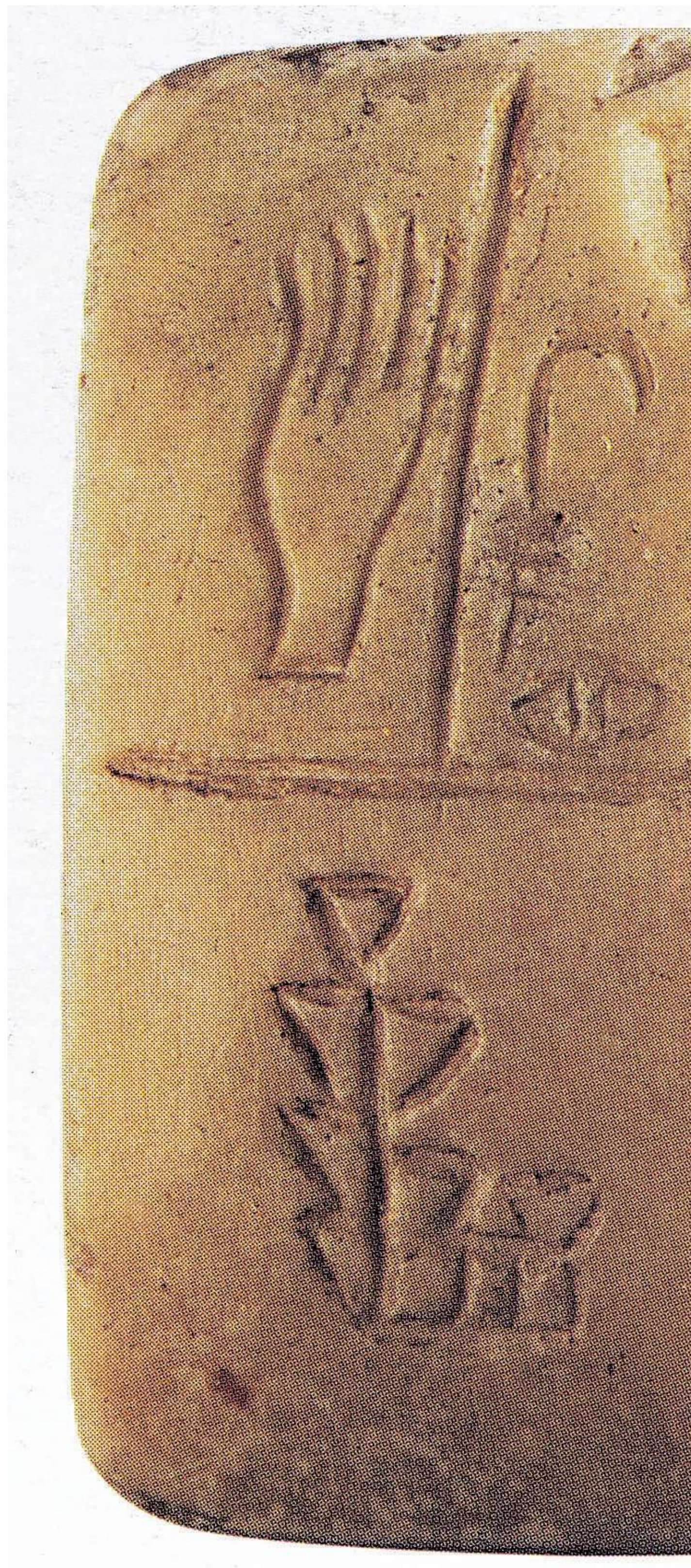
Accounting

THE OLDEST TRICKS IN THE BOOKKEEPING

Accounting is of course one of the best subjects to study in the Leaving Cert having the highest percentage of 'A' grades among the business subjects, writes Institute of Education accounting teacher **Arthur Russell**



INTRODUCTION

Accounting is of course one of the best subjects to study in the Leaving Cert having the highest percentage of "A" grades among the business subjects and one of the highest among all Leaving Cert subjects. As well as this, it is a great foundation for business management with most chief executive officers of public limited companies having some sort of accounting qualification.

SUGGESTED TIMING

The exam lasts for three hours, ie 180 minutes. With 10 minutes allocated to reading the paper this leaves 170 minutes to answer four/five questions depending on your choice in Section 1.

Question/Marks	Suggested Time Allocation
Question 1 – 120 marks	52 minutes approximatley
All 60 mark questions	26 minutes approximatley
All 100 mark questions	42 minutes approximatley
All 80 mark questions	34 minutes approximatley

HIGHER LEVEL PAPER STRUCTURE

Total Marks 400

SECTION 1 (120 MARKS)

Answer Question 1 or any two other questions

Question 1 – 120 marks
Question 2 – 60 marks
Question 3 – 60 marks
Question 4 – 60 marks

SECTION 2 (200 MARKS)

Answer any two questions

Question 5 – 100 marks
Question 6 – 100 marks
Question 7 – 100 marks

SECTION 3 (80 MARKS)

Answer one question

Question 8 – 80 marks
Question 9 – 80 marks

Students must answer four or five questions depending on their choice in Section 1.

Financial accounting is examined in Sections 1 and 2.

Cost and management accounting is examined in Section 3.

