



Accounting
STUDY GUIDE

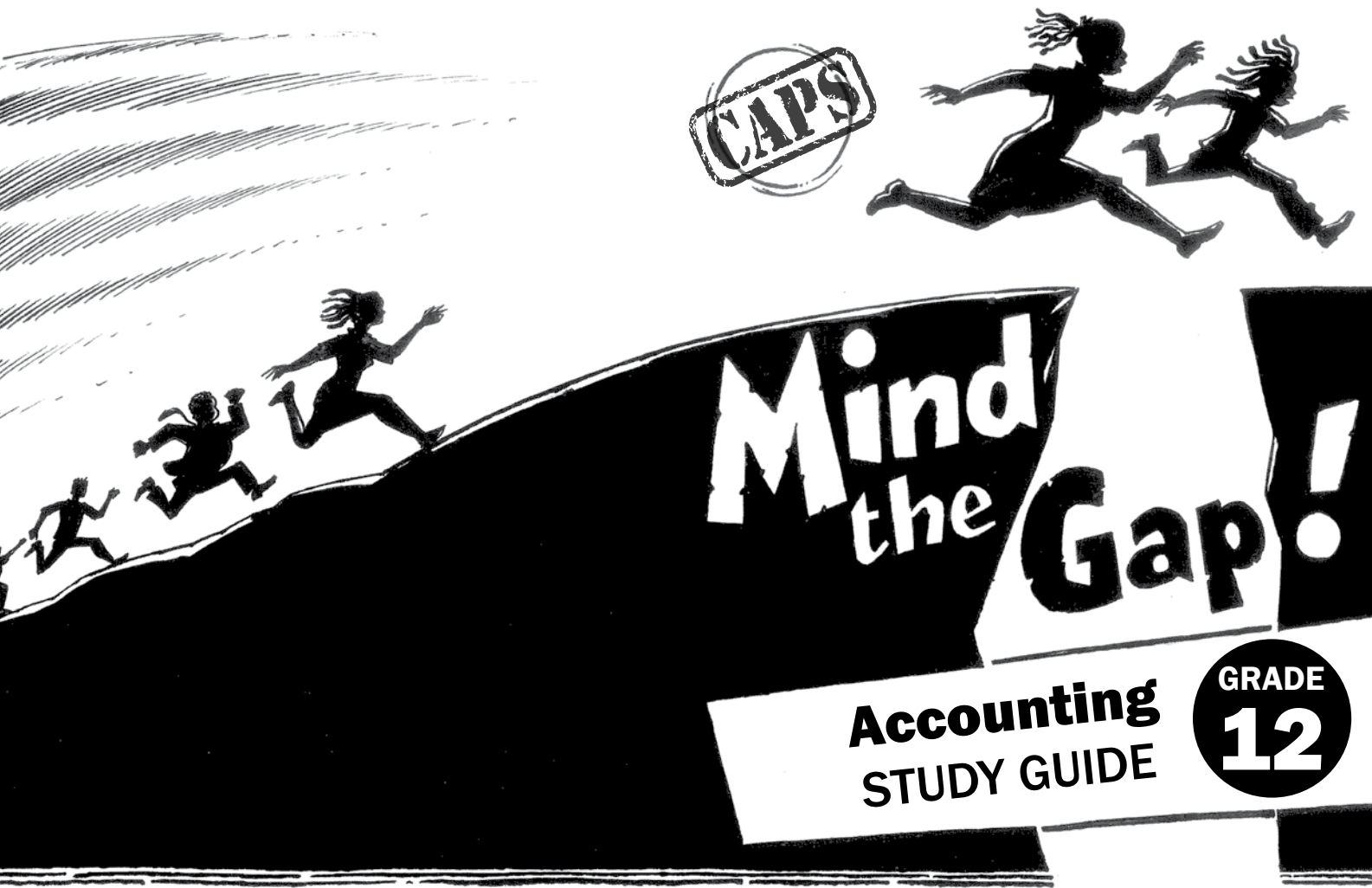
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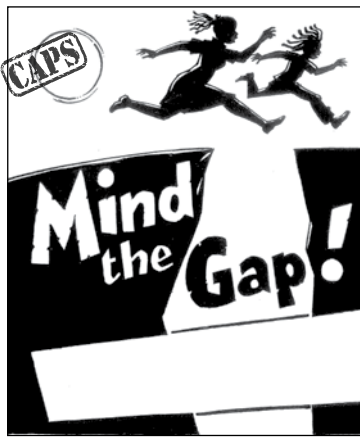
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Curriculum and Assessment Policy Statement (CAPS) Mind the Gap Grade 12 Study Guide Accounting
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Ministerial foreword

The Department of Basic Education has pleasure in releasing the second edition of *Mind the Gap* study guides for Grade 12 learners. These study guides continue the innovative and committed attempt by the Department of Basic Education to improve the academic performance of Grade 12 candidates in the National Senior Certificate (NSC) examination.

The study guides have been written by subject expert teams comprised of teachers, examiners, moderators, subject advisors and subject coordinators. Research started in 2012 shows that the *Mind the Gap* series has, without doubt, had a positive impact in improving grades. It is my fervent wish that the *Mind the Gap* study guides take us all closer towards ensuring that no learner is left behind, especially as we move forward in our celebration of 20 years of democracy.

