ACCOUNTING 3.1

Externally assessed
4 credits

AS 91404

Demonstrate understanding of accounting concepts for a New Zealand reporting entity

This Achievement Standard is related to:

- relevant parts of New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and subsequent updates
- the current New Zealand Framework (NZ Framework); (New Zealand Equivalent to the International Accounting Standards Board Conceptual Framework of Financial Reporting).

'Demonstrate understanding' involves applying accounting concepts to a New Zealand reporting entity so its stakeholders are able to make decisions.

'Demonstrate in-depth understanding' involves explaining the application of accounting concepts to a New Zealand reporting entity so that its stakeholders are able to make decisions.

'Demonstrate comprehensive understanding' involves justifying the application of accounting concepts to a New Zealand reporting entity so that its stakeholders are able to make decisions.

The **entity** is a reporting entity as defined in the Financial Reporting Act 1993.

Accounting concepts are selected from:

- features of reporting entities
- statutory reporting requirements
- New Zealand Generally Accepted Accounting Practice (NZ GAAP)
- general-purpose financial statements
- accounting policies
- NZ Framework.

Unit 1 – The conceptual framework

The **conceptual framework** refers to the concepts that underlie the preparation of financial statements and how they are presented. The concepts are based on those in the NZ Framework, which is a booklet issued by the New Zealand Institute of Chartered Accountants. The NZ Framework assists preparers of statements, in addition to auditors and users, to interpret financial statements.

The NZ Framework refers to qualitative characteristics of useful financial information. Often, in accounting, there are transactions or situations that cannot be measured numerically and which have a degree of subjectivity. In those cases the NZ Framework can be referred to as a source of authority and guidance. In order for information to be useful it must be relevant and faithfully represent what it says it represents.

The NZ Framework

Purpose of the NZ Framework
To assist preparers, auditors and users in presenting and interpreting financial information (see specific section for points to study)

Scope of the NZ Framework
- Objective of general purpose financial reports
- Underlying assumptions (going concern)
- Elements (assets, liabilities, equity, income and expenses)
- Qualitative characteristics

Status of the NZ Framework
Does not override a specific International Financial Reporting Standard (IFRS) but is a source of authority if the IFRS is silent on a particular issue

Fundamental
Essential aspects of information needed to ensure sound decisions can be made

Relevance
Information that is capable of making a difference in a decision

Subsections
Materiality
Predictive value
Confirmatory value

Faithful representation (formerly 'Reliability')
Information is useful when it represents what it says it represents

Subsections
Neutral
Complete
Free from material error

Enhancing
Information may be already relevant and faithfully represented but these enhancing characteristics make it more useful and assist in deciding how best to present information

Subsections
Comparability
Verifiability
Timeliness
Understandability

Purpose of the NZ Framework

The International Accounting Standards Board (ISAB) is currently working on harmonising standards so they are consistent from one country to another. Part of this work is developing a conceptual framework, of which New Zealand has a version called the NZ Framework.

The IASB's Conceptual Framework sets out the concepts that underlie the preparation and presentation of financial statements for external users. The purpose of the IASB's Conceptual Framework is:

a. To assist the IASB in the development of future IFRSs and in its review of existing IFRSs.

b. To assist the IASB in promoting harmonisation of regulations, accounting standards and procedures relating to the presentation of financial statements by providing a basis for reducing the number of alternative accounting treatments permitted by IFRSs.

c. To assist national standard-setting bodies in developing national standards.

d. To assist preparers of financial statements in applying IFRSs and in dealing with topics that have yet to form the subject of an IFRS.

e. To assist auditors in forming an opinion as to whether financial statements comply with IFRSs.

f. To assist users of financial statements in interpreting the information contained in financial statements prepared in compliance with IFRSs.

g. To provide those who are interested in the work of the IASB with information about its approach to the formulation of IFRSs.

ACCOUNTING 3.3

Externally assessed
5 credits

Demonstrate understanding of company financial statement preparation

This Achievement Standard is listed under the 'reporting' section of the accounting matrix, so the emphasis is on the preparation of the various financial statements for a company.

Merit answers involve explaining some of the accounting treatment of the various elements in the financial statements.

