the cost price). For example, if Marcus buys an item for \$100, he will sell it for \$200. This mark-up percentage is a smaller one than was used last year.
 - ii. The decision to reduce the mark-up percentage was successful because the sales dollars increased by \$200 000 (and increased profit), meaning that more people were prepared to buy the inventory at lower prices – sufficient to cover the decrease in mark-up.
 - b. i. This means that, in 2023, Sparkz Electrical had 7.5% (or 7.5 cents) in every dollar of sales remaining in the business as profit after accounting for all expenses. This is a decrease from last year.
 - ii. By changing its telephone and internet provider, Sparkz Electrical is trying to reduce its administration expenses. By reducing these expenses, the business will generate a greater profit for the year, which in turn will improve the net profit percentage.
 - c. The main reason for this decrease is the large increase in total assets (\$280 000), mainly due to the \$250 000 refurbishment which was finished during the year, and which has increased the average assets. These assets have not yet had time to start generating profit for a whole year, so hopefully this percentage will improve again next year. OR: Sparkz Electrical might have had to shut the shop for the duration of the refurbishments, which would have decreased its profit potential in the short term.
- 12. a. i. Mighty Cycles' current ratio can be used to assess the business's ability to repay its short-term debts. Samantha is relying on the business's Accounts receivable to enable it to do this. Because the Age of Accounts receivable is 58 days (nearly two months), Samantha might have problems paying her Accounts payable and expenses in the coming month because the business hasn't received the money from its debtors in time for her to pay her debts as they fall due.

ii. One of:

- The business could take out a long-term loan and use this money to repay the Accounts payable (current debts). This would decrease current liabilities, which would help improve the business's current ratio.
- Samantha should invest more money in the business. This
 money will increase the cash on hand that can then be used
 to repay the current debts, because the cash at bank has
 increased.

- Samantha could offer discounts to her Accounts receivable to encourage them to pay their debts faster. This will increase the cash flow in the business and can be used to repay the current debts
- b. i. This means that Samantha has funded 65% (or 65 cents in every dollar) of the business's total assets. This means that the business is financially stable as she has funded over half the business assets, which is more than the liabilities, and she can borrow to expand the business in the future if she wants to.
 - ii. Samantha repaid some of the loan and mortgage. To do this, she cashed in some of the business's investments. This repayment decreased the amount of liabilities, which in turn increased the proportion of the business assets that have been funded by Samantha, therefore increasing the equity ratio.
 Samantha repaid some of the loan and in doing so she invested more money in the business. This decreased the amount of liabilities, which in turn increased the proportion of the business assets that have been funded by Samantha, therefore increasing the equity ratio. Because she has increased her capital investment, this has also increased the equity which has led to the improvement in the equity ratio.
- 13. a. i. One way to reduce Comfy Couches' closing inventory is to have a discount sale. This should encourage more people to buy furniture, consequently increasing the inventory turnover and the closing inventory balance (providing Dileepa doesn't replace all the inventory he sells).

A second way to increase sales in order to reduce the closing balance of inventory is to have a big advertising campaign. More advertising will ensure that more people know about the shop and this should encourage more people to visit the shop, and to buy more furniture, thus reducing the amount of inventory on hand.

ii. Example:

One consequence if the inventory turnover does not improve is that the inventory might become very dated and unpopular, and could end up being obsolete. This will cause a decrease in profit if the stock has to be written off.

Another possible consequence is that the business might have trouble repaying its current debts (Accounts payable) because the inventory is not selling fast enough and there is not enough cash coming into the business. This will result in bad credit rating and loss of suppliers.

b. i./ii.lt is important that Dileepa changes his ordering policies. He can do this by reducing the reorder point at which more stock must be reordered, and by reducing the reorder quantities. This will ensure that the business is not carrying too much stock, and as a result the inventory turnover should improve. Even if the stock isn't selling, there won't be as much on hand, therefore reducing the inventory turnover risk.

OR:

It is important that Dileepa has stock that people want. He needs to make sure that he doesn't have much stock on hand so that he can replace sold stock with the latest fashions that people will want to buy. This will reduce the amount of stock on hand and increase the chances of selling what stock there is. This will, in turn, improve the inventory turnover.

