POA
Summary Notes

1. Accounting Theories
2. Definitions
3. Double entry/ Journals
4. Formulas
5. Financial Statements
6. POA theory questions

1. Accounting Theories

- state the general explanation of each accounting theory
- explain how each accounting theory is applied in specific scenarios

<table>
<tr><th>Accounting theory</th><th>General explanation</th><th>Specific application</th></tr>
<tr><td>Objectivity</td><td>Accounting information recorded must be supported by reliable and verifiable evidence so that financial statements will be free from opinions and biases.</td><td rowspan="3">A source document provides evidence (objectivity theory) to capture occurrence of a transaction. The transaction is recorded at the original cost that it occurred (historical cost theory).</td></tr>
<tr><td>Historical cost</td><td>Transactions should be recorded at their original cost.</td></tr>
<tr><td>Monetary</td><td>Only business transactions that can be measured in monetary terms are recorded.</td></tr>
<tr><td>Accounting entity</td><td>The activities of a business are separate from the actions of the owner. All transactions are recorded from the point of view of the business.</td><td>Explain how the accounting entity theory is applied to account for capital and drawings.

According to the accounting entity theory, only transactions that affect the business are recorded while transactions relating to the owner that do not affect the business are not recorded.</td></tr>
<tr><td>Accounting period</td><td>The life of a business is divided into regular time intervals.</td><td rowspan="2">As businesses are assumed to operate forever (going concern theory), financial statements should be prepared at regular time intervals (accounting period theory) to provide timely information for stakeholders to make decisions.</td></tr>
<tr><td>Going concern</td><td>A business is assumed to have an indefinite economic life unless there is credible evidence that it may close down.</td></tr>
</table>

Accounting theory	General explanation	Specific application
Revenue Recognition	Revenue is earned when goods have been delivered or services have been provided.	*Explain the revenue recognition theory behind the accounting of revenue and other income.* According to the revenue recognition theory, • revenue is recognised when goods are sold and delivered. • service fee revenue is recognised when services have been provided.
Accrual basis of accounting	Business activities that have occurred, regardless of whether cash is paid or received, should be recorded in the relevant accounting period.	*Explain the accrual basis of accounting behind the accounting of revenue and other income.* Based on the accrual basis of accounting, • service fee revenue received before services are provided should not be recognised until the services are provided to the customer regardless of whether payment has been received or not. • other income that relate to services that have been provided but not received must be recorded as other income in the current financial period. *Explain the accrual basis of accounting behind the accounting of other expenses.* According to the accrual basis of accounting, other expenses must be recognised in the period the services have been used, regardless of whether they have been paid for or not.

Accounting theory	General explanation	Specific application
Matching	Expenses incurred must be matched against income earned in the same period to determine the profit for that period.	*Explain the matching theory behind the accounting of cost of sales and other expenses.* According to the matching theory • the cost incurred to buy inventory must be matched against the sales revenue earned from selling the inventory in the same accounting period to determine the gross profit for that period. • other costs incurred during the operation of a business to generate revenue and other income must be matched against revenue and other income earned in the same accounting period to determine the profit for that period. *Explain the accounting of depreciation expense in relation to the matching theory.* When a business uses non-current assets to generate income, a portion of the original cost of the non-current assets has to be recorded as depreciation expense. It will be matched against the income earned in the same financial period (matching theory) to arrive at the profit for the period. *Explain the accounting of impairment loss on trade receivables using the matching theory.* The change in estimated amount of debts likely to be uncollectible will be reported as impairment loss on trade receivables (expense) in the same financial period as credit sales (income) was earned. The matching of expenses incurred to the income earned is in accordance to the matching theory.

Accounting theory	**General explanation**	**Specific application**
Consistency	Once an accounting method is chosen, this method should be applied to all future accounting periods to enable meaningful comparison.	*Explain the accounting of depreciation expense in relation to the consistency theory.* Unless there is a change of usage pattern, a business should use the same method of depreciation (consistency theory) and rate of depreciation every financial period to enable meaningful comparison of the net book value of non-current assets over time.
Materiality	Relevant information should be reported in the financial statements if it is likely to make a difference to the decision-making process.	*Explain the treatment of capital expenditure and revenue expenditure in relation to the materiality theory.* If the amount spent on a non-current asset is insignificant to decision-making when compared to the size of the income, profit, assets or equity of the business, it does not need to be classified as a capital expenditure and be reported as a non-current asset. Instead, it can be classified as revenue expenditure and be reported as an expense. This is in accordance with the materiality theory.

Accounting theory	**General explanation**	**Specific application**
Prudence	The accounting treatment chosen should be the one that least overstates assets and profits and least understates liabilities and losses.	*Explain the valuation of inventory in relation to prudence theory.* According to the prudence theory, inventory is valued at the lower of cost and net realisable value to ensure that inventory is not overstated. *Explain the accounting of allowance for impairment of trade receivables using the prudence theory.* The estimated amount of debts likely to be uncollectible will be reported as allowance for impairment of trade receivables and shown as a deduction against the book value of trade receivables. This is to ensure that trade receivables balance is not overstated (prudence theory) and reflects the net amount that is collectible.

2. Definitions

- Define assets, liabilities, equity, income and expenses and their examples

Assets: resources a business owns or controls that are expected to provide future benefits.