Excellence answers involve justifying the accounting treatment of the various elements in the financial statements.

AS 91406

PART 1: Processing

Unit 1 – Processing for the issue or repurchase of shares in a company

This section deals with:

- shares issued for cash to directors
- shares issued in exchange for other assets
- shares issued to repay debt
- shares issued for the purchase of an existing business
- shares issued for cash to the public, processed by the company, with an oversubscription
- shares issued for cash to the public, using a sharebroker
- share repurchase.

Recording journal entries

Recording the following ensures a complete journal entry:

- date
- debit particulars (account names), debit $ amount
- credit particulars (account names), credit $ amount
  (the total dollars of the debit entries must equal the total dollars of the credit entries)
- narration – a brief sentence, explaining the journal entry.

Convention has the debit entry recorded first, although markers in an exam will mark line by line provided there is a complete journal entry. Often the narration is not required.

Date	Particulars	Dr	Cr

In an examination, the account names should be the names used in the resource material provided, particularly from a trial balance, or should follow accepted accounting terminology.

Issuing of shares

Whenever a company issues shares, the capital of the company is increasing, so 'contributed equity' is *always* a credit entry. 'Contributed equity' is the account name used for the capital contributed by shareholders.

The asset that the company is receiving is the debit entry.

Shares issued for cash to directors

There is one journal entry, with Bank being the debit entry and Contributed equity being the credit entry.

Date	Particulars	Dr	Cr
Feb 9	Bank	500 000	
	Contributed equity		500 000
(Record 250 000 shares issued at $2 each to directors on initial formation of company)			

Shares issued in exchange for other assets

A company may purchase an asset by issuing shares to the current owner of the asset. The asset is valued, and sufficient shares are issued to pay the purchase price of the asset.

Date	Particulars	Dr	Cr
Mar 10	Vehicles	50 000	
	Contributed equity		50 000
	(Record 25 000 shares issued at $2 each for purchase of a vehicle)		

Ans. p. 266

Activity 1A – Contributed equity

For each of the following two situations, prepare the necessary general journal entries and the general ledger account for contributed equity. The situations are related, so the contributed equity account will alter.

1. Three friends, Alf Brown, Colin Davis and Edward Fox, decide to form a company, *Alphabet Ltd*. The three friends are to pay $20 000 each and receive 10 000 shares each in *Alphabet Ltd* on 1 April 2012.

Journal entry

Date	Particulars	Dr	Cr
	(Record issue of shares to directors)		

General ledger account – Contributed equity

Date	Particulars				Dr/Cr

Accounting 3.4

Internally assessed
5 credits

Prepare a report for an external user that interprets the annual report of a New Zealand reporting entity

AS 91407

This Achievement Standard is listed under the interpretation section of the accounting matrix, so the emphasis is on the writing of a report that interprets the annual report of a New Zealand reporting entity.

Merit answers involve writing a report that links financial and non-financial information from the annual report and draws a conclusion, with reasons, that has a recommendation to meet the needs of the user.

Excellence answers involve writing a report that interprets the annual report in relation to the entity's wider economic activities, draws a conclusion, stating limitations, and justifies a recommendation to meet the needs of the user.

The report needs to be prepared for an external user from the following categories, with the report tailored to that person's needs.

The user could be:
- a shareholder or a potential shareholder
- an interested employee or potential employee
- an interested consumer
- an interested community group.

The report will analyse and interpret a reporting entity's published annual report; usually the company selected should be one that is listed on the NZ Stock Exchange, or it could be a local council's annual report or that of another similar organisation.

Unit 1 – Analysis

The analysis involves a series of calculations covering the following areas.

Profitability

The analysis measures are: mark-up percentage, expense percentages, interest expense percentage, profit for the year percentage, return on equity percentage, return on average total assets percentage, percentage change in sales/profit for the year.

Liquidity

Measures are: current ratio, liquid ratio, inventory turnover, age of accounts receivable, equity ratio, times interest covered.

Cash management

Measures are: cash from operations, cash from investing, cash from financing.

Analysis for specific users

There could be other specific analysis required for the various users:
- Shareholder or potential shareholder – market analysis including dividends per share, dividend yield, earnings per share, price earnings ratio.