	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001
Final Accounts	120 **C**	120 **M**	120 **ST**	120 **M**	120 **ST**	120 **C**	120 **ST**	120 **M**	120 **C**	120 **ST**	120 **C**	120 **M**
Ration Analysis	100	100	100	100	100	100	100	100	100	100	100	100
Correction of Errors	60		100		100		100		100		60	
Tabular Statements		100		60		60	100		60		60	60
Published Accounts		60		100	60		60	100		60	100	
Cash Flow Statements	100		60		100		60					
Club Accounts		100			60				60			60
Service Firms Accounts	100		100			100			100		100	
Farm Accounts	60			60			60			100		100
Depreciation			60								60	
Revaluation	60			60		60			60	60		60
Incomplete Records		60		100		100				100		100
Control Accounts		60 **D**	60 **C**		60 **C**	60 **D**				60 **D**		
Product Costing	50		80	80		80		80		80	80	
Cash Budget	80		80	80		80			80		80	
Production Budget		80			80			80				80
Flexible Budget	30				24		80			80		
Marginal Costing		80			56		80		80			80

■ Mesopotamian Accounting Document. PHOTOGRAPH: GETTY

TOPIC FREQUENCY TABLE

Financial Accounting

Management Accounting

IN FINAL ACCOUNTS
C: Company
M: Manufacturing
ST: Sole Trader

IN CONTROL ACCOUNTS
D: Debtors
C: Creditors

MAY WE HAVE A WORD?

GENERAL ADVICE

1. Timing is crucial in every accounting exam. Students must stick rigidly to the timing advice given above. Many students find themselves sitting in the examination hall with 15 minutes left, and one full question left to complete. Panic then sets in and the student doesn't do herself justice scoring very poorly in her final question.

2. Accounting cannot be learnt. Continual practice of previous examination papers is vital. Of course there is a little theory that has to be studied carefully. Any student wishing to score an A1 must have a thorough knowledge of the theory of accounting.

3. Set aside plenty of rough work pages for calculations. Keep these workings close to the relevant question so that the examiner can apportion marks for any work completed in a satisfactory manner. Students run the risk of scoring zero marks for a particular figure if they omit their workings. Remember that workings can be laid out in note form or account form.

4. Do not attempt Question 1 unless you have a thorough working knowledge of all of the adjustments to the trial balance. These adjustments include: damaged stock; patents written off; bank reconciliation statements; disposal of fixed assets and depreciation; revaluation of fixed assets; debenture interest due; investment income due; bad debts provision; goods in transit; suspense; VAT; capital expenditure; sale or return; dividends etc. Later on in this article you can test yourself and find out if you have a good working knowledge of some of these adjustments.

5. Remember that most financial accounting topics can appear in either Section 1 (a short 60 mark question) or in Section 2 (a longer 100 mark question).

Topics, such as tabular statements, correction of errors, published accounts, cash flow statements, club accounts, service firms, would be regarded as normal Section 2 questions but have often been shortened and asked as Section 1 questions. There is even the possibility that a farm account, which is normally a Section 1 question, could be extended and examined in Section 2.

In 2011 incomplete records, which has been examined as a 100 mark question since the new Leaving Cert course was introduced in 1997, was examined as a 60 mark question. There is even the possibility that ratio analysis which has always been examined as a 100 marker could be shortened and examined as a 60 mark question. My advice is expect the unexpected.

6. Do not attempt to answer the correction of errors topic unless you have a solid understanding of the basic double-entry system, ie debits and credits. The following might be a useful guide to the double-entry system –

■ Expenses and gains are recorded in the trading and profit and loss account.

■ Expenses are normally on the debit side of their own accounts; typical expenses include purchases, wages, light and heat, discount allowed, repairs, rent payable, bad debts, interest payable etc.

■ Gains/income are normally on the credit side of their own accounts; typical gain accounts include sales, rent receivable, discount received, bad debts recovered, interest receivable, commission receivable and so on.

■ Assets and liabilities are recorded in the balance sheet.

■ Assets are normally on the debit side of their own accounts; typical assets include land, premises, vans, equipment, investments, goodwill, patents, debtors, bank, cash, drawings (in the sense that drawings is what the owner owes the business).

■ Liabilities are normally on the credit side of their own accounts; typical liabilities include creditors, bank overdraft, loans, and capital.

7. As the day of reckoning begins to draw closer and closer, one guaranteed way of alleviating that sinking feeling in your stomach, is to practise at least one accounting question every day. Have these answers corrected by your teacher and then fine-tune yourself by examining very closely where you have made your errors. Continue with this policy right up until the end of May and this will result in a huge improvement in your grade.

8. Do not make the mortal error of assuming that just because a topic appeared on last year's examination paper, that it cannot be asked on this year's paper, or that just because it normally is examined in Section 2 it cannot be examined in Section 1. There have been numerous occasions when a topic has appeared on the paper two years on the trot. Don't fall into this trap and be caught with egg on your face.

So remember that there are no shortcuts on the road to success, cover the entire course. It will be worth it, and remember that the only place that success comes before work is in the dictionary. Success is said to comprise two per cent inspiration and 98 per cent perspiration. So get on with it and don't look back in five or six months time and say "if only I had done a little more revision each night". Don't do it for anyone else, do it for yourself and do it now.

9. In a matter of a couple of months all this hard slog will be over, and you will find a huge burden lifted from your shoulders. So put your social life on hold, or at the very least limit it, and get stuck in. Remember: no regrets next August.

RATIO TO THE BOTTOM LINE

The following are a number of typical questions. Remember: these are not meant to be tips for Leaving Cert 2013. A typical section 2 question is a ratio analysis question which scores 100 marks. This is 25 per cent of the overall marks. Therefore you can allow yourself approximately 42-45 minutes to complete this question.

RATIO ANALYSIS

The following figures for the year ending 31/12/2012 have been taken from the accounts of A Matthews A Sheridan Ltd. a company engaged in the sale of marathon and endurance heart monitors.