Non-current assets		**Current assets**	
Office equipment	electronic appliances used in office (e.g. computers, printers)	Cash at bank	cash deposited with the bank
Motor vehicles	vehicles for business use (e.g. vans, trucks)	Cash in hand	physical cash kept by the business
Fixtures and fittings	furniture and items that are attached to a building by nail or screw for business use (e.g. tables, shelves)	Inventory	goods bought by the business to sell to its customers
Machinery	heavy-duty electronic appliances used to perform complex tasks (e.g. drills)	Trade receivables	revenue earned but not yet collected from credit customers
Premises / Property	buildings and land owned and used by the business	Income receivable	income earned but not yet collected from credit customers
		Prepaid expense	expenses not incurred but paid in advance
		Allowance for impairment of trade receivables	estimated amount of debts likely to be uncollectible from credit customers
		Supplies	items used by employees to provide service to its customers

Liabilities: Obligations owed by a business to others that are expected to be settled in the future

Non-current liabilities		Current liabilities	
Loan	money borrowed from banks and other lenders	Trade payables	amounts owed to credit suppliers after buying goods and other assets
Mortgage loan	money borrowed using collaterals	Bank overdraft	money borrowed, when the bank account is overdrawn and the available balance goes below zero
		Income received in advance	income not earned but collected in advance
		Expense payable	expense incurred but not yet paid to credit suppliers
		Dividends payable	a portion of retained earnings that has been declared but not yet paid to shareholders

Equity: Claim by the owner(s) on the net assets of a business

Owner's equity		Shareholders' equity	
Capital	resources contributed by the owner for business use	Share capital	cash raised by issuing shares to investors
Profit or loss for the period	the difference between the income earned and the expenses incurred within one accounting period	Retained earnings (or accumulated losses)	accumulation of profits and losses that has not been distributed to shareholders yet since operation
Drawings	assets taken from a business for the owner's personal use	Dividends	a portion of retained earnings that is distributed to shareholders

Income: Amounts earned from the activities of a business

Service fee revenue	money earned from providing services (e.g. legal fee revenue)
Sales revenue	• money earned from selling goods • selling price of goods that have been sold
Sales returns**	selling price of goods that have been returned by customers
Discount received	cash discount received from credit suppliers for making early payment
Interest income (on deposit)	amount earned on the cash held in the business bank account
Rent income	money earned from letting out part of the shop/ office space
Commission income	amount earned for making sales or closing deals for third parties

Expenses: Costs incurred to earn income in the same accounting period

Cost of sales	cost price of goods that have been sold
Discount allowed	cash discount given to credit customers for making early payment
Interest expense (on loan)	charges for borrowing money from banks or other lenders
Rent expense	cost to utilise a property or location for an office, shop or storage space
Utilities expense	cost to use electricity, water, waste disposal, heating, and sewage
Insurance expense	cost to protect property, inventory and workers of the business
Wages and salaries expense	cost to compensate employees for their time and services
Advertising expense	cost to promote its products, brands, and image via various media channels
Depreciation expense	a portion of the original cost of the non-current asset allocated over its useful life
Impairment loss on trade receivables	change (increase/decrease) in estimated amount of debts likely to be uncollectible from credit customers
Impairment loss on inventory	amount of potential loss (decrease) when cost of goods falls below its net realisable value

3. Double entry/ Journals

<table>
<tr><th>Record transactions</th><th>Account to be debited</th><th>Account to be credited</th></tr>
<tr><td>Obtain loan</td><td>Cash at bank
+A</td><td>Loan
+L</td></tr>
<tr><td>Repayment of loan</td><td>Loan
-L</td><td>Cash at bank
-A</td></tr>
<tr><td rowspan="2">Purchase of non-current asset (capital expenditure)
• on credit
• using cash / cheque</td><td rowspan="2">Non-current asset
+A</td><td>Trade payable
+L</td></tr>
<tr><td>Cash in hand /
Cash at bank
-A</td></tr>
<tr><td rowspan="2">Purchase of goods
• on credit
• using cash / cheque</td><td rowspan="2">Inventory
+A</td><td>Trade payable
+L</td></tr>
<tr><td>Cash in hand /
Cash at bank
-A</td></tr>
<tr><td rowspan="2">Return of goods to credit suppliers
• previously purchased on credit
• refund cash / cheque</td><td>Trade payable
-L</td><td rowspan="2">Inventory
-A</td></tr>
<tr><td>Cash in hand /
Cash at bank
+A</td></tr>
<tr><td>Payment to credit suppliers</td><td>Trade payable
-L</td><td>Cash in hand /
Cash at bank
-A</td></tr>
<tr><td>Received cash discount from credit suppliers</td><td>Trade payable
-L</td><td>Discount received
+I</td></tr>
</table>