- Employee – directors fees' percentage change, payments to employees over $100 000
- Interested consumer – origins of goods, mark-up percentage, profit for the year percentage, percentage change in profit, return on equity percentage
- Interested community group – environmental report, donations to community groups, number of employees.

The most likely user would be a shareholder or potential shareholder, or an employee.

Analysis formulas

Profitability

Analysis measure	Formula
Mark-up percentage	$\frac{\text{Gross profit}}{\text{Cost of goods sold}} \times \frac{100}{1}$
Gross profit percentage	$\frac{\text{Gross profit}}{\text{Sales}} \times \frac{100}{1}$
Interest expense percentage	$\frac{\text{Interest expense}}{\text{Total revenue}} \times \frac{100}{1}$
Expense percentage	$\frac{\text{Total expenses}}{\text{Total revenue}} \times \frac{100}{1}$
Profit for the year percentage	$\frac{\text{Profit for the year}}{\text{Total revenue}} \times \frac{100}{1}$
Rate of return on equity percentage	$\frac{\text{Profit for the year}}{\text{Average equity*}} \times \frac{100}{1}$
Rate of return on total assets percentage	$\frac{\text{Profit before interest \& tax}}{\text{Average total assets**}} \times \frac{100}{1}$
Percentage change in revenue	$\frac{\text{This year's revenue – last year's revenue}}{\text{Last year's revenue}} \times \frac{100}{1}$
Percentage change in profit for the year	$\frac{\text{This year's profit – last year's profit}}{\text{Last year's profit for the year}} \times \frac{100}{1}$
Wages expense percentage (or any other significant expense)	$\frac{\text{Wages}}{\text{Total revenue}} \times \frac{100}{1}$

AS 91407

Example

If there was only a CVP Profit Statement for *Scooters Galore* and no per-unit information then the following would apply.

Sales	960 000
Less variable costs	390 000
Equals contribution margin	570 000
Less fixed costs	400 425
Equals profit	$169 575

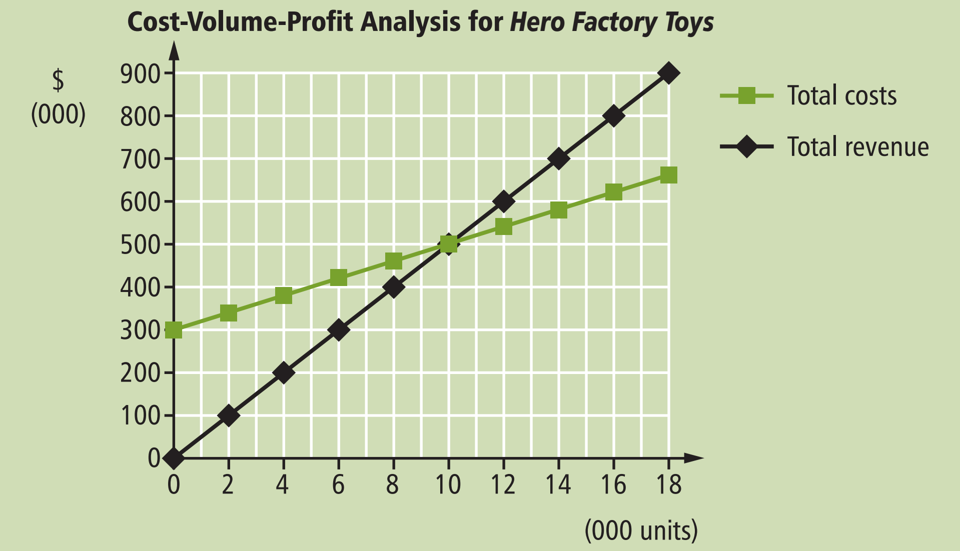
contribution margin ratio $= \frac{570\ 000}{960\ 000} = 0.59375$

break-even sales $= \frac{400\ 425}{0.59375} = \$674\ 400$

Cost-volume-profit analysis graph

The break-even point can also be determined using a graph to display the total sales and total cost curves.