Trading, Profit and Loss Account for y/e 31/12/2012

	€	€
Sales		800,000
Stock 1/1/2012	70,000	
Purchases	480000	
	550,000	
Stock 31/12/2012	(120,000)	
		(430,000)
Gross Profit		370,000
Operating Expenses		(98,000)
Operating Profit		272,000
Interest		(16,000)
Net Profit		256,000
Dividends Paid		(180,000)
Retained Profits		76,000
P+L Balance 1/1/2012		100,000
P+L Balance 31/12/2012		176,000

Balance Sheet as at 31/12/2012

	€	€
Fixed Assets		990,000
Investments (market value €150,000)		130,000
Current Assets	330,000	
Current Liabilities	(120,000)	210,000
		1,330,000
Financed By		
5% Debentures 2014 secured	320,000	
Ordinary Share Capital – €1 shares	640,000	
10% Preference Share Capital	194,000	
P+L Balance	176,000	1,330,000

The market value of one ordinary share is € 1.90.

The relevant ratios for 2011 include the following:

Earnings per share	30 cent
Price earnings ratio	4.8 years
Return on capital employed	15%
Interest cover	12 times
Acid test ratio	0.9 : 1
Gearing – based on the debt to equity %	70%
Dividend yield	10.42%
Market price	€ 1.44
Dividend per share	15 cent

A) Calculate the following for 2012–
1. The return on capital employed.
2. The earnings per ordinary share.
3. The dividend yield.
4. The dividend cover.
5. The interest cover.

B) Advise Katie Russell, bank manager of JRUSE Bank Ltd, on whether she should give a loan of € 200,000, at 10 per cent per annum, to this company, for expansion purposes.

SOLUTION A

1. Return on Capital Employed

The formula is:

$$\frac{\text{Net profit + debenture interest}}{\text{Capital employed}} \times \frac{100}{1}$$

$$\frac{€256{,}000 + €16{,}000}{€1{,}330{,}000} \times 100 = 20.45\,\%$$

The debenture interest is 5% of the debentures of €320,000 = €16,000.

The capital employed is the total of the financed by section of the balance sheet.

2. Earnings Per Share

This is the profit, left over to the ordinary shareholders, per share and it is calculated as follows:

$$\frac{\text{Net profit less preference dividend}}{\text{Number of issued ordinary shares}}$$

$$\frac{€\,256{,}000 - €19{,}400}{640{,}000\ \text{shares}} = 36.97\ \text{cent}$$

The preference dividend is calculated by 10% of the issued preference share capital of €194,000, giving you an answer of €19,400.

3. Dividend Yield

This is the ordinary dividend per share calculated as a percentage of the market price of one ordinary share.

The formula is:

$$\frac{\text{Ordinary dividend per share} \times 100}{\text{Market Price}}$$

$$\frac{25.09\text{c} \times 100}{190\text{c}} = 13.21\%$$

The dividend per share of 25.09 cent is derived as follows –

$$\frac{\text{Total dividend less preference dividend}}{\text{Number of ordinary shares}}$$

$$\frac{€180{,}000 - €19{,}400}{640{,}000\ \text{shares}} = 25.09\ \text{cent}$$

4. The Dividend Cover

This is the number of times the profit left over to ordinary shareholders covers the dividend paid out to those same shareholders.

The formula is:

$$\frac{\text{Earnings per share}}{\text{Dividend per share}}$$

The earnings per share we have already calculated in Part 2 as 36.97 cent per ordinary share.

The dividend in cent per share is calculated in Part 3 above as 25.09 cent per share.

$$\text{Dividend cover} = \frac{36.97\ \text{cent}}{25.09\ \text{cent}} = 1.47\ \text{times}$$

5. Interest Cover

This is the number of times that the operating profit covers the debenture interest.

The formula is:

$$\frac{\text{Net Profit plus Interest}}{\text{Interest}}$$

$$\frac{€256{,}000 + €16{,}000}{€16{,}000} = 17\ \text{times}$$

Other questions one can be asked in Part A of Question 5 include:
1. Cash purchases or cash sales.
2. Stock turnover and the calculation of the opening stock.
3. The price earnings ratio.
4. The price dividends ratio.
5. The gearing ratio and the effect this has on the appropriation of profit.

SOLUTION B

The analysis section requires at least six points with each one fully developed. The following are the suggested headings to be used for analysis purposes.

The bank manager, Katie Mullen, should grant the loan for the following reasons:

1. Liquidity – liquidity determines whether a company can or cannot pay its current liabilities out of its liquid assets.
The acid test ratio is:

$$\frac{\text{Current assets less closing stock}}{\text{Current liabilities}}$$

$$\frac{€\,330{,}000 - €120{,}000}{€120{,}000} = 1.75 : 1$$

The norm is 1 : 1. The firm is liquid and the position has improved on last year when it was 0.9 : 1. For every €1 in short term debts there is € 1.75 in liquid assets. However the extra interest payments will worsen the liquidity position of the firm in the short-term. At the moment the firm may even be too liquid and should consider reducing its current assets and investing this money in more productive assets. For now the company can pay its immediate short-term debts out of its liquid assets.

2. Profitability – this is measured by the return on capital employed, which has been calculated in Part A above at 20.45 per cent. The firm is profitable because it is earning much more than the return from risk free investments of approximately three per cent. It has also improved on last year's figure of 15 per cent, and it is well above the interest charge of 10 per cent on the new loan. This will please the bank manager because it shows that the company will be able to generate funds to pay the interest. The management is making an efficient use of its resources.

3. Gearing – this is an examination of the long-term capital structure of a firm to find out if the company is financed by debt or by equity. There are a number of formulae that can be used at this point, all fully correct. The one used here is the debt to equity percentage.

$$\frac{\text{Debentures + preference share capital} \times 100}{\text{Ordinary share capital + retained profits}}$$

$$\frac{€320{,}000 + €194{,}000 \times 100}{€640{,}000 + €176{,}000} = 62.99\,\%$$

The firm is lowly geared at 62.99 per cent and the position has improved on last year's figure of 70 per cent. The company is financed more by equity than by debt. Including the new loan the firm is still lowly geared at 87.5 per cent, so the bank will be quite happy to give it a loan of €200,000 for this reason.