<table>
<tr><th>Record transactions</th><th>Account to be debited</th><th>Account to be credited</th></tr>
<tr><td rowspan="2">Sale of goods
• on credit
• received cash / cheque</td><td>Trade receivables
+A</td><td rowspan="2">Sales revenue
+I</td></tr>
<tr><td>Cash in hand /
Cash at bank
+A</td></tr>
<tr><td>Cost price of goods sold</td><td>Cost of sales
+Ex</td><td>Inventory
-A</td></tr>
<tr><td rowspan="2">Return of goods by credit customers
• previously sold on credit
• refund cash / cheque</td><td rowspan="2">Sales returns
-I</td><td>Trade receivables
-A</td></tr>
<tr><td>Cash in hand /
Cash at bank
-A</td></tr>
<tr><td>Cost price of goods returned</td><td>Inventory
+A</td><td>Cost of sales
-Ex</td></tr>
<tr><td>Collections from credit customers</td><td>Cash in hand /
Cash at bank
+A</td><td>Trade receivables
-A</td></tr>
<tr><td>Gave cash discount to credit customers</td><td>Discount allowed
+Ex</td><td>Trade receivables
-A</td></tr>
<tr><td>Dishonoured cheque</td><td>Trade receivables
+A</td><td>Cash at bank
-A</td></tr>
<tr><td>Withdrew cash discount given</td><td>Trade receivables
+A</td><td>Discount allowed
-Ex</td></tr>
<tr><td>Withdrew from bank as office cash</td><td>Cash in hand
+A</td><td>Cash at bank
-A</td></tr>
<tr><td>Deposit excess cash into bank</td><td>Cash at bank
+A</td><td>Cash in hand
-A</td></tr>
</table>

Adjust accounts	Account to be debited	Account to be credited
Net realisable of goods falls below cost	Impairment loss on inventory +Ex	Inventory -A
Insurance claim on damaged goods	Insurance claim receivable +A	Impairment loss on inventory -Ex
Collection of insurance claim	Cash in hand / Cash at bank +A	Insurance claim receivable -A
Increase in estimated uncollectible debts	Impairment loss on trade receivables +Ex	Allowance for impairment of trade receivables + **contra**-A
Decrease in estimated uncollectible debts	Allowance for impairment of trade receivables - **contra**-A	Impairment loss on trade receivables -Ex
Write-off debts / bankrupt (**confirmed** uncollectible)	Allowance for impairment of trade receivables - **contra**-A	Trade receivables -A
Depreciation of NCA	Depreciation expense +Ex	Accumulated depreciation + **contra**-A

Sale of non-current asset	Account to be debited	Account to be credited
Removal of NCA	Sale of non-current asset	Non-current asset -A
Removal of accumulated depreciation	Accumulated depreciation - **contra**-A	Sale of non-current asset
Collection of sales proceeds	Cash at bank +A	Sale of non-current asset
Transfer gain/loss on sale of NCA • Gain	Sale of non-current asset	Income summary (+ C) (gain)
• Loss	Income summary (- C) (loss)	Sale of non-current asset

Other Expenses	Account to be debited	Account to be credited
Reverse • expenses payables	Expenses payables -L	Other expenses -Ex
• prepaid expenses	Other expenses +Ex	Prepaid expenses -A
Payment for expenses (**revenue** expenditure)	Other expenses +Ex	Cash in hand / Cash at bank -A
Adjust • expenses payables (incurred)	Other expenses +Ex	Expenses payables +L
• prepaid expenses (**not** incurred)	Prepaid expenses +A	Other expenses -Ex
Close other expenses	Income summary	Other expenses

Revenue	Account to be debited	Account to be credited
Reverse service fee revenue received in advance	Service fee revenue received in advance -L	Service fee revenue +I
Sale of services • on credit	Trade receivables +A	Service fee revenue +I
• received cash / cheque	Cash in hand / Cash at bank +A	
Adjust service fee revenue received in advance (**not** earned)	Service fee revenue -I	Service fee revenue received in advance +L
Close service fee revenue	Service fee revenue	Income summary

Other Income	Account to be debited	Account to be credited
Reverse • income received in advance	Income received in advance -L	Other income +I
• income receivable	Other income -I	Income receivable -A
Receipt of cash	Cash in hand / Cash at bank +A	Other income +I
Adjust • income received in advance (**not** earned)	Other income -I	Income received in advance +L
• income receivable (earned)	Income receivable +A	Other income +I
Close other income	Other income	Income summary

Sole Proprietorship	Account to be debited	Account to be credited
Contribution from owner	Any assets +A	Capital +C
Close income summary • Profit • Loss	Income summary	Capital +C (profit)
	Capital -C (loss)	Income summary
Withdrawal by owner for personal use	Drawings +D	Any assets -A
Close drawings	Capital -C	Drawings -D

Private Limited Company	Account to be debited	Account to be credited
Contribution from shareholders	Cash at bank +A	Share capital +C
Close income summary • Profit • Loss	Income summary	Retained earnings +C (profit)
	Retained earnings -C (loss)	Income summary
Declared dividends • But not paid yet • Paid immediately	Dividends +D	Dividends payables +L
	Dividends +D	Cash at bank -A
Close dividends	Retained earnings -C	Dividends -D

4. Formulas

Basic accounting equation	Assets = Liabilities + Equity
Expanded accounting equation (sole proprietorship)	Assets = Liabilities + Owner's equity Assets = Liabilities + Capital + Profit (or – Loss) – Drawings Assets = Liabilities + Capital + (Income – Expenses) – Drawings
Capital	Beginning capital + Additional capital + Profit (or – Loss) – Drawings
Expanded accounting equation (private limited company)	Assets = Liabilities + Shareholders' equity Assets = Liabilities + Share capital + Retained earnings Assets = Liabilities + Share capital + Profit (or – Loss) – Dividends Assets = Liabilities + Share capital + (Income – Expenses) – Dividends
Share capital	Total number of shares issued × Issued price per share ($)
Dividends	Total number of shares issued × Declared dividends per share ($)
Discount	Invoice price = List price – Trade discount Amount paid = Invoiced price – Cash discount (allowed / received)