The following graph illustrates a break-even analysis for *Hero Factory Toys*, which produces toys that sell for $50 per 'hero' and have a variable cost of $20 per hero. *Hero Factory Toys* has fixed costs of $300 000 per annum and a relevant range of 18 000 toys.



The total revenue curve is prepared by multiplying the number of units sold by the selling price.

The total cost curve starts at $300 000. That is because *Hero Factory Toys* has fixed costs of $300 000 per annum. Even when it is not selling any toys it still has costs of $300 000. The total cost curve then increases by $20 per unit produced. The $20 per unit represents the variable cost per toy.

Also notice that the graph shows output only up to 18 000 units. This is the relevant range for *Hero Factory Toys*. Any output beyond 18 000 toys will result in an increase in fixed costs for *Hero Factory Toys*. Remember the relevant range shows the maximum available production with existing resources, so if *Hero Factory Toys* wants to increase production beyond 18 000 toys, it will need to invest in additional resources such as plant and machinery, which will increase fixed costs.

AS 91408

The point where the two curves meet is the break-even point, because this is where total costs equal total revenue. For *Hero Factory Toys*, break-even is 10 000 toys or sales revenue of $500 000.

Had we used the break-even formula demonstrated above, we would have got the same result:

$$\frac{\text{Fixed costs}}{\text{Contribution margin}} = \text{break-even}$$

For *Hero Factory Toys*: $\frac{\$300\,000}{\$30} = 10\,000$ toys

The cost-volume-profit analysis graph can also be used to determine profit or loss at given levels of sales. Any output below the break-even point will result in a loss, because total costs are greater than total revenue. Any output above the break-even point will result in a profit.

For *Hero Factory Toys*, we can use the graph to identify the profit/loss situation:

- at 6 000 toy sales, *Hero Factory Toys* will make a loss of $120 000
- at 16 000 toy sales, *Hero Factory Toys* will make a profit of $180 000.

Hero Factory Toys is an example of a trading firm where the cost-volume-profit analysis is determined on a per-unit-produced basis. Service firms can also use cost-volume-profit analysis. Generally, costs for a service firm are charged out based on a time unit rather than an individual unit of production. Some service firms, such as accountants and lawyers, charge out time in five-minute blocks, while other firms determine costs in hourly units.

Ans. p. 280

Activity 3B – Preparing cost-volume-profit analysis for a service firm

Service firms can also use cost-volume-profit analysis. This question deals with the service provided by a dentist.

Pearly Whites is a dental clinic in Oamaru. Holly White is the owner of *Pearly Whites*. The following information relates to the dental clinic.

The hourly rate charged out to patients is $200, variable costs per hour are $80 and fixed costs are $240 000 per annum. The relevant range is currently limited to two dentists working 40 hours per week for the 50 weeks a year the clinic is open. Last year, *Pearly Whites* charged out 3 700 hours to patients.

1. a. List four fixed costs that might be included in the $240 000 of fixed costs for *Pearly Whites*.

b. Identify three semi-variable costs that *Pearly Whites* might have.

c. Calculate the contribution margin for *Pearly Whites*.

d. Calculate the number of hours *Pearly Whites* needs to charge out to patients in order to break even.

Accounting 3.6

Internally assessed
4 credits

Demonstrate understanding of a job cost subsystem for an entity

Achievement Standard 91409 (Accounting 3.6) is listed under the systems section of the accounting matrix, so the emphasis is on the explanation of the various controls used in a job cost subsystem to ensure the integrity and viability of the subsystem.

Merit answers involve processing detailed financial information to determine the cost of a job, as well as explaining the application of the elements of a job cost subsystem.

Excellence answers involve processing detailed financial information to justify the cost of a job, as well as justifying the application of the elements of a job cost subsystem.

The elements of a job cost subsystem include:

- internal controls on the source documents used in a job cost subsystem
- selecting an appropriate base for allocating overhead costs
- correctly allocating costs to a job
- under- or over-applied overhead.

Unit 1 – Job cost subsystem

A job cost subsystem is the method used by a manufacturing business to determine the cost of individual or unique jobs.

Manufacturing can be on a large scale, producing large volumes of the same product, e.g. tins of baked beans. The cost of producing one 440 g tin of baked beans is the same as the cost of producing another 440 g tin of baked beans.