The formula debt to capital employed is fully acceptable in the analysis of gearing, however, with this formula the percentage must be less than 50 per cent to be lowly geared.

Interest cover – the present interest cover is 17 times. The company can easily pay its interest charges out of profits, and the situation has improved on last year when the cover was 12 times. However the extra loan will worsen the interest cover somewhat. The bank will be very happy about the company's ability to meet its interest charges.

4. Purpose – the loan is for expansion purposes and the bank will be very pleased with this because this will generate extra revenue, which can be used to service the loan. However the bank would like to know what type of expansion the company is considering as there is a credit squeeze and the bank must prioritise the really profitable projects it intends investing in.

5. Security – the bank will want to know the real market value of the fixed assets in case the company defaults on the loan. At the moment the cost of the fixed assets is €990,000 and there are already debentures secured against these fixed assets of €320,000. This leaves €670,000 left over, as security against a new loan of €200,000 and this seems adequate to satisfy the bank's needs for security. As well as this the company has investments that are valued at €150,000 having cost the company €130,000. However we need more information on the present debentures because we don't know whether the security is fixed or floating nor do we know whether the fixed assets have adequate depreciation, and is there a figure for goodwill included.

6. Dividend cover – this shows how much of the profits are retained for future expansion purposes and the repayments of loans. These figures have been calculated in Part A above. The cover is 1.47 times – out of an earnings per share of 36.97 cent the company is paying dividends of 25.09 cent and retaining 11.88 cent. The bank will not be very pleased with this because the company is not retaining enough of the profits for future expansion purposes, or for the setting aside, into a reserve fund, to go towards the repayment of the loan. Last year's cover was two times and this means the firm is retaining less of its profits this year compared to last year.

Other points that could be discussed include market price, sector, investment policy and so on. Be very careful in the analysis section because in 2007 and in 2012 students were given the projected ratios for next year rather than last year's figures.

Franciscan friar and mathematician Luca Pacioli (1445 - c.1514), known as the father of accounting, teaching the Duke of Urbino Guidobaldo Da Montefeltro. The painting is attributed to Jacopo de Barbari. Pictured on the table are various geometrical tools. PHOTOGRAPH: GETTY IMAGES

How to get your A1

Accounting

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From: Enfield, Co Meath
Studying: Pharmacy, Trinity College Dublin
School: The Institute of Education

Continuous Practice

I sat in your place this time last year, reading article after article trying to pick up any hints or tips that I could before the exams started in June. I arrived in the institute at the start of sixth year with some knowledge of accounting, scoring average grades, but with the support of some outstanding teaching and continuous practice I was confident I could achieve a high grade.

The most important advice I can give you is to practice. The adjustments for each question are often repeated and continuous practice will increase your efficiency at them, which will help you manage your time when you're sitting the exam next June. It's important to have a method for approaching each question. My method was to complete all the adjustments on a separate page before filling out the accounts. The adjusted figures can then be easily transferred into the accounts. Present all the adjustments neatly as marks can be given for these workings.

Recommended Questions

There are a few questions that I would highly recommend students to answer. Question 1 each year is always a final account. In the past, it has always been a company, sole trader or manufacturing final account. I would advise knowing all the adjustments for each of these question types, because it often happens that an adjustment that appears in the manufacturing final account can appear in the company or sole trader final account and vice versa. Become familiar with the layout of these accounts, as marks can be lost for entering items under the wrong headings.

Question 5 – interpretation of accounts. This is another very important question as it is guaranteed to appear every year. The key to succeeding in this question is to learn off the ratios. Once you know these and understand what they mean, you can answer the entire question without any problems. When commenting on the performance of the business in Part B, always compare the figures of the previous year with the current year to achieve full marks.

Be Good in Theory

Theory is one part of the paper students should not neglect. You should start learning the theory now. However if you struggle on the day, make sure to write down some points irrespective of how basic they may appear, as you may be awarded some marks.

Again, the best advice I can give you is to practice by doing questions. From now until June I recommend doing five questions per week, choosing each question from a different part of the course. The more proficient and confident you are sitting the paper, the better you will do. Best of luck!

Trinity College Dublin. PHOTOGRAPH: DARA MAC DÓNAILL

CALCULATE AND BE DAMNED

PUBLISHED ACCOUNTS

Another typical Section 1 or 2 question is a published accounts Question.

The following is the trial balance of K Brovko F Kelleher PLC as at 31/12/2012. The company has an Authorised Capital of 800,000 Ordinary shares at €1 each and 450,000 10 per cent preference shares at €1 each. The accountant Amy Bennet has prepared the following trial balance:

	€	€
Purchases and Sales	810,000	1,470,000
Debtors and Creditors	85,000	45,000
Rental Income		26,000
12% Debentures 2015		200,000
Interest on Debentures	18,000	
Patents	120,000	
Advertising	46,000	
Buildings at Cost	450,000	
Buildings Accumulated Depreciation		27,000
Wages and Salaries	60,000	
Dividends paid	35,000	
8% Investments	180,000	
Investment Income		10,000
Distribution Costs	44,000	
Administration Costs	30,000	
Profit on Sale of Land		150,000
VAT	18,000	
PAYE		35,000
Bank	341,000	
Bad Debts Provision 1/1/2012		12,000
Profit and Loss Balance at the 1/1/2012		4,000
Stock at the 1/1/2012	40,000	
Issued Ordinary Share Capital		250,000
Issued Preference Share Capital		100,000
Vans at Cost	70,000	
Accumulated Depreciation on Vans		18,000
	2,347,000	2,347,000