Depreciation expense (Straight line method)	$\frac{\text{Cost} - \text{Scrap value}}{\text{Estimated useful life}}$ **OR** $\text{Rate of depreciation (\%)} \times (\text{Cost} - \text{Scrap value})$ Scrap value: amount that the business can receive at the end of the estimated useful life of the non-current asset
Depreciation expense (Reducing balance method)	$\text{Rate of depreciation (\%)} \times \text{Net book value}$ Net book value = Cost – Accumulated depreciation
Gain (or loss) on sale of non-current asset	Sales proceeds – Net book value
Allowance for impairment of trade receivables	Estimated percentage (%) × Ending trade receivables balance
Impairment loss on trade receivables	Ending allowance – Beginning allowance + Debts written off
Cost of inventory purchased	Purchase price + Other costs incurred to bring in goods Transport, custom duties, insurance on goods, packing materials, wages for employees to repack goods
Impairment loss on inventory	Cost – Net realisable value – Insurance claim receivable
Interest expense incurred	Interest rate per annum (%) × Principal sum borrowed

Profitability Ratios

Gross profit margin (%)	$\frac{\text{Gross profit}}{\text{Net sales revenue}} \times 100\%$
Mark-up on cost (%)	$\frac{\text{Gross profit}}{\text{Cost of sales}} \times 100\%$
Profit margin (%)	$\frac{\text{Profit}}{\text{Net sales revenue}} \times 100\%$
Return on equity (%)	$\frac{\text{Profit}}{\text{Average equity}} \times 100\%$ $\text{Average equity} = \frac{\text{Equity (start)} + \text{Equity (end)}}{2}$ • Sole proprietorship: owner's equity • Private limited company: shareholders' equity

Liquidity Ratios

Working capital	Current assets − Current liabilities
Current ratio	$\frac{\text{Current assets}}{\text{Current liabilities}}$
Quick ratio	$\frac{\text{Current assets} - \text{Inventory} - \text{Prepaid expense}}{\text{Current liabilities}}$ **OR** $\frac{\text{Cash} + \text{Receivables}}{\text{Current liabilities}}$

Efficiency Ratios

Rate of inventory turnover (times)	$\frac{\text{Cost of sales}}{\text{Average inventory}}$ $\text{Average inventory} = \frac{\text{Inventory (start)} + \text{Inventory (end)}}{2}$
Days sales in inventory (days)	$\frac{\text{Average inventory}}{\text{Cost of sales}} \times 365 \text{ days}$ **OR** $\frac{1}{\text{rate of inventory turnover}} \times 365 \text{ days}$
Rate of trade receivables turnover (times)	$\frac{\text{Net credit sales revenue}}{\text{Average net TR}}$ $\text{Average net TR} = \frac{\text{Net TR (start)} + \text{Net TR (end)}}{2}$
Trade receivables collection period (days)	$\frac{\text{Average net TR}}{\text{Net credit sales revenue}} \times 365 \text{ days}$ **OR** $\frac{1}{\text{rate of TR turnover}} \times 365 \text{ days}$ • Trading business: sales revenue • Service business: service fee revenue

Financial Statements

Tips on preparing the financial statements with adjustments

1	Expenses	Prepaid expenses - expenses Expense payables + expenses
2	Income	Income receivables + income Income received in advance - income
3	Interest expense	(%) x bank loan
4	Depreciation expense (straight-line method)	Rate (%) x Cost of non-current asset Or $\frac{\text{Cost – scrap value}}{\text{No of useful life}}$
5	Depreciation expense (reducing-balance method)	Rate (%) x Net Book Value of non-current asset Or Rate (%) x (Cost – accumulated depreciation)
6	Accumulated depreciation	Total depreciation
7	Allowance for impairment of trade receivables	(%) x trade receivables
8	Impairment loss on trade receivables	Ending allowance – beginning allowance + write off
9	Bank loan or mortgage loan	Current portion of long-term borrowings + Long-term borrowings
***		
10	Impairment loss on inventory	Cost – Net realisable value
11	Share capital	Share price x number of shares
12	Dividends	Dividends x number of shares

1. Statement of financial performance of a **trading** business

Company name
Statement of Financial Performance for the year ended 31 December 2022

	$	$
Sales revenue	xxx	
Less: Sales returns	xxx	
Net sales revenue		xxx
Less: Cost of sales		xxx
Gross profit		A
Other income		
Discount received	xxx	
Commission income	xxx	
Rent income	xxx	
Gain on sale of non-current asset	xxx	B
Less: Other expenses		
Discount allowed	xxx	
General expenses	xxx	
Salaries expense	xxx	
Insurance expense	xxx	
Interest on loan	xxx	
Depreciation on fixtures and fittings	xxx	
Depreciation on motor vehicles	xxx	
Impairment loss on trade receivables	xxx	
Loss on sale of non-current asset	xxx	C
Profit for the year		A+B-C

There are two portions for a trading business.
- Trading portion shows the gross profit/loss from the buying and selling of goods.
- Profit and loss portion reports the overall profit earned from operating the business.