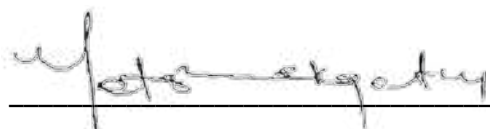
The second edition of *Mind the Gap* is aligned to the 2014 Curriculum and Assessment Policy Statement (CAPS). This means that the writers have considered the National Policy pertaining to the programme, promotion requirements and protocol for assessment of the National Curriculum Statement for Grade 12 in 2014.

The *Mind the Gap* CAPS study guides take their brief in part from the 2013 National Diagnostic report on learner performance and draws on the 2014 Grade 12 Examination Guidelines. Each of the *Mind the Gap* study guides provides explanations of key terminology, simple explanations and examples of the types of questions that learners can expect to be asked in an exam. Marking memoranda are included to assist learners in building their understanding. Learners are also referred to specific questions in past national exam papers and examination memos that are available on the Department's website – www.education.gov.za.

The CAPS edition include Accounting, Economics, Geography, Life Sciences, Mathematics, Mathematical Literacy and Physical Sciences. The series is produced in both English and Afrikaans. There are also nine English First Additional Language study guides. They include EFAL Paper 1 (Language); EFAL Paper 3 (Writing); and a study guide for each of the Grade 12 prescribed literature set works.

The study guides have been designed to assist those learners who have been underperforming due to a lack of exposure to the content requirements of the curriculum and aims to mind-the-gap between failing and passing, by bridging the gap in learners' understanding of commonly tested concepts so candidates can pass.

All that is now required is for our Grade 12 learners to put in the hours preparing for the examinations. Learners make us proud – study hard. We wish each and every one of you good luck for your Grade 12 examinations.



Matsie Angelina Motshekga, MP
Minister of Basic Education
May 2014



Matsie Angelina Motshekga, MP
Minister of Basic Education

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Dear Grade 12 learner

This *Mind the Gap* study guide has been CAPS aligned and helps you to prepare for the end-of-year Accounting Grade 12 examination.

This study guide does not cover the entire curriculum, but it does focus on core content of each knowledge area and **points out where you can earn easy marks**.

You must work your way through this study guide to improve your understanding, identify your areas of weaknesses and correct your own mistakes.

We are confident that this *Mind the Gap* can help you to prepare well so that you pass the end-of-year exams. To ensure a high quality pass, you should also cover the remaining aspects of the curriculum using other textbooks and your class notes.

Also pay special attention to the way the workings have been shown in the worked examples. This is the best way for you to earn maximum marks.

In order for you to be successful in Accounting you must:

- Ensure that you know the formats or layouts of the:
 - Income Statement
 - Balance Sheet
 - Cash Flow Statement
 - Production Cost Statement
 - General Ledger accounts
- Understand the concepts explained in this guide and know how to do calculations.
- Work through as many past examination papers as you can (use the explanations and steps in this guide to assist you). There are some suggested questions from past papers at the end of each section for extra practice. Be careful when working through questions relating to Companies of past papers as there are some aspects that are treated differently under CAPS.

Remember, your success in the final exam will depend on how much extra time you put into preparing.

Overview of the CAPS Accounting Grade 12 exam

- There is one exam of 3 hours for 300 marks.
- All questions are compulsory (no choice questions).
- There are no different sections.
- All past papers have had 6 questions.
- Each question covers different levels so all learners should be able to gain some marks in every question.
- All questions should be attempted.
- Questions will include conceptual understanding, application, interpretation and reflective type questions.
- Learners will be provided with a specially prepared answer book for their answers. This is specially designed for the Accounting exam. The answer booklet provides space for every question. All calculations, workings and final answers will be done in this answer booklet.









How to use this study guide

This study guide covers **selected parts** of the different topics of the Grade 12 Accounting curriculum. The selected parts of each topic are presented in the following way:

- An explanation of terms and concepts
- Worked examples to explain and demonstrate
- Activities with questions for you to answer
- Answers for you to use to check your own work



	Pay special attention		Hints to help you remember a concept or guide you in solving problems		Worked examples
	Step-by-step instructions		Refers you to exam questions		Activities with questions for you to answer

- A **checklist from the exam guidelines** for Accounting has been provided on page xiv for you to keep track of your progress. Once you have mastered the core concepts and have confidence in your answers to the questions provided, tick the last column of the checklist.
- The **activities are based on exam-type questions**. Cover the answers provided and do each activity on your own using the suggested steps in this guide. Then check your answers. Reward yourself for the things you get right. If you get any incorrect answers, make sure you understand where you went wrong before moving onto the next section. Pay special attention to the way the workings have been shown in the worked examples. This is the best way for you to earn maximum marks. Where you see this tick you will be awarded a mark even if your answer is incorrect, provided you have followed the correct procedure (e.g. adding, subtracting or transferring figures).
- **Exemplar Exam papers** are also included in the study guide for you to do. Check your answers by looking back at your notes and the exam memoranda. Past exam papers go a long way in preparing you for what to expect and help reduce exam anxiety. Go to www.education.gov.za to download more past exam papers.

Use this study guide as a workbook. Make notes, draw pictures and highlight important concepts.