The following additional information is also relevant:

1. Stock at the 31/12/2012 is €45,000.
2. Wages and salaries are to be allocated 80 per cent to administration and 20 per cent to distribution.
3. Provision is to be made for debenture interest due and investment income due, directors fees €25,000, auditors fees of €21,000, corporation tax of €77,000.
4. Depreciation on buildings is to be provided for at the rate of two per cent per annum straight line and delivery vans at the rate of 20 per cent reducing balance.
5. During the year land that had cost €200,000 was sold for €350,000.
6. The patent is being written off over 10 years. The writing off commenced in 2008 and is to be included in the cost of sales.
7. At the end of the year it was decided to revalue the company buildings to €600,000. The company wishes to incorporate this value in this year's accounts.
8. The company is being sued by a customer for damage caused by one of its products. Its legal advisers state that it is unlikely to be liable for damages totalling €60,000.
9. Included in administation expenses is discount received of €17,000.

YOU ARE REQUIRED:

a) To prepare the published profit and loss account for the year ended 31/12/2012 and a balance sheet as at that date in accordance with the Companies Acts and appropriate accounting standards showing the following notes:

1. Accounting policy note for tangible fixed assets and stock.
2. Operating profit.
3. Dividends.
4. Interest payable.
5. Tangible fixed assets.
6. Contingent Liability.

b) (i) Explain the term 'qualified report'.
(ii) Outline briefly, four agencies that regulate the production, content and presentation of company financial statements.

SOLUTION
(A)
Profit and loss account for year ending 31/12/2012:

	Notes	€
Turnover		1,470,000
Cost of Sales		(825,000)
Gross Profit		645,000
Distribution Costs		(112,400)
Administration Expenses		(150,000)
Operating Income		43,000
Operating Profit	2	425,600
Income from Financial Assets		14,400
Profit on Sale of Land		150,000
Interest Payable	4	(24,000)
Profit on Ordinary Activities before Tax		566,000
Corporation Tax		(77,000)
Profit on Ordinary Activities after Tax		489,000
Dividends Paid	3	(35,000)
Retained Profit		454,000
Profit and Loss Balance at the 1/1/2012		4,000
Profit and Loss Balance at the 31/12/2012		458,000

Balance Sheet as at 31/12/2012

	Notes	€	€	€
Fixed Assets				
Intangible Assets				100,000
Tangible Assets	5			641,600
Financial Assets				180,000
				921,600
Current Assets				
Stocks			45,000	
Debtors			95,400	
Bank			341,000	
			481,400	
Creditors amounts falling due in less than one year				
Creditors		45,000		
Other Creditors		52,000		
Taxation		112,000	(209,000)	
Net Current Assets				272,400
Total Assets less Current Liabilities				1,194,000
Financed By				
Ordinary Share Capital			250,000	
Preference Share Capital			100,000	
Revaluation Reserve			186,000	
Retained Profits			458,000	
			994,000	
Creditors amounts falling due in more than one year				
12% Debentures 2015			200,000	
				1,194,000

1. Accounting policy notes – buildings were revalued at the end of the year at €600,000 and have been included in the accounts at this revalued amount. Depreciation is calculated in order to write off the value of the tangible assets over their estimated useful economic life as follows: buildings two per cent per annum straight line and vans 20 per cent per annum reducing balance. Stocks are valued on a first in first out basis at the lower of cost and net realisable value.
2. The operating profit of €425,600 is arrived at after charging the following:
– Depreciation on tangible fixed assets €19,400, directors fees €25,000,
– Auditors fees €21,000, patents amortised €20,000.
3. Dividends:
– Preference dividend paid €10,000; 10cent per share.
– Ordinary Dividend paid €25,000; 10 cent per share.
4. Interest payable – the interest payable on the 12 per cent debentures €200,000 (repayable in 2015) is €24,000.
5. Tangible fixed assets

	Land	Buildings	Vans	Total
	€	€	€	€
Cost 1/1/12	200,000	450,000	70,000	720,000
Disposal	(200,000)			(200,000)
Revaluation		150,000		150,000
Cost 31/12/12	0	600,000	70,000	670,000
Accum. Deprec 1/1/12		27,000	18,000	45,000
Charge for 2012		9,000	10,400	19,400
Revaluation		(36,000)		(36,000)
Accum. Deprec 31/12/12	0	0	28,400	28,400
Net Book Value 1/1/12	200,000	423,000	52,000	675,000
Net Book Value 31/12/12	0	600,000	41,600	641,600

6. Contingent liability – the company is being sued in the courts by a customer for damages caused by a faulty product. The company's legal advisers have said that the company is unlikely to be liable. The maximum liability, in the unlikely event that the court case is lost, is €60,000.

(B)
A qualified report is when an auditor, in her opinion, is not satisfied or is unable to conclude that:
1. The financial statements give a true and fair view of the state of

affairs of the company at the end of the year and of its profit and loss account for the year.
2. The financial statements are prepared in accordance with the Companies Acts.
3. All the information necessary for an audit was available.
4. The net assets are more than 50per cent of the called up capital.

The agencies are:
1. The Government through its company legislation.
2. The accounting profession through its financial reporting standards and its statements of standard accounting practise.
3. The EU through its accounting directives.
4. The stock exchange through its listing rules. Public limited companies must report twice a year to the stock market.