There are two different scenarios where you put bracket to represent a negative number.
- Loss for the year
- Reversal of impairment loss on trade receivables

2. Statement of financial performance of a **service** business

Company name
Statement of Financial Performance for the year ended 31 December 2022

	$	$
Service fee revenue		A
Other income		
Discount received	xxx	
Commission income	xxx	
Rent income	xxx	
Gain on sale of non-current asset	xxx	B
Less: Other expenses		
Discount allowed	xxx	
General expenses	xxx	
Salaries expense	xxx	
Insurance expense	xxx	
Interest on loan	xxx	
Depreciation on fixtures and fittings	xxx	
Depreciation on motor vehicles	xxx	
Impairment loss on trade receivables	xxx	
Loss on sale of non-current asset	xxx	C
Profit for the year		A+B-C

3. Statement of financial position of a sole proprietorship

Company name

Statement of Financial Position as at 31 December 2022

Assets	$	$	$
<u>Non-current assets</u>	Cost	Accumulated depreciation	Net book value
Land and property	xxx	xxx	xxx
Fixtures and fittings	xxx	xxx	xxx
Office equipment	xxx	xxx	xxx
Motor vehicles	xxx	xxx	xxx
			A
<u>Current assets</u>			
Trade receivables	xxx		
Less: Allowance for impairment of trade receivables	xxx	xxx	
Cash in hand		xxx	
Cash at bank		xxx	
Inventory		xxx	
Income receivables		xxx	
Prepaid expenses		xxx	B
Total assets			A+B
Equity and Liabilities			
<u>Owner's equity</u>			
Capital (Beg Capital + Profit – Drawings)			C
<u>Non-current liabilities</u>			
Long-term borrowings			D
<u>Current liabilities</u>			
Current portion of long-term borrowings		xxx	
Bank overdraft		xxx	
Trade payables		xxx	
Expense payable		xxx	
Income received in advance		xxx	
Dividends payable		xxx	E
Total equity and liabilities			C+D+E

4. Statement of financial position of a company***

Company name
Statement of Financial Position as at 31 December 2022

Assets	$	$	$
Non-current assets	Cost	Accumulated depreciation	Net book value
Land and property	xxx	xxx	xxx
Fixtures and fittings	xxx	xxx	xxx
Office equipment	xxx	xxx	xxx
Motor vehicles	xxx	xxx	xxx
			A
Current assets			
Trade receivables	xxx		
Less: Allowance for impairment of trade receivables	xxx	xxx	
Cash in hand		xxx	
Cash at bank		xxx	
Inventory		xxx	
Income receivables		xxx	
Prepaid expenses		xxx	B
Total assets			A+B
Equity and Liabilities			
Shareholders' equity			
Share capital, 100 000 ordinary shares		xxx	
Retained earnings (Beg RE + Profit – Dividends)		xxx	C
Non-current liabilities			
Long-term borrowings			D
Current liabilities			
Current portion of long-term borrowings		xxx	
Bank overdraft		xxx	
Trade payables		xxx	
Expense payable		xxx	
Income received in advance		xxx	
Dividends payable		xxx	E
Total equity and liabilities			C+D+E

5. POA theory questions

Ch 1: Introduction to Accounting

Type of businesses	1. Explain the difference between a trading business and a service business. Trading business buys from suppliers and sells goods to customers while service business provides services to its customers.
Types of business ownerships	2. State two features (advantages) of being a sole proprietor. ● A sole proprietor is the only owner of the business and has absolute control over it. ● The sole owner can easily update the particulars of the new owner to notify the corporate regulatory authority of the transfer of ownership. ● The sole proprietorship has minimal administrative duties to adhere to. ● The sole owner is entitled and has access to all business profits. 3. State two features (advantages) of being a limited liability partnership. ● It is more likely for banks and other lenders to lend money to the LLP as there are more sources of personal assets from partners and business assets to serve as collaterals. ● When the LLP incurs debts and losses, the partners are not personally liable for them. They are not affected unless it is caused by their wrongful actions. ● The LLP has few regulatory duties to comply with. 4. State two features (advantages) of being a private limited company. ● It is more likely for banks and other lenders to lend money to the PLC as there are more business assets of high value to serve as collaterals. ● When the company incurs debts and losses, shareholders are not obliged to pay them using their personal assets. ● Shareholders can pay a stamp duty to the tax authority to give their shares to another person or organisation.

<table>
<tr><td></td><td>5. State three differences between a shareholder in a private limited company and a sole proprietor in a business.

● The shareholders have no control over the running of the business, unless they are part of the management team while the only owner usually runs the business by himself or herself and has absolute control over it.
● The company exists forever until wound up or struck off while the SP exists as long as the owner is alive and desires to continue operation.
● The PLC must comply with statutory requirements and file its annual financial reports while the SP has minimal administrative duties to adhere to.
● The shareholders receive a portion of the profits when the PLC declare dividends while the only owner is entitled and has access to all profits made by the SP.
● When the business incurs debts and losses, shareholders suffers limited liabilities while the only owner is obliged to pay them using his or her personal assets.</td></tr>
<tr><td>Stakeholders and their decision needs</td><td>6. Name two stakeholders and the decision that they might make by using a business’ accounting information.