Top 10 study tips



- 1.** Have all your materials ready before you begin studying – pencils, pens, highlighters, paper, etc.
- 2.** Be positive. Make sure your brain holds onto the information you are learning by reminding yourself how important it is to remember the work and get the marks.
- 3.** Take a walk outside. A change of scenery will stimulate your learning. You'll be surprised at how much more you take in after being outside in the fresh air.
- 4.** Break up your learning sections into manageable parts. Trying to learn too much at one time will only result in a tired, unfocused and anxious brain.
- 5.** Keep your study sessions short but effective and reward yourself with short, constructive breaks.
- 6.** Teach your concepts to anyone who will listen. It might feel strange at first, but it is definitely worth reading your revision notes aloud.
- 7.** Your brain learns well with colours and pictures. Try to use them whenever you can.
- 8.** Be confident with the learning areas you know well and focus your brain energy on the sections that you find more difficult to take in.
- 9.** Repetition is the key to retaining information you have to learn. Keep going – don't give up!
- 10.** Sleeping at least 8 hours every night, eating properly and drinking plenty of water are all important things you need to do for your brain. Studying for exams is like strenuous exercise, so you must be physically prepared.

Study skills to boost your learning

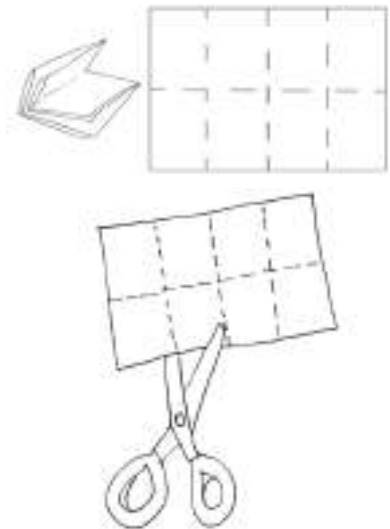
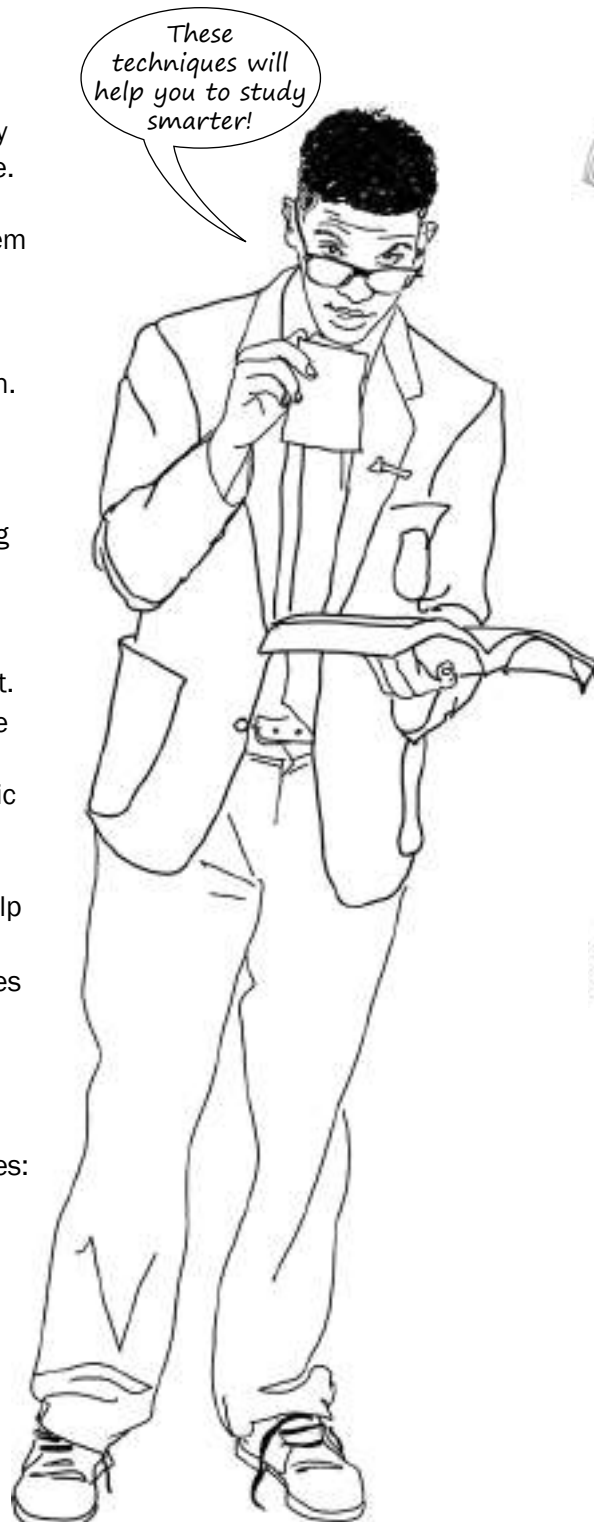
This guide makes use of 3 study techniques you can use to help you learn the material:

1. Mobile notes
2. Mnemonics
3. Mind maps

Mobile notes

Mobile notes are excellent tools for learning all the key concepts in the study guide. Mobile notes are easy to make and you can take them with you wherever you go:

1. Fold a blank piece of paper in half. Fold it in half again. Fold it again.
2. Open the paper. It will now be divided into 8 parts.
3. Cut or tear neatly along the folded lines.
4. On one side of each of these 8 bits of paper, write the basic concept.
5. On the other side, write the meaning or the explanation of the basic concept.
6. Use different colours and add pictures to help you remember.
7. Take these mobile notes with you wherever you go and look at them whenever you can.
8. As you learn, place the cards in 3 different piles:
 - I know this information well.
 - I'm getting there.
 - I need more practice.
9. The more you learn them, the better you will remember them.