Manufacturing can also involve small individualised jobs, where the costs involved are specific to each particular job, e.g. a printer preparing invitations to a wedding ceremony; although each job has similar parts, no two jobs of printing are identical. Therefore precise costs for each job must be recorded so the amount to be charged to clients can be accurately calculated.

Costs must be known or estimated before a job begins, so the customer can be given a quote for the job. The estimate is arrived at by recording costs for each section of work and accumulating the costs to find the total cost of a job. A mark-up is then applied to the job to cover other business expenses and to generate a profit.

AS 91409

Costs

Inventory

A manufacturing business has three different types of inventory, all of which have debit balances.

- **Raw materials** – the components used to make the finished goods.
- **Work in progress (WIP)** – the goods for which production has started but the goods are not complete or finished.
- **Finished goods** – goods that are complete and available for sale.

Production process

The manufacturing process has different stages in which the materials change into finished goods.

raw materials → work in progress → finished goods

In addition to raw materials, two other costs are added to the 'work in progress' stage: **direct labour** and **factory overheads**. It is best to think of items joining and leaving a stage of inventory. When joining, an item has a debit entry and when leaving it has a credit entry.

Raw materials

Raw materials are either:

- **direct materials** – their use can be traced to a particular job
- **indirect materials** – their use cannot be traced to a particular job, so the materials are recorded as part of factory overhead costs.

Examples of indirect materials are grease used by a mechanic, nails or screws on a building site, or materials used to set up a machine for a task before the job begins.

Grease used by a mechanic is an example of an 'indirect material'

Labour

Costs for labour are for **direct labour** or for **indirect labour**.

- Direct labour – the cost of the employees producing the job: their hours worked can be traced to a particular job; e.g. the machine operator, or mechanic. It is the cost of the actual hours that the employee worked on a particular job (actual hours multiplied by the employee's hourly pay rate).
- Indirect labour – the hours worked cannot be traced to a particular job, so are recorded as part of factory overhead costs; e.g. for factory supervisor, cleaning machines at the end of a day.

Factory overheads

'Factory overheads' are the costs that are necessary for production to occur but which cannot be specifically identified and traced to a particular job. Examples are factory electricity, factory rent, factory supervisor's salary, factory cleaning, or grease used by a mechanic. These costs are still part of the cost of producing a job and need to be allocated to each job.

Answers

Achievement Standard 91404 (Accounting 3.1)

Activity 1A – NZ Framework overview (page 3)

1. (For example) To assist users of financial statements in interpreting the information contained in financial statements prepared in compliance with IFRSs and to assist auditors in forming an opinion on whether financial statements comply with IFRSs
2. **a.** The IFRS should be followed.
   b. The IFRS is superior to the NZ framework because it outlines the international standards that entities must follow when presenting financial information. The NZ framework can only enhance these standards or be used to develop new standards.
3. (For example) The underlying assumption in the preparation of financial statements; qualitative characteristics of useful financial information.
4. Fundamental qualitative characteristics are essential to the preparation of financial information because they ensure that the information is of sufficient quality to enable useful decisions to be made, whereas enhancing qualitative characteristics enhance or add value to financial information that may already be relevant and faithfully represented. The enhancing characteristics ensure the information is more useful and gives guidance on how best to present information.
5. If the preparers of financial statements need clarification on a certain point that is not fully covered in the International Financial Reporting Standard then they will be able to refer to the NZ Framework as a back-up source of authority. For example, if a company has leasehold property, it may wish to refer to the asset definition and recognition criteria in the NZ Framework to see if the property should be classified as an asset in the Statement of Financial Position.
6. They would refer to the element definition and recognition criteria to check that items had been correctly recorded in the Statement of Financial Position. Auditors would also use the concept of materiality as a guide as to whether an item is of sufficient size or nature to influence the decisions of users.