● Owners and shareholders will decide whether to continue to invest in the business or sell the business, depending on the risks and returns related to the business
● Managers will consider ways to improve the performance of the business
● Employees will decide whether continue working at the business
● Lenders will decide whether to grant loans to the business, depending on the business’ ability to repay the loan principal and pay interest
● Suppliers will decide whether to sell to the business on credit, depending on its ability to pay
● Customers will decide whether to buy from the business, depending on the business’ ability to provide the goods and/or services that they need and good after-sales service
● Government will decide the amount of tax to collect from the business
● Competitors will decide whether they are comparable to the business and consider how to improve their own performance</td></tr>
<tr><td>Role of accounting and accountants</td><td>7. State two roles of accounting.

Accounting is an information system that:
● provides accounting information for stakeholders
● to make informed decisions regarding the management of resources and performance of businesses.</td></tr>
</table>

	8. Explain the role of accountants. Accountants have to: • adapt, solve problems, think critically and provide accounting and non-accounting information for decision-making • provide timely, relevant and credible information, based on accounting theories, which are easily and appropriately understood by stakeholders.
Professional ethics	9. Eve applied for a bank loan to purchase a new delivery vehicle. She has asked her accountant to change her profit figures for the previous year in order to improve her chances of getting the loan. Eve has threatened to move her business to another accountant if he does not agree. State the principle of professional ethics that Eve's accountant should follow in this situation. Give one reason for your answer. • Objectivity • If Eve succumbed to the threat of dismissal and provide a false profit figure, it would mislead the bank into thinking that the business is profitable and able to repay its loans. • The bank might then make the decision to approve its application for a bank loan and risk being unable to collect the loan principal and interest. 10. Name and explain the two principles of professional ethics which must be applied by accountants in the preparation and presentation of accounting information. • Integrity: An accountant with integrity is straightforward and honest in all professional relationships. • Objectivity: An accountant who is objective will not let bias, conflict of interest or the undue influence of others override his or her professional judgement. 11. Explain the importance of an accountant's professional ethics. Since stakeholders place trust in the information provided by accountants, it is important that accountants have integrity and are objective so that they will not mislead users into making poor decisions.

Ch 2: Accounting Information System

Type of transactions	12. State the difference between a cash transaction and a credit transaction. Payment is made at the same time or immediately during a cash transaction while payment is delayed or postponed during a credit transaction. 13. Suggest a reason why Beautiful Floral buys services on credit instead of paying cash for them. When the business buys services on credit, it is able to delay payment and use the cash to meet its immediate needs.
Accounting cycle	14. What is an accounting information system? Accounting information system (AIS) is a system that a business uses to collect, store and process accounting data. 15. List the stages of the accounting cycle. The accounting cycle comprises four stages. • Source documents are used to identify and record transactions daily. • The ending balances of ledger accounts are listed in a trial balance and adjusted at least once in a financial year. • The adjusted balances are reported in the financial statements at least once in a financial year. • After the financial statements are finalised, income, expenses, income summary, drawings and dividends accounts are closed at the end of the financial year. 16. State the order in which financial transactions are processed through the accounting system. Source documents, journal, ledger, trial balance, financial statements
Source documents	17. What are source documents? Source documents provide proof that transactions have occurred and details that can be recorded in a journal. 18. State one possible reason why Chang Yee (owner) would issue a credit note to a customer. Business issues credit note to reduce the amount owed by credit customers: • who were previously overcharged • after goods were returned

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Source Document	Purpose of Source Document
Receipt	**Acknowledges** payment received from customers immediately after the business has sold goods or provided services.
Remittance advice	**Informs** credit supplier that payment by cheque has been made for a specific invoice.
Invoice	**Informs** credit customers of the amount owed after the business sold goods or provided services on credit.
Credit note	**Reduces** the amount owed by credit customers: • who were previously overcharged; or • after goods were returned.
Debit note	**Increases** the amount owed by credit customers who were previously undercharged.
Payment voucher	**Processes** payment to credit suppliers: • must be approved by authorised personnel; and • must be supported by original supplier's invoice.
Bank statement	Checks and tallies against the business records of its cash at bank account.

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Ch 4: Double-entry Recording

Rule	19. State the double entry recording rule. There are three rules of the double-entry system. • Each business transaction will affect at least two accounts. • At least one account will be debited, where the amount will be recorded on the debit column of that account. • At least one account will be credited, where the amount will be recorded on the credit column of that account.
Goods returns	20. State two reasons why customers might make returns. • Goods are defective/faulty/spoilt/expired. • Goods delivered are different from what were ordered e.g. wrong specifications.
Cash discount	21. State why a business might receive cash discounts from a supplier. When the business pays early, the business receives cash discount from its credit suppliers. 22. State why a business may allow a cash discount to a customer. When credit customers pay early, the business gives cash discount to the credit customers. 23. State the benefits to a business of offering cash discounts to customers. When customers are encouraged to pay early, the business will be able to receive cash earlier and use it to meet its daily operational needs.

<table>
<tr>
<td>Trade discount</td>
<td>
24. State two reasons why a supplier would offer a trade discount.