1. Fold an A4 paper into 8 squares. Cut or tear neatly along the folded lines.



2. Write the basic concept on one side of a bit of paper.



3. Write the definition of the basic concept on the back of the piece of paper.



Mnemonics

A **mnemonic** code is a useful technique for learning information that is difficult to remember. This is an example of a word mnemonic using the word **BALANCE** where each letter of the word stands for something else:

- B** – Best – doing your best is more important than being the best.
- A** – Attitude – always have a positive attitude.
- L** – Load – spread the load so you don't leave everything to the last minute. Use a study timetable to plan.
- A** – Attention – pay attention to detail. Only answer what is required.
- N** – Never give up! Try, try and try again!
- C** – Calm – stay calm even when the questions seem difficult.
- E** – Early – sleep early the night before your exam. If you prepare well you will not need to cram the night before.

Mnemonics are code information and make it easier to remember.

The more creative you are and the more you link your 'codes' to familiar things, the more helpful your mnemonics will be.

This guide provides several ideas for using mnemonics. Be sure to make up your own.

*Neither you nor the world knows what you
can do until you have tried.*

Ralph Waldo Emerson

Mind maps

There are several mind maps included in this guide, summarising some of the sections.

Have a look at the following pictures of a brain cell (neuron) and, below it, a mind map:

Figure 1: Brain cell or neuron

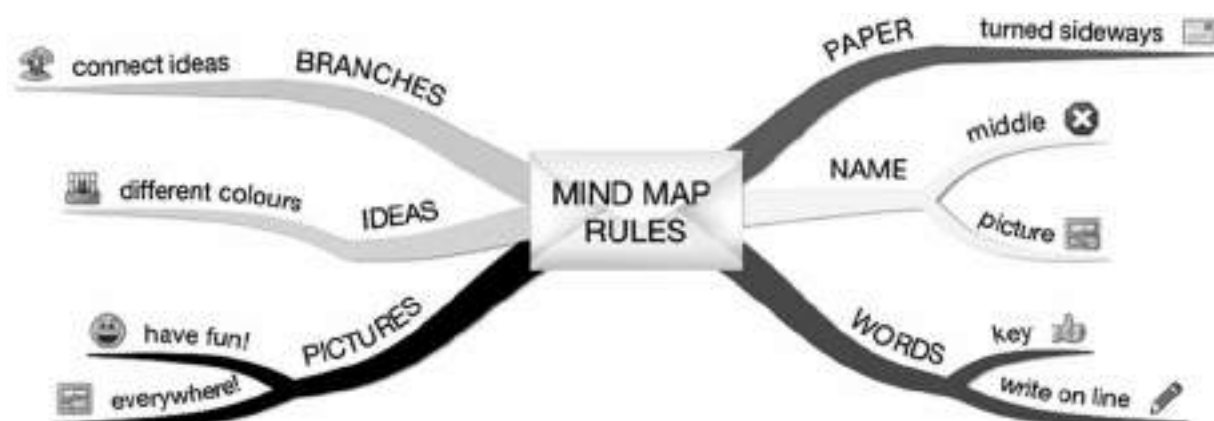


Figure 2: Mind map rules

Mind maps work because they show information that we have to learn in the same way that our brains 'see' information.

As you study the mind maps in the guide, add pictures to each of the branches to help you remember the content.

You can make your own mind maps as you finish each section.

How to make your own mind maps:

1. Turn your paper sideways so your brain has space to spread out in all directions.
2. Decide on a name for your mind map that summarises the information you are going to put on it.
3. Write the name in the middle and draw a circle, bubble or picture around it.
4. Write only key words on your branches, not whole sentences. Keep it short and simple.
5. Each branch should show a different idea. Use a different colour for each idea. Connect the information that belongs together. This will help build your understanding of the learning areas.
6. Have fun adding pictures wherever you can. It does not matter if you can't draw well.

Mind mapping your notes makes them more interesting and easier to remember.



On the day of the exam ...

1. Make sure you have all the necessary stationery for your exam, i.e. pens, pencils, eraser and calculator (with new batteries). Make sure you bring your ID document and examination admission letter.
2. Arrive on time, at least one hour before the start of the exam.
3. Go to the toilet before entering the exam room. You don't want to waste valuable time going to the toilet during the exam.
4. Use the 10 minutes reading time to read the instructions carefully. This helps to 'open' the information in your brain. All questions in Accounting are compulsory, but you do not have to answer them in order. Start with the question you think is the easiest to get the flow going.
5. Break the questions down to make sure you understand what is being asked. If you don't answer the question properly you won't get any marks for it. Look for the key words in the question to know how to answer it. A list of question words is on page ix of this study guide.
6. Try all the questions. Each question has some easy marks in it so make sure that you do all the questions in the exam.
7. Never panic, even if the question seems difficult at first. It will be linked to something you have covered. Find the connection.
8. Manage your time properly. Don't waste time on questions you are unsure of. Move on and come back if time allows.
9. Check weighting – how many marks have been allocated for your answer? Take note of the ticks in this study guide as examples of marks allocated. Do not give more or less information than is required.
10. Write big and bold and clearly. You will get more marks if the marker can read your answer clearly. Show workings in brackets for Accounting as suggested in this study guide.