WORKINGS:

Cost of Sales:
€40,000 + €810,000 – €45,000 + €20,000 (patents)

Distribution Costs:
€44,000 + €46,000 (advertising) + €10,400 (depreciation on vans) + €12,000 (wages and salaries)

Administration Costs:
€30,000 + €17,000 (discount received) + €48,000 (wages and salaries) + €9,000 (depreciation on buildings) + €25,000 (directors fees) + €21,000 (auditors fees)

Operating Income:
€17,000 (discount received) + €26,000 (rental income)

Investment Income:
8% x €180,000

Interest Payable:
12% x €200,000

Debtors:
€85,000 (debtors) – €12,000 (bad debts provision) + €18,000 (VAT) + €4,400 (14,400 – 10,000 (investment income due))

Other Creditors:
€25,000 (directors fees) + €21,000 (auditors fees) + €6,000 (interest due)

Revaluation Reserve:
€150,000 + €36,000

JOIN THE CLUB

A popular Section 1 or 2 Question is a club accounts question, which would score 60 or 100 marks. Students should complete this question in approximately 26 or 45 minutes depending on whether it is in Section 1 or 2.

CLUB ACCOUNTS SAMPLE QUESTION

Included among the assets and liabilities of the T SheridanI Williams Football Club, on the 1/1/2012 were the following: buildings at cost €680,000; equipment at cost €90,000; bar stock €2,000; creditors for supplies to the bar €3,200; eight per cent investments €40,000; subscriptions received in advance €2,000; stock of heating oil €900; investment income due €300; bar debtors €420; wages due €900; levy reserve fund €50,000; life membership €20,000.

The following is a receipts and payments account for the year ended 31/12/2012:

Receipts and Payments Account

	€		€
Investment Income	3,300	Balance at Bank	17,200
Subscriptions	223,000	Equipment	20,000
Bar receipts	75,000	Purchases for the bar	42,000
Annual Sponsorship	30,000	Light and heat	3,000
Catering receipts	10,700	Insurance	7,000
Sale of equipment (cost €5,000)	3,500	New extension	200,000
		Repayment of 60,000 loan on 31/10/2012 together with 18 months interest	65,400
		Prize bonds	3,000
		Wages and salaries	32,000
		Catering costs	6,900
Balance	51,000		
	396,500		396,500

You are given the following additional information:
1. Closing stock of the bar at 31/12/2012 is €3,700(this includes a stock of heating oil of €400).
2. Equipment owned on the 31/12/2012 is to be depreciated at the rate of 20 per cent of cost per annum and buildings at the rate of two per cent per annum on cost.
3. Bar debtors and creditors, at the 31/12/2012 amounted to €480 and €2,800 respectively.
4. Subscriptions includes:
   a) One new life member bringing the total life members to 11.
   b) Subscriptions received for 2013 of €500.
   c) Levy on 10 members of €250 each due for 2011.
   d) Levy on 100 members of €250 each for 2012.
5. Electricity due at the 31/12/2012 is €500.
6. Life membership is to be written off over a five year period beginning in 2012.

You are required to:
a) Calculate the accumulated fund on the 1/1/2012.
b) Calculate the profit/loss of the bar for the year ended 31/12/2012.
c) Prepare the income and expenditure account for the year ended 31/12/2012.
d) Prepare the balance sheet as at 31/12/2012.
e) Calculate and comment on the bar profit as a percentage of the sales.

SOLUTION

a) Balance Sheet as at 31/12/2012

	€	€	€
Fixed Assets	**Cost**	**Depreciation**	**Net**
Buildings	880,000	17,600	862,400
Equipment	105,000	21,000	84,000
	985,000	38,600	946,400
Investments			40,000
			986,400
Current Assets			
Stocks		3,700	
Debtors		480	
Prize Bonds		3,000	
Investment Income due 3,200 – (3,300-300)		200	
		7,380	
Current Liabilities			
Creditors	2,800		
Subscriptions prepaid	500		
Electricity due	500		
Bank overdraft	51,000	(54,800)	(47,420)
			938,980
Financed By			
Accumulated Fund		660,420	
Levy reserve fund(50,000 + 25,000)		75,000	
Excess of income		185,960	
			921,380
Long term liabilities			
Life members			17,600
			938,980

b) Bar Trading Account for the year ended 31/12/2012

	€	€
Sales (75,000 – 420 + 480)		75,060
Cost of Sales		
Opening Stock	2,000	
Purchases (42,000 – 3,200 + 2,800)	41,600	
	43,600	
Closing Stock (3,700 – 400)	(3,300)	(40,300)
Bar Profit		34,760

c) Income and Expenditure Account for the year ended 31/12/2012

	€	€
Income		
Bar Profit		34,760
Investment Income 8% of 40,000		3,200
Subscriptions Note 2 (223,000 + 2,000 -2,000- 500 - 2,500 - 25,000)		195,000
Catering profit		3,800
Annual sponsorship		30,000
Life member subscriptions		4,400
		271,160
Expenditure		
Light and Heat 3,000 + 900 – 400 +500	4,000	
Loss on sale of equipment	1,500	
Interest on the Loan 5,400 ÷ 18 months x 10 **Note 1**	3,000	
Insurance	7,000	
Wages 32,000 – 900_	31,100	
Depreciation Equipment 105,000 x 20%	21,000	
Depreciation Buildings 880,000 x 2%	17,600	(85,200)
Excess of Income		185,960

d) Accumulated Fund at 1/1/2012

	€	€
Assets 1/1/2012		
Buildings		680,000
Equipment		90,000
Stock		2,000
Investments		40,000
Stock of oil		900
Levy due		2,500
Investment income due		300
Debtors		420
		816,120
Liabilities 1/1/2012		
Bank overdraft	17,200	
Levy reserve fund	50,000	
Life membership	20,000	
Wages due	900	
Loan	60,000	
Interest due on the loan **Note 1**	2,400	
Subscriptions prepaid	2,000	
Creditors	3,200	(155,700)
Accumulated Fund 1/1/2012		**660,420**