- 14. a. The business has loosened its credit policy, allowing more people to buy on credit and for greater amounts. This has resulted in more inventory being sold, which has increased the inventory turnover. The business might have changed its inventory mix to sell stock that was more in demand, in order to increase sales and inventory turnover.
 - i. As the Accounts receivable are taking longer to repay their debts, the business is not receiving the money fast enough for Tim to

be able to repay the Accounts payable and expenses as they fall due. He has needed to extend his overdraft to make sure that his debts are paid on time.

ii. Example:

- Handy Haven could offer discounts to its debtors if they pay
 their accounts early (for example, within two weeks) this
 would mean that more people, wanting to receive the
 discount, will pay earlier and this will reduce the age of
 Accounts receivable.
- Handy Haven could send out reminder letters and make phone calls to all those who are overdue in paying their accounts. This should make some pay faster and improve the age of debtors.
- Handy Haven should stop giving credit to all debtors who
 have overdue accounts. This will make them pay up if
 they want to buy more. The business then needs to ensure
 that debtors pay on time, by charging interest on overdue
 accounts in the future. Because the debtors will want more
 credit and not want to pay extra, they should pay faster, thus
 improving Handy Haven's age of Accounts receivable.
- 15. The financial expenses percentage for 2020 tells Extreme Sports that 8% (or 8 cents in every dollar) of sales is taken up by paying interest expenses (finance costs). This is higher than the industry average (double, in fact) and is therefore a concern.

It is important that *Extreme Sports* improve this percentage because it is a lot worse than the industry average. This means that *Extreme Sports* is spending a bigger proportion of money from sales on interest than other sports shops spend. A consequence is that a smaller proportion is left in the business as profit. To increase the profit in the future the business's financial expenses percentage needs to be reduced.

To achieve a reduction in the finance cost percentage, the business needs to pay off some of its term liabilities (by the owner investing more cash). Doing so will ensure that less interest will have to be paid, therefore the company will have less finance costs and a smaller finance cost percentage. Another way to reduce the interest expenses (and therefore the finance cost percentage) is by restructuring and finding a bank that will charge a lower interest rate.

Activity 20: Modified NCEA examination questions (page 292)

1.	Analysis measure	Working	Answer (for 2023)
	Distribution costs %	(60 000 ÷ 600 000) × 100	10%
	Profit for the year %	(GP – Exp) (120 000 ÷ 600 000) × 100	20%
	Current ratio	(215 000 ÷ 250 000)	0.86:1
	Equity ratio	(400 000 ÷ 800 000)	0.50:1
	Age of Accounts receivable	$(30\ 000 + 40\ 000) \div 2 \times 365$ (500\ 000 \times 1.15)	22.2 = 23 days
	Inventory turnover	400 000 ÷ (145 000 + 175 000) ÷ 2	2.5 times

2. Part A: Analysing Cleaning Supplies' liquidity

- a. i. This tells Sara that Cleaning Supplies has 60 cents of liquid assets to repay every \$1 of liquid liabilities. This means that it is unlikely that the business will be able to repay its immediate debts as they fall due, and that the business has less ability to repay debts than it did last year.
 - ii. The most likely reason for the decline in the liquid ratio is the large increase in Accounts payable – due to the increased purchases of inventory and because it was used to help fund

the increase in property, plant and equipment. The increase in Accounts payable increases liquid assets and, in turn, decreases the liquid ratio. In addition, the owner has taken large amounts of drawings, which has decreased the positive bank account into overdraft. This decrease in bank has decreased the liquid assets and has worsened the liquid ratio. It could have been caused by the \$12,000 cash drawings.

- b. i. If Sara does not improve the liquid ratio of her business, she might be unable to repay her Accounts payable and other expenses as they fall due. This might mean that she will be charged interest on her accounts, thus decreasing the business's profit. Her creditors might also stop the business's credit which will mean that Sara can't buy more inventory, leading to a possible loss in sales.
 - ii. Sara should invest more cash (\$25 000 so the liquid ratio is at least 1:1) in the business. This will increase the Bank account back to positive, which will increase the business's liquid assets and in turn the liquid ratio. Alternatively, the business could borrow more money from the bank on a five-year loan (about \$30 000) and use it to pay off most of the Accounts payable. This will decrease the Accounts payable (which is a liquid liability) and improve the liquid ratio. (Note This isn't very advisable in this particular case due to the poor equity ratio and therefore it might not be accepted as an appropriate answer.) Alternatively, Sara could sell some property, plant or equipment for cash. This will increase the bank account, and consequently also increases liquid assets and liquid ratio.