Question words to help you answer questions

It is important to look for the question words (the words that tell you what to do) to correctly understand what the examiner is asking. Use the words in the following table as a guide when answering questions.

Question word	What is required of you
Analyse	Separate, examine and interpret
Classify	Divide into groups or types so that things that are similar are in the same group
Comment	Write generally about
Compare	Point out or show both similarities or differences
Define	Give a clear meaning
Describe	List the main characteristics of something
Discuss	Consider all information and reach a conclusion
Evaluate	Express an opinion based on your findings
Explain	Make clear, interpret and spell out
Forecast	Say what you think will happen in the future
Give/provide	Write down only facts
Identify	Name the essential characteristics
Interpret	Give the intended meaning of
List	Write a list of items
Mention	Refer to relevant points
Name	State something – give, identify or mention
State	Write down information without discussion
Suggest	Offer an explanation or solution



Examples of question words

Choose a definition from COLUMN B that matches the type of account in COLUMN A.

Draw a line from COLUMN A to COLUMN B to match the definitions.

Column A	Column B
1. Fixed/tangible assets	A This increases profit and therefore increases owner's equity.
2. Current assets	B This decreases profit and therefore decreases owner's equity.
3. Non-current liabilities	C Amounts owing that will take longer than 12 months to pay off.
4. Current liabilities	D Assets which are expected to be kept for a long period of time, usually longer than a year. Without them the business will not exist or earn a profit.
5. Income	E The value (net worth) of the business at any point in time (total assets – total liabilities).
6. Expenses	F Amounts owing that will be paid back within 12 months.
7. Owner's equity	G Assets which are expected to be converted into cash in a short period of time (i.e. less than a year).

In every exam question, put a **CIRCLE** around the question word and **underline** any other important key words. These words tell you exactly what is being asked.



Learner's Checklist

Use this checklist to monitor your progress when preparing for your examination.

	Topic	Covered in the Study Guide	I do not understand	I understand
1.	Basic Accounting Concepts	✓		
2.	Companies			
	Accounting equation	✓		
	Company concepts	✓		
	GAAP principles	✓		
	Company ledger accounts	✓		
	Final accounts of companies:			
	Trading account	✓		
	Profit and loss account	✓		
	Appropriation account	✓		
	Financial statements with adjustments:			
	Income Statement	✓		
	Balance Sheet	✓		
	Cash Flow Statement	✓		
	Notes to the financial statements	✓		
	Analysis and Interpretation of financial statements	✓		
	Comment on an audit report	✓		
3.	Manufacturing			
	Manufacturing concepts	✓		
	Production Cost Statement with notes	✓		
	Cost calculations	✓		
	Break-even point	✓		
	Trading and Profit and Loss Statements	*		
4.	Budgets			
	Budgeting concepts	✓		
	Debtors' collection schedule	✓		
	Creditors' payment schedule	✓		
	Cash budget (analyse and interpret)	✓		
	Projected Income Statement (analyse and interpret)	✓		
5.	Reconciliations			
	Bank reconciliation	✓		
	Debtors reconciliation	✓		
	Age analysis	✓		
	Creditors reconciliation	✓		
6.	Inventories			
	Inventory concepts	✓		
	Inventory valuation – specific identification, FIFO and weight average methods	✓		
7.	VAT			
	Concepts and calculations	✓		
	VAT control account	✓		
8.	Fixed Assets			
	Asset disposal	✓		

Basic accounting concepts

1.1 Basic concepts

TERM	DEFINITION
Accrued expenses/ expenses payable	Expenses that are still owing at the end of the financial year.
Accrued income/ income receivable	Income that is still owing to the business at the end of the financial year.
Asset	Item of value owned by a person or business which enables a profit to be made.
Bad debts	Debts written off as the debtors are unlikely to settle their accounts.
Cost of sales	Cost of sales is the cost price of all goods that have been sold.
Creditors	People/suppliers the business owes money to.
Debtors	People who owe the business money for goods bought on credit.
Depreciation	The amount by which fixed assets reduce in value over time due to use.
Income received in advance/ deferred income	Income that has already been received by a business but which is for the next financial year.
Liability	An amount owed by a person or business to another person or business.
Loss	When the expenses are more than the income.
Mark-up	The percentage added to the cost price to calculate the selling price, i.e. the profit %.
Owners' equity	The net worth (value) of the business at any given time. Or, assets less liabilities.
Prepaid expenses	Expenses that have already been paid but which are for the next financial year.
Profit	When the income is more than the expenses.
Trading stock deficit	This amount is calculated when the physical stock-take figure is less than the figure for trading stock in the general ledger.
Trading stock surplus	This amount is calculated when the physical stock-take figure is more than the figure for trading stock in the general ledger.



These definitions help you understand the meaning of basic accounting concepts that are used in this study guide.

Spend time learning the meanings of these terms. Use mobile notes to help you learn them. See page ix for more information.



1.2 Rules of Accounting



These rules of accounting do not change. LEARN THEM WELL!!!