To encourage:

customers to buy in bulk
their patronage
their loyalty

25. Differences between a trade discount and cash discount.

<table>
<tr><th></th><th>Trade Discount</th><th>Cash Discount</th></tr>
<tr><td>Define</td><td>A reduction to the list price</td><td>A reduction to the invoiced price</td></tr>
<tr><td>Purpose</td><td>Encourage:
customers to buy in bulk;
their patronage; and
their loyalty.</td><td>Encourage credit customers to pay early, within a specified time.</td></tr>
<tr><td>Calculation</td><td>Reduces list price.
Invoice price = List price − Trade discount</td><td>Reduces invoiced price.
Amount paid = Invoiced price − Cash discount</td></tr>
<tr><td>Recording</td><td>Not recorded in the ledger account as only the invoiced price is recorded</td><td>Recorded in the ledger account as discount allowed or discount received</td></tr>
</table>
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</table>

Ch 5: Trial Balance and Financial Statements

Trial balance	26. Explain why a business prepares a trial balance at the end of the financial year. A trial balance is prepared to: • facilitate the preparation of the financial statements • ensure arithmetic accuracy in recording 27. Explain the limitation of a trial balance. A balanced trial balance is not an absolute proof of accuracy. There may be errors not revealed by a trial balance.
Statement of financial performance	28. State the purpose of a statement of financial performance. A statement of financial performance shows the income earned and expenses incurred for a period of time and informs stakeholders of the profitability of a business. 29. Explain the difference between the statements of financial performance of a trading and of a service business. There are two portions of a statement of financial performance for a trading business, trading portion and profit and loss portion. However, for a service business, there is no trading portion in its statement of financial performance.
Statement of financial position	30. Explain the meaning of the term 'current assets'. Current assets refer to resources a business owns or controls that are expected to provide future benefits which are used within one financial year. 31. Explain the meaning of the term 'current liabilities'. Current liabilities refer to obligations owed by a business to others that are expected to be settled/paid within one financial year. 32. State the difference between a current asset and a non-current asset. The benefits of current asset are used within one financial year while the benefits of non-current assets last beyond one financial year.

	33. State the difference between a current liability and a non-current liability. Current liability is due to be paid within one financial year while non-current liability is due to be paid beyond one financial year. 34. Explain why trade receivable is a current asset. Payment is expected to be collected from credit customers within one financial year. 35. Explain why machinery is a non-current asset. Machine used by the business to produce/process goods can be used for more than one financial year. 36. Explain why trade payable is a current liability. Amounts owed to credit suppliers is expected to be paid within one financial year. 37. Explain why bank loan is a non-current liability. Money borrowed from bank is expected to be paid beyond one financial year.

Ch 6 & 7: Income and Expenses

Income	38. Explain the difference between revenue and other income. Revenue refers to amounts earned through the main activities of the business while other income refers to amounts earned from business activities other than the main business activity.
Expenses	39. Explain the difference between cost of sales and other expenses. Cost of sales refer to the total cost price of goods that have been sold while other expenses refer to costs incurred in the operation of a business.

Ch 8: Cash

Dishonoured cheque	40. State two reasons why a cheque would be returned by the bank as dishonoured. • Cheque has expired - It was dated six months ago and is now no longer valid. • Cheque is post-dated - It was written for a future date and the bank will only pay on or after that date. • Information on cheque is not consistent - Amount written in numbers does not match amount written in words. • Information on cheque is not complete - There is no date, amount to be paid or signature. • Payer's bank account does not have enough money.
Internal controls	41. Explain why internal controls are needed to protect cash. As cash is highly portable, it has a high chance of getting stolen. Internal controls are needed to reduce the possibility of theft or the likelihood of error in order to ensure that cash is well-protected and accurately reported. 42. Name and explain two types of internal controls over cash. • Segregation of duties - Separate cash handling and cash recording duties among different employees so that no single person has control over the entire cash process. • Custody of cash - Secure cash and cheques in a locked storage. • Authorisation - Obtain proper approvals for all payments from authorised personnel. • Bank reconciliation - Compare the business' records with the bank's records to identify items that caused the differences between the ending balances in the business cash at bank account and the bank statement.
Bank reconciliation	43. State two reasons for preparing a bank reconciliation statements. • To identify items that caused the differences between the ending balances in the business cash at bank account and the bank statement • To detect errors, discrepancies, or irregularities on time and reduce the possibility of cash being misappropriated 44. State two types of item paid or received directly through the bank for which a bank statement may be used as proof. • Direct deposits – credit transfer, interest on deposit • Direct payment – standing order, bank charges, interest on loan • Dishonoured cheque

<table>
<tr><td></td><td>45. Name three items which cause the difference between the ending balances of a bank statement and business’ cash at bank account.

• Direct deposits – credit transfer, interest on deposit
• Direct payment – standing order, bank charges, interest on loan
• Dishonoured cheque
• Cheques not yet presented
• Deposits in transit</td></tr>
<tr><td></td><td>46. Format of a bank reconciliation statement

Company name
Bank reconciliation statement as XX

<table><tr><td></td><td>$</td><td>$</td></tr><tr><td>Balance as per bank statement</td><td></td><td>A</td></tr><tr><td></td><td></td><td></td></tr><tr><td>Add: Deposits in transit</td><td></td><td></td></tr><tr><td>Micky Mouse</td><td></td><td>B</td></tr><tr><td></td><td></td><td></td></tr><tr><td>Less: Cheques not yet presented</td><td></td><td></td></tr><tr><td>Donald</td><td>XX</td><td></td></tr><tr><td>Goofy</td><td>XX</td><td>C</td></tr><tr><td></td><td></td><td></td></tr><tr><td>Balance as per adjusted cash at bank account</td><td></td><td>A+B-C</td></tr></table></td></tr>
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Ch 9: Inventories

Valuation	47. State how ending inventory must be valued in the financial statements. Inventory is valued at the lower of cost and net realisable value.
FIFO	48. Explain what is meant by the FIFO method of inventory valuation. First-In-First-Out (FIFO) method assumed that goods which are purchased first are sold first. Hence, goods that are purchased last are assumed to remain in the business as the ending inventory.
Impairment loss on inventory	49. Explain what is meant by net realisable value. Net realisable value refers to the selling price of the inventory less the additional cost to sell the inventory.