Part B

- a. i. This ratio means that Sara has financed 45% (or 45 cents in every dollar) of total assets in Cleaning Supplies. This means that the business is not very stable and that it would be unlikely to be able to borrow more money until this ratio increases to above 0.50:1 (that is, more than half).
 - ii. Cleaning Supplies has borrowed more money as non-current liabilities have increased, and this money has probably been used to purchase more property, plant and equipment as these assets have also increased.
 - OR: The business has increased its inventory levels by purchasing larger amounts of inventory on credit (that is, Accounts payable has increased). This both increases the proportion of assets funded by liabilities and reduces the equity proportion.
- b. Sara needs to invest more cash or assets in the business. This will increase her capital, which increases the total equity and the equity ratio. Sara could then use some of this money to repay the Accounts payable or loan which will decrease the liabilities and increase the equity ratio even further.
 - The business could sell off any old and inefficient assets and use the money from the sale to repay the liabilities, such as the loan. This will decrease the liabilities, therefore improving the equity ratio.

Part C

- a. i. This tells Sara that it takes her business 65 days on average to receive the money from her Accounts receivable. This means that Cleaning Supplies does not have good credit control because it is taking longer to recover debts than the expected period of one month.
 - ii. This trend tells Sara that her credit policy has been improving over the past year because her debtors are paying her more quickly, on average, than they were last year. Although this result is still poor, the time taken to receive the money is improving.
- b. 1. Sara could offer a discount for those debtors who pay their accounts within two weeks. Many would want to take advantage of the discount and therefore they would pay quickly. This would mean that the debtors, on the whole, would be taking less time to pay their debts, therefore improving the age of debtors.

Sara could charge interest on overdue accounts, which is another way to encourage people to pay on time. For example, any account more than a month old will incur an interest penalty. This will encourage people to pay more quickly and therefore improve the age of Accounts receivable.

Sara needs to ring all the debtors whose accounts are overdue and send them reminder letters. She should also stop their credit until they have paid their overdue accounts. This will encourage people to pay their debts faster and in turn improve the age of Accounts receivable.

3. Part A

- a. Gross profit percentage = 40.5%
 Distribution cost percentage = 18.1%
- b. i. The finance cost percentage of 2.8% in 2013 tells Carl that Carl's Furniture has spent 2.8 cents of every dollar of sales on interest expenses (2.8% of sales), which is more than last year and which is a poor trend.
 - ii. The reason for the increase in finance cost percentage is that Carl's Furniture increased the amount spent on interest from \$3 000 in 2022 to \$16 000 in 2023. The reason for the increase was the large increase in mortgage taken out to purchase the new showrooms, from \$45 000 to \$210 000. The increase in mortgage has led to the increase in the finance costs.
 - iii. Carl might not be concerned by the increase in finance cost percentage as it is still very low and Carl's Furniture is still making a profit. The reason for the increase is due to borrowing to purchase a non-current asset – a new salesroom. This is expected to increase the number of customers and increase sales and Carl should be able to repay the mortgage over time, reducing the finance cost when the sales continue to increase.
- c. The distribution cost percentage has increased from 15.2% to 18.1%, which is not a good trend. The main reason for the increasing trend is the increase in advertising, primarily full-page advertisements in the local newspaper and new radio advertisements. This increase is expected because the new salesroom has to be promoted to attract new customers.

Recommend that Carl's Furniture reduce the amount spent on advertising next year by using black-and-white paper advertisements rather than colour / half-page not full-page advertisements. This will decrease the distribution costs and the distribution cost percentage and increase profit percentage. So long as some advertising continues, the firm should not lose customers, especially with the new salesroom which is a promotion in itself.

Alternatively Carl's Furniture could reduce its shop electricity use by ensuring the lights are turned off when not needed and by using fewer of them. Using energy-saving light bulbs will also help. This will reduce the cost of shop electricity, which decreases the distribution cost and distribution cost percentage and increases profit percentage. It should not cause a reduction in sales as customers will still visit the new showroom and there will continue to be advertising.

Part B

a. The equity ratio in 2023 tells Carl that he, the owner, has invested 38 cents for every \$1 of total assets into Carl's Furniture. This is a decrease from 2022 as a result of borrowing more, i.e. increasing the mortgage to finance the new salesroom. The increase in liabilities has meant that Carl's Furniture is using greater debt financing. This has increased the total assets but has not increased the equity, which is why the equity ratio decreased.

This low equity ratio of well below 50% means that *Carl's Furniture* will struggle to borrow more in the future until it repays some of the mortgage or Carl invests more money into the business, as the business would be seen as not very financially stable by lenders. Therefore Carl needs to finance any new expansion by investing money himself.