ASSETS	OWNER'S EQUITY				LIABILITIES		
Dr A Cr	Dr Drawing Cr		Dr Capital Cr		Dr L Cr		
+ -	+ -	- +					
	Dr Expenses Cr		Dr Income Cr				
	+ (if expenses increase then profit decreases)	- (if expenses decrease then profit increases)	- (if income decreases then profit decreases)	+ (if income increases then profit increases)			

1.3 Classification of accounts

NON-CURRENT ASSETS	OWNER'S EQUITY		NON-CURRENT LIABILITIES (to be paid over more than 12 months)
	EXPENSES	INCOME	
Tangible/fixed assets <ul style="list-style-type: none"> Land and buildings Equipment Vehicles Financial assets <ul style="list-style-type: none"> Fixed deposit (longer than 12 months) 	<ul style="list-style-type: none"> Cost of sales Interest expense Rent expense Salaries and wages Stationery Fuel Packing material Repairs Insurance Advertising Discount allowed Telephone Water and electricity Loss on sale of asset Bad debts Depreciation Trading stock deficit Provision for bad debts adjustment (+) 	<ul style="list-style-type: none"> Sales Current income Interest income Rent income Discount received Bad debts recovered Profit on sale of asset Trading stock surplus Provision for bad debts adjustment (-) 	<ul style="list-style-type: none"> Mortgage bond Loans
CURRENT ASSETS Inventories <ul style="list-style-type: none"> Trading stock Consumable stores on hand Trade and other receivables <ul style="list-style-type: none"> Debtors' control Accrued income/income receivable Prepaid expenses Cash and cash equivalents <ul style="list-style-type: none"> Bank (DR) Petty cash Cash float Fixed deposit (less than 12 months) 			CURRENT LIABILITIES (to be paid in less than 12 months) <ul style="list-style-type: none"> Trade creditors Bank overdraft (CR) Short term portion of loan Accrued expenses/expenses payable Income received in advance/deferred income



Activity 1: Matching items

Choose a definition from COLUMN B that matches the type of account in COLUMN A.

Draw a line from COLUMN A to COLUMN B to match the definitions.

Column A	Column B
1. Fixed/tangible assets	A This increases profit and therefore increases owner's equity.
2. Current assets	B This decreases profit and therefore decreases owner's equity.
3. Non-current liabilities	C Amounts owing that will take longer than 12 months to pay off.
4. Current liabilities	D Assets which are expected to be kept for a long period of time, usually longer than a year. Without them the business will not exist or earn a profit.
5. Income	E The value (net worth) of the business at any point in time (total assets – total liabilities).
6. Expenses	F Amounts owing that will be paid back within 12 months.
7. Owner's equity	G Assets which are expected to be converted into cash in a short period of time (i.e. less than a year).

[7]

Answers to activity 1

Column A	Column B
1	D
2	G
3	C
4	F
5	A
6	B
7	E

[7]



Activity 2: Multiple-choice questions

Three options are provided as possible answers to the following questions.

Circle the correct answer.

1. Bank overdraft is classified as a...	2. Consumable stores on hand is classified as...
A Non-current liability	A Owner's equity
B Current asset	B Current asset
C Current liability	C An expense

[2]

Answers to activity 2

1	C	This is a current liability because it will be paid back within 1 year (short-term).
2	B	This is a current asset because the business will use them within the next 12 months.

[2]



1.4 Steps to recording transactions

Refer to Rules of Accounting and Classification of accounts on page 2.

- Read the transaction/adjustment.
Bought stationery and paid by cheque, R150.
- Identify the two accounts affected – (double entry principle).
1. Stationery 2. Bank
- Decide what type of accounts these are (classify).
Stationery = expense and therefore affects owner's equity
Bank = current asset
- Decide which account is debited and which account is credited.
The expense is increasing therefore DR stationery
The asset is decreasing therefore CR bank
- Record your answer showing the effect on Assets (A), Owners' equity (O) and Liabilities (L):

Three questions that will assist you:

- If an Asset: is it increasing or decreasing my possessions?
- If a liability: is it increasing or decreasing my debt?
- If an Owners' equity: is it increasing or decreasing the interest of the owner?

Account debit	Account Credit	A =	O +	L
Stationery	Bank	-150	-150	0

A zero indicates no effect. **DO NOT** leave blank!



Activity 3: Accounting equation

Refer to Steps to recording transactions 1–4 above.

Record the transactions in the Table below assuming bank is favourable (Dr) at all times.

- Wrote off a debtor's account of R500 as a bad debt.
- Sent a cheque to a creditor to settle our account of R2 000.
- Received rent of R5 000 from a tenant.
- Bought trading stock on credit for R1 800.
- Bought equipment for R600 and paid by cheque.

When a bank is favourable it means it is an asset of the business and remains in a debit balance.

	Account debit	Account credit	A =	O +	L
1					
2					
3					
4					
5					

[5]

Answers to activity 3

	Account debit	Account Credit	A =	O +	L
1	Bad debts (expense increasing)	Debtors control (asset decreasing)	-500	-500	0
2	Creditors control (liability decreasing)	Bank (asset decreasing)	-2 000	0	-2 000
3	Bank (asset increasing)	Rent income (income increasing)	+5000	+5000	0
4	Trading stock (asset increasing)	Creditors control (liability increasing)	+1800	0	+1 800
5	Equipment (asset increasing)	Bank (asset decreasing)	±600	0	0

[5]



Keep going!

2 Chapter

Companies

2.1 Concepts relating to companies

Persons in a company:



Companies is the **BIGGEST** section in your exam. Spend time on it!