Note 1: The interest due at the 1/1/2012 is calculated by subtracting €65,400 and the loan of €60,000 to arrive at a figure of €5,400. This is the total interest for 18 months of which eight months are due at the 1/1/2012. Divide €5,400 by 18 months and multiply by eight months and you get €2,400. Subtract €5,400 and €2,400 and you get €3,000 which is the interest for the 10 months of 2012 and this is to be entered as an expense in the income and expenditure account.
Note 2: The subscriptions figure of €195,000 is calculated by taking the base figure of €223,000 adding on the prepaid at the 1/1/2012 of €2,000 to get €225,000. Then go down to adjustment number 4 and subtract the one new life member of €2,000 to get €223,000. Next subtract the subs prepaid at the 31/12/2012 of €500 to get €222,500. Next subtract the levy for 2011 of €2,500 and the levy for 2012 of €25,000 and you arrive at the final figure to be sent to the income and expenditure account of €195,000.

d) The bar profit as a percentage of sales is 46.31 per cent. This compares favourably with other profit making private enterprises. It indicates that the management has a tight control on cash takings and stock. Management is making sure that there is little pilferage or obsolescence of stocks. We would like to see last year's profit percentage figure to determine if the profit percentage is improving or worsening. Management should make a decision on whether to expand the square footage of the bar.

MAKING ADJUSTMENTS

TEST YOURSELF
Final Account Adjustments

Students who are not familiar with the adjustments in Question 1 should avoid this question and opt for the two 60 mark question alternative instead. The following are a number of typical adjustments to the trial balance and students should now test themselves on these. The answers will be given further on down in the article.

ADJUSTMENT 1 – GOODS IN TRANSIT

Trial Balance	Debit	Credit
	€	€
Purchases	650,000	
Creditors		85,500

Stock of trading goods at the 31/12/2012 is €72,500. No record had been made in the books for goods in transit on the 31/12/2012. The invoice for these goods had been received showing the recommended retail selling price of €7,000 which is cost plus 25 per cent.

Calculate the following:
1. The purchases figure to be entered in the trading account for 2012.
2. The closing stock figure to be entered in the trading account for 2012 and the balance sheet as at 31/12/2012.
3. The creditors figure in the balance sheet as at 31/12/2012.

ADJUSTMENT 2 - SALE OF FIXED ASSETS AND DEPRECIATION

Trial Balance	Debit	Credit
	€	€
Vans at cost 1/1/2012	172,000	
Accumulated Depreciation on Vans 1/1/2012		78,000
Purchases	620,000	

Provide for depreciation on vans at the rate of 20 per cent of cost from the date of purchase to the date of sale.

Note:
On the 30/9/2012 a van that had cost €60,000 on the 1/6/2010 was traded in against a new van that cost €84,000. An allowance of €22,000 was given on the old van. The cheque for the net amount of this transaction was incorrectly treated as a purchase of trading goods. This was the only entry made in the books in respect of this transaction.

Calculate the following:
1. The Vans at cost figure in the balance sheet at 31/12/2012.
2. The depreciation expense in the profit and loss account for 2012.
3. The profit/loss on the disposal of the old van sent to the profit and loss account.
4. The accumulated depreciation on vans in the balance sheet at the 31/12/2012.
5. The purchases figure in the trading account for 2012.

ADJUSTMENT 3 - SALE OR RETURN

Trial Balance	Debit	Credit
	€	€
Sales		935,000
Debtors	94,400	

Stock of trading goods at the 31/12/2012 is €92,000. It was discovered that finished goods that cost €8,000 to produce were invoiced to a customer on a sale or return basis.

These goods had been incorrectly entered in the accounts as a credit sale at cost plus 20per cent.

Calculate the following:
1. The sales figure in the trading account for 2012.
2. The debtors figure in the balance sheet as at 31/12/2012.
3. The closing stock figure in the trading account for 2012 and in the balance sheet as at 31/12/2012.

ADJUSTMENT 4 – BANK RECONCILIATION

Trial Balance	Debit	Credit
	€	€
Bank		5500
Creditors		81,000
Debtors	73,900	
6% Investments 1/5/2012	180,000	
Investment income received		1800

The bank balance in the company's accounts, above, does not agree with the bank statement that arrives on the 31/12/2012, which shows a credit balance of €4,040.

A number of discrepancies have arisen as follows:

1. Investment income of €2,700 has been received directly into our bank branch.

2. A cheque for €780 issued to a supplier had been entered in the books as €870.

3. A credit transfer of €750 had been paid direct to the firm's bank branch on behalf of a debtor who has recently been declared bankrupt. This represents a first and final payment of 30 cent in the euro.

4. A cheque for fees of €6,000 issued to the auditors had not been presented at the bank for payment.

Calculate:
1. The bank balance to be entered in the balance sheet at the 31/12/2012.
2. The investment income figure in the profit and loss account for 2012.
3. The investment income due to be entered in the balance sheet as at 31/12/2012.
4. The creditors figure to be entered in the balance sheet as at 31/12/2012
5. The debtors figure to be entered in the balance sheet as at 31/12/2012.
6. The bad debts expense to be recorded in the profit and loss account for 2012.

ADJUSTMENT 5 - ERROR INVOLVING VAT

Trial Balance	Debit	Credit
	€	€
Buildings at cost	900,000	
VAT		4,300

A new building was purchased during the year for €200,000 plus VAT at 12.5 per cent. The amount paid to the seller was entered in the buildings account. The correct entry was made in the bank account but no entry was made in the VAT account.

Calculate the following:
1. The buildings figure in the balance sheet as at 31/12/2012.
2. The VAT figure in the balance sheet as at 31/12/2012.

ADJUSTMENT 6 - PATENTS

Trial Balance	Debit	Credit
	€	€
Patents (incorporating 3 months investment income)	60600	
6% Investments 1/6/2012	160000	

Patents which incorporates three months investment income are to be written off over a five year period commencing in 2012.