- b. Rate of return on average total assets = 11.1%.
- c. i. In 2022 the return on total assets for Carl's Furniture was 14.2%. This means that the assets were used by Carl's Furniture to generate an average return of 14.2 cents for every \$1 average total assets.
 - ii. The trend in return on total assets decreased from 14.2% to 11.1%, which is a poor trend. The main reason for the trend is the large increase in assets from \$176 300 to \$452 000, due to the new salesroom and greater inventory, due to the need to put more furniture in the salesroom. As the salesroom was opened only in June there wasn't a full year to generate sales from it, so next year's return on assets should be improved. Carl's Furniture also lost sales in the first few months of the financial year due to the building noises, which are no longer happening. The loss of sales would have decreased the profit for the year. These are reasons that Carl shouldn't be too disappointed in the lower return in 2023. Because the new salesroom will now be open for 12 months in 2024 and there will be no building noises, there should be an increase in customers and therefore in sales and profit, which will increase the return on total assets next year.

Part C

- a. Age of accounts receivable = 29 days (always round up)
- b. i. In 2022 the average length of time it took *Carl's Furniture* debtors to pay their accounts was 20 days from the date of sale.
 - ii. In 2023 the age of accounts receivable increased from 20 days to 29 days, which is a worsening trend. One main reason for the increase in age is the increase in sales made in 2023, as a result of the new salesroom and the carrying of more inventory. Another reason could be that the new accounts clerk has not been proactive in chasing the debts to pay within the 15-day terms / has not sent reminder letters. When the accounts clerk was appointed Carl was too busy to go through this with him.
 - iii. Because the debtors are taking longer to repay their debts there is less cash coming into Carl's Furniture as quickly, yet Carl's Furniture still has to pay its expenses and purchases on time. This can put strain on the bank account and as a result it is currently in overdraft because recently the payments have been greater than the receipts so the business might need a bigger overdraft, or arrange to pay suppliers later, thus incurring interest.
- i. Bill should charge interest for all debtors who haven't paid in the 15 days that Carl's Furniture seeks to achieve.
 - ii. This will increase the speed at which debtors repay their accounts because they will not want to pay extra on top of what they owe. This increase in payment receipts will decrease the total Accounts receivable on hand at a time, which decreases the age of Accounts receivable. This will in turn improve the cash flow because the debtors will repay faster, increasing the bank balance and the ability to get the bank account out of overdraft.

OR

- Bill could offer a small discount for those who pay within 7 days to encourage debtors to pay their accounts faster.
- ii. This would result in some debtors paying faster, although it is unlikely that all will, so the increase in discount expenses shouldn't be too great. The fact that debtors will repay faster to take advantage of paying less in total should decrease the age of Accounts receivable. This will improve the short-term cash flow position, as receipts will increase faster because debtors are paying more quickly. This will help Carl's Furniture to pay expenses and improve the bank balance. A little less cash now is better than not receiving it at all or very late. In the long term, less cash will be received, but if this is built into the mark-up, it will not be too detrimental to the overall cash flow.

4. Part A

- a. Gross profit per centage = 60%
 Administrative expense percentage = 20%
 Profit for the year percentage = 8%
 Percentage change in sales = -17% (17% decrease)
- b. i. K D Carpets' increase in mark-up % from 130% in 2021 to 150% in 2022 would have resulted in an increase in the selling price of the carpet. In 2021 the carpet which cost \$200/m would have sold for \$460/m (plus GST), whereas in 2022 the carpet with the same cost would have sold for \$500/m.
 - ii. Examples: Consequence 1 Decrease in sales by 17% Explanation 1 As a result of *K D Carpets* increasing its mark-up and therefore selling price there was a decrease in sales from \$960 000 in 2021 to \$800 000 in 2022, which is shown by the 17% decrease in percentage change in sales. This was made worse because of the new competitor which, along with the increased prices, has meant customers have been lost, and therefore sales. Consequence 2 Decrease in profit for the year Explanation 2 In 2021 *K D Carpets*' profit for the year was \$84 000, while in 2022 this had dropped to \$60 000, one reason being the decrease in sales caused by the increase in mark-up scaring away some of the customers to the new competitor. As a result of not reducing administration expenses and an increase in finance costs, the reduced sales revenue resulted in an overall decrease in profit.

Consequence 3 – Increase in loan and finance cost Explanation 3 – Due to the increase in mark-up % (and selling prices) and the loss of customers and therefore sales receipts, there was pressure put on the cash flow and bank balance of *K D Carpets*. As a result, it had to increase its loan by \$39 000, which increased the finance costs and decreased the profit. (Also the decrease in bank balance – similar answer.)