Use mobile notes to learn these concepts. See page ix for instructions on how to make them.

Concept	Explanation
Directors	People who are appointed by the shareholders to run the company.
Independent auditor (external)	An auditor who expresses an opinion on the financial statements in an auditor's report but does not work for the company.
Internal auditor	An auditor, who supervises the preparation of the financial statements, is responsible for internal control and is employed by the company.
Shareholders	People who own the company.
South African Revenue Services (SARS)	The government department to whom the company must pay income tax on the profits and VAT when due.

Documents relating to companies

Concept	Explanation
Auditor's report	This is an opinion given by a qualified person on whether the financial statements are reliable or not.
<ul style="list-style-type: none"> • Qualified auditor's report 	When the auditors find the financial statements acceptable EXCEPT for some aspects that need to be changed, fixed or investigated.
<ul style="list-style-type: none"> • Unqualified auditor's report 	When the auditors find the financial statements acceptable in ALL respects.
<ul style="list-style-type: none"> • Disclaimer 	When the auditors are not prepared to express an opinion on the financial statements (because they are too unreliable).
Balance Sheet	This statement reflects the assets, liabilities and net worth (owners' equity of the company). Another term for this is 'Statement of Financial Position'.
Cash Flow Statement	This shows the flow of cash in a company (money coming in and money going out).
Income Statement	This statement shows the profit or loss made from business operations (income and expenses). Another term for this is 'Statement of Comprehensive Income'.
Tax assessment	This is issued by SARS to confirm the amount of income tax which the company has to pay based on profits.

Further concepts relating to companies

Concept	Explanation
Authorised share capital	The maximum number of shares a company can sell.
Dividends	That portion of the profits (after tax) which has been approved to be shared amongst the shareholders (total dividends = interim + final). Dividends that are paid to the shareholders during the year. Dividends that are declared (recommended) to the shareholders at the end of the financial year.
• Interim dividends • Final dividends	
Income tax	Tax the company pays to SARS on its profits.
Issued share capital	The number of shares that have actually been sold to shareholders. Use number of issued shares to calculate dividends.
Limited liability	The liability of the shareholders is limited to their investment in the company (they cannot lose their personal assets).
No par value	There is no value attached to shares until they are issued.
Provisional tax	Payments made to SARS during the year based on estimated profits (every 6 months).
Retained income	A portion of the profits after tax that are not paid out to the shareholders in dividends but kept (retained) for future growth of the company.
Issue price	The price at which shares are issued to the public.
Shareholders earnings	Net profit after tax.
Shareholders for dividends	The amount still owing to shareholders for dividends declared but not yet paid.
Buy back shares	Issued shares that have been repurchased by the company and are retired or cancelled.

Some acronyms (abbreviations) used in companies

AGM	Annual General Meeting
CA	Chartered Accountant
CIPRO	Company and Intellectual Property Commission
GAAP	Generally Accepted Accounting Practice
IFRS	International Financial Reporting Standards
JSE	Johannesburg Securities Exchange
MOI	Memorandum of Incorporation
SAICA	South African Institute for Chartered Accountants
SAIPA	South African Institute for Professional Accountants

GAAP concepts

Concept	Explanation
Business entity rule	The finances of the company are kept separate from that of the shareholders
Going concern	Financial statements are prepared with the understanding that the company will continue operating in the future
Historical cost	All assets are recorded at their original cost price e.g. Land and Buildings are recorded at the price that you paid for them
Matching	Income and expenses must be recorded in the correct financial year e.g. sales and cost of sales
Materiality	All important items must be shown separately in the financial statements (e.g. directors' fees) or when decisions must be made (e.g. is it worth having separate accounts for wages and salaries if you have only two employees?)
Prudence	Figures used in financial statements should be realistic (conservative – always record the worst scenario). The aim of this principle is to show the reality “as it is” and not make things prettier than what they are. E.g. you will show ‘net debtors’ in the balance sheet (trade debtors minus provision for bad debts)

2.2 Company General Ledger accounts



SARS (income tax) implies a liability owing to SARS.

- a) Ordinary share capital
- b) SARS (income tax)
- c) Shareholders for dividends
- d) Income tax
- e) Dividends on ordinary shares (ordinary share dividends)
- f) Appropriation account



These are the most commonly asked company ledger accounts.

For any words you do not understand, refer to the company concepts at the beginning of this section.



Activity 1: Typical examination questions



Worked example 1

Use the following information to complete the ledger accounts given on the answer sheet for kwik fix ltd for the financial year ended 30 June 2011.

To calculate the average share price, use this figure and divide it by the no. of shares issued.

$$1\ 000\ 000 \div 500\ 000 \text{ shares} = R2$$

Information

1	1 July 2010	At the beginning of the year, the company had the following opening balances: Ordinary share capital (500 000 shares) Retained income SARS (Income tax) Shareholders for dividends	R1 000 000 180 000 (ct) 9 000 130 000
2	1 July 2010	Issued 50 000 shares to the public at R7,50 per share	
3	23 July 2010	Paid the amounts owing to SARS and the shareholders.	
4	31 December 2010	A first provisional tax payment of R112 500 was made to SARS half-way through the financial year.	
5	31 December 2010	An interim dividend of 15 cents per share was paid to shareholders.	
6	31 March 2011	Bought back 20 000 shares from a disgruntled shareholder. The directors decided to buy back these shares at R8,50 per share.	
7	30 June 2011	A second provisional tax payment of R120 000 was made to SARS at the end of the financial year.	
8	30 June 2011	Final dividends of 30 cents per share were declared at the AGM but have not yet been paid to the shareholders.	
9	30 June 2011	After the completion of the audit, the income tax figure for the year was determined as R240 000. This was calculated on a net profit figure of R800 000.	
10	30 June 2011	Show the closing transfers to the final accounts.	