Activity 1B – NZ Framework assumptions (page 5)

1. The purpose of the NZ Framework is to set out underlying concepts and assumptions that are used when preparing general-purpose financial statements
2. Suppliers, employees, investors, Inland Revenue Dept. (any three)
3. Financial statements intended to meet the needs of users who do not have the power to require an entity to prepare reports tailored to the users' particular information needs.
4. **a.** General Purpose Financial Reports consist of the Income Statement, Statement of Changes in Equity, Statement of Financial Position and Statement of Cash Flows.
   b. General-purpose financial reports provide financial information about the reporting entity that assists the decision-making of existing and potential investors, lenders and other creditors. Special-purpose financial reports are additional information requested by users who are affected by the operation of the entity and have the power to demand certain types of information. The NZ Framework does not cover special-purpose financial statements.
   c. Examples: A bank might request a cash budget to support a loan application or the IRD might request information about GST collected and paid to support a GST return.
5. The accrual basis states that financial information must be recorded when it occurred and reported to the period to which it relates. The interest of $600 owing on the loan will be added to the interest on loan expense that is reported in the Income Statement because this expense relates to the period ended 31 March 2015.
   The interest of $600 owing on the loan will be reported in the Statement of Financial Position as 'accrued expense', a current liability because there will be future economic benefit in the form of cash flowing out in the next accounting period to pay the bank interest for the use of the loan.
6. The going concern assumption is that an entity is assumed to continue to operate into the foreseeable future, so assets should be recorded at historical cost. If a company is not a going concern, buildings and vehicles should be recorded at their market value rather than their historical cost, because this is the price the company would be likely to receive for them if it had to stop operations due to financial difficulty. Recording the assets at market value would ensure the financial information is useful for making decisions about the entity.

Activity 1C – Fundamental characteristics (page 8)

1. Using historical cost as the basis for measurement can be described as neutral because doing so presents the value of the property (such as a fishing boat) free from bias. It does not involve estimates that might influence how the user interprets the information. A source document provides the original purchase price of the fishing boat, giving a true and fair view. A higher value (in order to manipulate users into thinking the boat is worth more than it is) is not stated.
2. *Sanford Limited* is likely to use estimates for the depreciation on property, plant and equipment (such as fish-processing factories) and the allowance for doubtful debts when selling on credit to fish markets. These estimates can be made free from material error by arriving at the estimates using specific and consistent methods from year to year. While the estimates might not result in precise values for the factories, any differences are likely to be small and would not influence users' decisions.
3. The notes to the financial statements showing details of property, plant and equipment demonstrate completeness by displaying all necessary information, such as how much fishing boats cost and how much they have depreciated. This information can be given to end users so they can gain a full understanding of the operations of *Sanford Limited* and of the methods and valuations that have been used for calculating property, plant and equipment. This indicates that information is faithfully represented and is useful for decision-making.
4. The Statement of Financial Position can have predictive value because the information in it can be used as an input to establish what is likely to happen in the future. For example, the accounts receivable gives information about how much cash will come in during the next few months. Looking at interest payable will show how much cash is needed to pay this expense next year. Investors can also look at the amount of property, plant and equipment to see if *Sanford Limited* is

able to maintain its current level of sales. This type of information from a Statement of Financial Position can be used to prepare a cash budget or Statement of Cash Flows.

5. Information is considered to be material if its size or nature is large enough that omitting the information or misstating it would influence the decisions of end users. The fishing quota makes up a significant portion of total assets so its size is big enough to affect decisions. In addition, its nature is material because *Sanford Limited* is a fishing company so its fishing quota is directly related to its main revenue stream – if it did not have a quota it would not be allowed to fish. Therefore this intangible asset is material both because of its large size and because of its important nature and information concerning it is likely to affect the decisions of users.

Activity 1D – Enhancing qualitative characteristics (page 9)