Ch 11: Non-Current Assets

Expenditure	50. Explain the meaning of the term 'capital expenditure'. Capital expenditure refers to: • costs to buy and bring the non-current assets to their intended use • costs to enhance the non-current assets • costs incurred on non-current assets that provide benefits for more than one year 51. Explain the meaning of the term 'revenue expenditure'. Revenue expenditure refers to: • costs to operate, repair and maintain the non-current assets in working condition • costs incurred on non-current assets that provide benefits which will be used within one year
Depreciation	52. State two causes of depreciation. • Usage • Wear and tear • Obsolescence • Legal limits 53. Explain why the business uses the reducing-balance method of depreciation, rather than the straight-line method, for the motor vehicles. • The business used the reducing-balance method as the business expects to use the motor vehicles more in its earlier years and less as the non-current asset gets older and becomes less efficient. • It does not expect to use the motor vehicles uniformly throughout its estimated useful life, hence, straight-line method is not used.

Ch 13: Long-term Borrowings

Bank loan vs bank overdraft	54. Explain two ways in which a bank loan is different from a bank overdraft. • Bank overdraft refers to the amount that the business withdrew beyond what it has deposited in the bank account while bank loan refers to the additional amount borrowed. • The business deposits cash into the bank account within the year to reduce the overdraft while the business makes regular cash payments in equal instalments over the loan period or a one-time lump-sum payment at the end of the loan period to reduce the principal sum.

Ch 14: Equities

Owner's equity	55. State three reasons why the owner's equity in a sole proprietorship may be different at the end of the accounting year from that at the beginning. • The sole owner contributes additional assets to the business. • The business made a profit or incurred a loss for the period. • The sole owner withdraws business assets for personal use.
Shareholders' equity	56. State three reasons why the shareholders' equity in a private limited company may be different at the end of the accounting year from that at the beginning. • The private limited company issued new shares. • The business made a profit or incurred a loss for the period. • The private limited company declared dividends.

Ch 16: Financial Statements Analysis ***

Profitability	57. State two reasons why it is important that a business is profitable. • It is important to make a gross profit from the buying and selling of goods to gain a competitive advantage over its competitors. • It is also important for the business to make a profit so that this can be reinvested in the business. 58. State what is measured by return on equity. Return on equity measures the amount of profit a business earns for every dollar of equity invested by the owner or shareholders in the business. 59. Jennifer Tang is considering comparing the profitability of her business with that of a competitor. Name two profitability ratios which Jennifer Tang could use. • Gross profit margin • Mark-up on cost • Profit margin • Return on equity 60. Suggest two way to improve the profitability of the business. • Buy goods at lower cost price - Buy in bulk to obtain trade discount • Increase sources of other income - Sublet excess space to another business to earn rental income • Reduce operating expenses - Reduce the use of electrical appliances to lower utilities expenses
Liquidity	61. Explain what is meant by the liquidity of a business. Liquidity is the ability of a business to convert current assets into cash to pay current liabilities. 62. Explain the meaning of the term ‘working capital’. Working capital refer to the excess of current assets over current liabilities.

63. State two reasons why working capital is important for a business.

- The business needs to have enough current assets to settle its current liabilities when they fall due.
- The business needs to have enough current assets to pay for its daily operating expenses to ensure business run smoothly
- It will be easier for the business to obtain short-term loan from the lenders

64. Distinguish between the quick ratio and the current ratio.

Current ratio measures the ability of a business to pay its short-term debts using its current assets while quick ratio measures the ability of a business to pay its short-term debts using its quick assets, excluding inventory and prepayments.

65. Advise on two measures she may take to improve her liquidity position.

- Increase sources of cash - Obtain cash contribution from owner or shareholders
- Manage cash outflow - Reduce operating expenses e.g. utilities

66. Identify two problems the business may face as a result of the (poor) liquidity of the business.

A business with low liquidity is usually short of cash and may be unable to settle its immediate debts. If this persists, the business may:

- eventually close down
- be unable to negotiate for better credit terms with supplier
- be unable to obtain bank loan

67. Suggest why the liquidity of the business has changed even though profit remained the same over the three years.

Liquidity is determined by its current assets and current liabilities while profit is determined by its income and expenses.
The business may buy goods on credit, which will affect liquidity but has no effect on profit.
The business may sell to the same group of customers and make the same amount of sales. However, these customers may make payment at different times, which explains the change in liquidity but not profit.

Efficiency	68. Suggest two ways in which inventory turnover rates can be improved. • Sell inventory faster - Provide trade discounts to encourage customers to buy in bulk and regularly • Keep sufficient inventory on hand - Use technological tools to improve the accuracy of predictions about customer demand in order to know when and how much inventory to buy 69. Suggest one way to improve the efficiency in the management of its trade receivables. • Improve credit granting processes - Ensure credit is granted to customers who are financially able • Provide monetary incentives - Offer cash discounts to encourage credit customers to pay early • Increase debt collection efforts - Send regular reminders to credit customers who delay payment or refuse to pay