Part B

- a. i. The trend in distribution cost percentage for KD Carpets is decreasing, which is an improvement. This means that there has been a decrease in the amount of distribution expenses (e.g. sales wages, advertising) in relation to the total sales received.
 - ii. One reason for the decrease in distribution cost percentage was the fact that *K D Carpets* did not renew the regional television advertising, which meant fewer sales, but a large decrease in the amount of advertising expenses for 2022, which contributed to the decrease in the distribution costs from \$310 000 to \$248 000, and as a result a decrease in distribution cost percentage from 32% to 31%.
 - iii. As a result of not having television advertising in 2022, there was less exposure for KD Carpets, and as a result fewer customers because they went to competitors, which contributed to the fall of 17% in sales.
- b. One of:

Examples

Recommendation: Karina needs to ensure that her staff are well trained and needs to have an excellent after-sales service.

Justification: By ensuring the carpet is laid to a high standard, *K D Carpets* will generate a good reputation and increase sales. It will also ensure that no time is lost having to fix up jobs (which means Karina is paying her workers twice for the same job and which decreases her profit). Doing the job properly the first time will increase profit, and also means her workers are available to do more installations more quickly than before. This means she should be able to do more jobs than her competitor.

Recommendation: Karina should increase her advertising and definitely follow up on the radio jingle mentioned on the 'sticky' notes.

Justification: By increasing her advertising, Karina will have a lot more exposure and more potential customers will hear the advertisement and visit her shop. By increasing the customer exposure, *K D Carpets* should be able to increase its sales and, as a result, its profit for the year and profit percentage. If *K D Carpets* advertises that it is well established and that it provides excellent service, this will help it compete against the new business.

Part C

- a. Equity ratio 2022 = 0.67:1
- b. i. This means that in 2022 Karina has invested/financed 67 cents for every \$1 assets in K D Carpets which means that K D Carpets is reasonably stable because the owner has financed a greater proportion of the assets than the liabilities, despite the increasing loan balance
 - ii. One main reason for the decreasing trend in equity ratio from 0.74: 1 to 0.67: 1 is the large increase in the loan, which has been used to finance the increase in property, plant and equipment that K D Carpets purchased. This has increase the total assets from \$478 000 to \$525 000, increasing the liabilities, which in turn has decreased the closing equity and equity ratio. Another reason for the decrease in equity ratio was the increase in drawings from \$37 000 to \$66 000. Because the amount of drawings was greater than this year's profit there was a decrease in equity. This decrease, along with the increase in assets, resulted in a decrease in the equity ratio for K D Carpets for the year ended 31 March 2022.
 - iii. The trend of the decreasing equity ratio is a concern. However, the level is still very stable, and given the cause of the fall, it is not a big problem. The increase in the loan is an expected consequence of the large increase in property, plant and equipment, and is acceptable, given the high equity ratio of KD Carpets. It will, however, put pressure on the finance costs and profit in the future.
 - Karina can easily reduce her drawings and this will help increase the equity ratio of *K D Carpets*, providing her drawings are less than the profit for the year. With the measures to increase sales this should also improve in the upcoming year so is not a major concern.

Part D

- a. Current ratio 2021 = 2.93:1, Inventory turnover 2022 = 5.77 times
- b. i. This means that in 2022 K D Carpets has \$1.90 in current assets to repay every \$1 of current liabilities. As a result K D Carpets should be able to meet its current / short-term debts as they fall due in the normal course of business; however, its ability to meet debts has fallen from the previous year.
 - ii. Inventory turnover of 5.77 times means that, on average, K D Carpets sells the equivalent to the inventory on hand 5.77 times per year. This is a good level (all inventory is sold nearly every two months); however, considering this has nearly halved from last year, this is an unfavourable result. Examples of reasons for the trend in inventory turnover decreasing are:
 - The increase in mark-up % from 130% to 150% which led to an increase in selling price, fewer customers and fewer sales.
 This meant that less inventory was sold so there is more kept as inventory this year (\$61 000 compared with \$50 000 last year). As a result, the carpet is getting older and harder to sell.
 - The new competitor that has opened up has led to more competition and therefore fewer customers and fewer sales.
 This meant that less inventory was sold so there is more kept as inventory this year (\$61 000 compared with \$50 000 last year). As a result the carpet is getting older and harder to
 - The low inventory turnover will put pressure on K D Carpets' ability to repay its current debts because it is relying on the inventory to be sold to repay those debts. Given that it takes more than two months to sell the inventory (on average) this is not good because many of K D Carpets' current debts will need to be paid in the next 4–6 weeks (as measured in the liquid ratio). In addition, the inventory is 57% of the current assets, making it an important asset in the repayment of current debts. Therefore the lower inventory turnover makes it more difficult than it was last year to meet current debts.

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