1. *Sanford Limited* shows the Income Statement for both 2011 and 2012 because this enhances the characteristic of comparability. Investors are able to compare the figures from one year to the next to identify trends in the company, e.g. whether sales of fish are increasing or not.
2. The annual report being available for end users only a few months after the end of the financial year allows timely decisions to be made because the information the report contains is up to date. The information can therefore assist end users to make useful decisions promptly at the start of the next financial year, before too much time has elapsed.
3. Understandability is aided by presenting revenue in a clear and concise manner that is easy for end users to comprehend. Users can identify which countries are generating most income for the company and which countries are not generating so much revenue.
4. Having both financial statements and comprehensive notes to the financial statements is aiding understandability because end users are given clear and concise information in which it is initially easy to see the major trends in the company's performance. If extra detail is required, it is assumed users have a reasonable knowledge of accounting principles and methods and enough diligence to look in the notes. This aids their understanding and therefore enhances decision-making.
5. An auditor's report can assist with the verifiability of financial statements because more than one knowledgeable person has reached agreement on how to treat a certain situation, and the auditor's report guarantees that the financial information prepared is free from bias and is neutral, because auditors are a separate entity from the company they are auditing and auditors must comply with reporting standards and a code of ethics. If the auditor disagrees with the treatment of a material part of the statements, this will be pointed out in the auditor's report.
6. Many different individuals and companies that have a relationship with *Sanford Limited* would benefit from viewing the financial statements. Employees might want to check their job security; suppliers would want to check that *Sanford Limited* has a good credit rating and is able to pay its debts; communities where there are fish-processing plants might want to see if *Sanford Limited* will continue operating in their area; and investors would want to see if they are gaining sufficient return on their investment. The benefit users of the annual report of *Sanford Limited* receive would outweigh the costs to *Sanford Limited* of preparing the annual financial statements, getting an audit and then publishing the information.

Activity 2A – Elements: Skill-development tasks (page 12)

1.

Aspect of the definition of recognition criteria	Application to an electronic fish-finder asset
Past event	The purchase of the fish finder by the company in the past
Present control	*Sanford Limited* is the legal owner and can stop others from using the fish finder.
Future economic benefit	The fish finder will be used to find fish, which can be caught and sold for cash in the future.
Probable economic benefit will be received	The fish finder will result in more fish being caught, which, once caught can be sold for cash.
Measured with reliability	The value of the fish finder can be measured reliably, because reference can be made to the source document to find the purchase price.

2.

Aspect of the definition of recognition criteria	Application to an interest received
Increase in economic benefit	Cash is received when the interest is paid into the business bank account.
Increase in asset	When the interest is received it is paid into the bank account, which is an asset that increases.
Increase in equity	The interest received will increase the profit on the Income Statement, which in turn will increase the equity.
Not a contribution from the owner	The interest received is from another party and not a contribution by shareholders.
Measured with reliability	The value of the interest received can be measured reliably by referring to the bank statement, which will record the amount received.

Activity 2B – Elements: Recognition criteria (page 13)

1. A fishing boat will be used to travel out into the ocean and catch fish, which can then be processed and sold. When the fish are sold they will provide future economic benefit
2. The fishing boat would have been purchased by *Sanford Limited* at some stage in the past. *Sanford Limited* has control because it has the right to use the boat for fishing as best it sees fit and can prevent others from using the boat.
3. It is more rather than less likely that the boat will be used for fishing and to catch fish which can be sold. When the fish are sold, cash will be received. Therefore it is probable that future economic benefit will be received. When the fishing boat was purchased there would have been a sale and purchase agreement for the boat showing the purchase amount. Therefore the cost can be based on the purchase amount on that document, which can be measured reliably.
4. When *Sanford Limited* pays the mortgage there will be an outflow of its cash resources from its bank account. As cash has economic benefits to *Sanford Limited* when it is paid out to the bank as a mortgage repayment, it can be said that there is an outflow of economic benefit.
5. When the fish are sold on credit there is an increase in the accounts receivable asset of *Sanford Limited*, which will result in an increase in economic benefit when the accounts are paid by cash. The sale will increase profit, which will then flow on to increasing equity. Selling fish to a supermarket is an arms-length transaction, so it is not a contribution by one of the shareholders or owners. The credit sale can be measured reliably by looking at the invoice showing the amount that has to be paid by the supermarket. It is likely that the supermarket will pay the invoice because it is legally obliged to do so and will want to maintain a good credit rating to ensure it can deal with *Sanford Limited* in the future.
6. The telephone expense has been recorded simultaneously with the creation of an accounts payable liability, because making the calls has triggered a present obligation to pay this with cash in the future. The amount can be measured reliably by referring to the invoice that shows the amount payable.

ANSWERS

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