Calculate:
1. The patents written off in the profit and loss account for 2012.
2. The patents figure to be entered in the balance sheet as at 31/12/2012.
3. The investment income figure to be entered in the profit and loss account for 2012.
4. The investment income due to be entered in the balance sheet at 31/12/2012.

SOLUTION TO FINAL ACCOUNT ADJUSTMENTS

Adjustment 1:
1. Purchases – €655,600 (650,000 + 5,600)
2. Closing stock – €78,100 (72,500 + 5,600)
3. Creditors – €91,100 (85,500 + 5,600)

Adjustment 2:
1. Cost of vans – €196,000 (17,2000 + 84,000 – 60,000)
2. Depreciation for 2012 – €35,600 (9,000 + 22,400 + 4,200)
3. Loss on disposal – €10,000 (60,000 – 28,000 – 22,000)
4. Accumulated depreciation at 31/12/2012 – €85,600 (78,000 + 35,600 – 28,000)
5. Purchases for 2012 – €558,000 (620,000 – 62,000)

Adjustment 3:
1. Sales – €925,400 (935,000 – 9,600)
2. Debtors – €84,800 (94,400 – 9,600)
3. Closing stock – €100,000 (92,000 + 8,000)

Adjustment 4:
1. Bank – €1,960 of an overdraft (5,500 – 2,700 – 90 – 750) or (4,040 – 6,000)
2. Investment income – €7,200 (180,000 at six per cent for 8 months)
3. Investment income due – €2,700 (7,200 – 1,800 – 2,700)
4. Creditors – €81,090 (81,000 + 90)
5. Debtors – €71,400 (73,900 – 750 – 1,750)
6. Bad debts – €1,750 (750 ÷ 30 x 70)

Adjustment 5:
1. Buildings – €875,000 (900,000 – 25,000)
2. VAT – €20,700 as a current asset (4,300 as a liability less 25,000 VAT refund due)

Adjustment 6:
1. Patents written off – €12,600 (60,600 + 2,400 ÷ 5)
2 .Patents in the balance sheet – €50,400 (63,000 – 12,600)
3. Investment income – €5,600 (160000 at six per cent ÷ 12 x 7)
4. Investment income due – €3,200 (5,600 – 24,00)

MARGINAL VERSUS ABSORPTION COSTING

SECTION 3

A typical question in Section 3 is on marginal costing and the differences between it and absorption costing.

E Bluett S Epstein Ltd produces 16,000 units of a single product during the year ended 31/12/2012, where 12,000 units of the same product were sold at €12 per unit.

The production costs were as follows:

Direct materials – €1 per unit

Direct labour – €1.60 per unit

Variable overheads – €1 per unit

Fixed overhead costs for the year are €6000

Prepare the profit and loss statements under marginal and under absorption costing.

SOLUTION

Marginal costing profit and loss statement for year ending 31/12/2012

	€	€
Sales (12,000 units @ €12)		144,000
Less Variable Costs		
Materials (16,000 @ €1)	16,000	
Labour(16,000 @ €1.6)	25,600	
Variable Overhead (16,000 @ €1)	16,000	
	57,600	
Less Closing Stock (57,600÷16,000x4,000)	(14,400)	(43,200)
Contribution		100,800
Fixed Costs		(6,000)
Profit		94,800

Absorption costing profit and loss statement for the year ending 31/12/2012

	€	€
Sales		144,000
Less Costs		
Materials	16,000	
Labour	25,600	
Variable Overheads	16,000	
Fixed Overheads	6,000	
	63,600	
Closing Stock (63,600÷16,000 x 4,000)	(15,900)	(47,700)
Profit		96,300

The profit figures are different as closing stock is valued differently. Closing stock under marginal costing will have a lower value than under absorption costing because fixed costs are not included with the closing stock. Profit under marginal costing is €1,500 lower because the closing stock is €1,500 lower.

Absorption costing is used when preparing financial statements as it agrees with standard accounting practices, which match costs and revenues of the same period.

ANOTHER TYPICAL SECTION 3

STOCK CONTROL AND FIFO

C Byrne Ltd. is a retail store in Blessinggram that buys and sells one product. The following information relates to the purchases and sales for the year 2012.

Period	Credit Purchases	Credit Sales	Cash Sales
1/1/12 to 31/3/12	6,200 units @ €6	1,800 units @ €11	3,000 units @ €12
1/4/12 to 30/6/12	6,800 units @ €7	2,200 units @ €12	2,800 units @ €11
1/7/12 to 30/9/12	7,200 units @ €8	2,600 units @ €12	2,800 units @ €12
1/10/12 to 31/12/12	3,200 units @ €9	2,400 units @ €14	2,200 units @ €14

On the 1/1/2012 there was an opening stock of 3,000 units at €6 each.

You are required to:
(a) Calculate the closing stock, using the first in first out method.
(b) Prepare a trading account for the year ending 31/12/2012.

SOLUTION

a) The closing stock in units is the opening stock plus the total purchases less the total sales as follows:

3,000 units (opening stock) plus 23,400 units (total purchases) less 19,800 units (total sales) and this leaves us with an answer for closing stock of 6,600 units.

Now place a monetary value on these 6,600 units and the easiest way to do this is to take the purchase column above and work from the bottom up:

The closing stock value is 3,200 units at €9 = €28,800 plus 3,400 units at €8 = €27,200 giving a combined figure of €56,000.

b) Trading Account for year ending 31/12/2012

	€	€
Sales		242,200
Opening Stock	18,000	
Purchases	171,200	
	189,200	
Closing Stock	(56,000)	(133,200)
Gross Profit		109,000