Notes below refer to the information above and to the ledger accounts below (1 – 10):

- 1 The balances for SARS (Income tax) and Shareholders for dividends are the amounts that were not paid last year and need to be paid this year.
- 2 Shares issued to the public at issue price of R7,50 per share
- 3 The amounts owing to SARS and the shareholders from last year are now being paid.
- 4 The first provisional tax payment is always made half-way (6 months) into the financial year and the second provisional tax payment is made at the end of the financial year.
- 7
- 5 The interim dividend is paid during the year
- 8 The final dividend is declared (not paid) at the end of the financial year.
- 6 Shares bought back at R8,50 per share from a shareholder. New average price to be calculated. To calculate average price, find the value of Ordinary Share Capital, $R1\ 375\ 000 \div 55\ 000 = R2,50$. It means that you're only going to claim R2,50 per share and the rest will be claimed from Retained Income.
- 9 The income tax figure for the year is the amount of tax the company owes calculated on the net profit for the year. This needs to be compared to the provisional tax payments made to see whether the company owes SARS more tax (liability) or whether SARS owes the company (asset).
The net profit of R800 000 is calculated in the Profit and Loss Account and transferred to the Appropriation Account.
- 10 The final accounts include the Trading Account, Profit and Loss Account (covered in this example) and the Appropriation Account.

EXAMPLE OF A TRADING ACCOUNT AND PROFIT AND LOSS ACCOUNT
(exactly the same as a sole trader or partnership)

TRADING ACCOUNT (F1)

N

2011	June	28	Cost of Sales	GJ	300 000	2011	June	28	Sales	GJ	1 470 000
			Profit and loss	GJ	1 170 000						
					1 470 000						1 470 000

PROFIT AND LOSS ACCOUNT (F2)

N

2011	June	28	Salaries	GJ	130 000	2011	June	28	Trading account (gross profit)	GJ	1 170 000
			Directors fees (new)	GJ	160 000				Rent Income	GJ	24 000
			Audit fees (new)	GJ	40 000				Profit on sale of asset	GJ	16 000
			Provision on bad debts adjustment	GJ	1 000						
			Water and electricity	GJ	29 000						
			Telephone / cell phones	GJ	50 000						
			Appropriation		800 000						
					1 210 000						1 210 000

General Ledger of Kwik Fix Ltd

These numbers refer to the explanations above.

Shares issued: 500 000 + 50 000 = 550 000 shares issued.

Average price of shares:
 $R1\ 000\ 000 + R375\ 000 = R1\ 375\ 000$
 $R1\ 375\ 000 \div 550\ 000\ \text{shares} = R2,50$

Balance Sheet Section									
Dr					Cr				
Ordinary Share Capital									
2011 Mar	31	Bank 6 (20 000 × R2,50)	CPJ	50 000	2010 July	1	Balance 1	b/d	1 000 000
						31	Bank 2 (50 000 × R7,50)	GJ	375 000
		Balance	c/d	1 325 000					
				1 375 000					1 375 000
					2011 July	1	Balance	b/d	1 325 000

Balance Sheet Section									
Dr					Cr				
SARS (Income tax)									
2010 July	23	Bank 3	CPJ	9 000	2010 July	1	Balance 1	b/d	9 000
2010 Dec	31	Bank 4	CPJ	112 500	2011 June	30	Income tax 9	GJ	240 000
2011 June	30	Bank 7	CPJ	120 000					
		Balance	c/d	7 500					
				249 000					249 000
					2011 July	1	Balance	b/d	7 500

The Income Tax assessment was more than the provisional payments. Therefore the balance is on the credit side making it a liability (Trade and Other Payables).

Nominal Accounts Section									
Dr					Cr				
INCOME TAX									
2011 June	30	SARS (Income tax) 9	GJ	240 000	2011 June	30	Appropriation 10	GJ	240 000

Balance Sheet Section									
Dr					Cr				
SHAREHOLDERS FOR DIVIDENDS									
2010 July	23	Bank 3	CPJ	130 000	2010 July	1	Balance 1	b/d	130 000
2011 June	30	Balance	c/d	159 000	2011 June	30	Dividends on ordinary shares 8	GJ	159 000
				289 000					289 000
					2011 July	1	Balance	b/d	159 000

The R159 000 is the final dividend and is still owing to the shareholders. This is a liability (Trade and Other Payables).

Nominal accounts section									
Dr					Cr				
DIVIDENDS ON ORDINARY SHARES									
2010 Dec	31	Bank 5 (550 000 × 0.15)	CPJ	82 500	2011 June	30	Appropriation 10	GJ	241 500
2011 June	30	Shareholders for dividends 8 (530 000 × 0.30)	GJ	159 000					
				241 500					241 500

There are three different ways of preparing the Appropriation account. Choose the alternative that you have been taught.

Option 1: The Retained Income for the year is transferred from the Appropriation account to the Retained Income account.

Balance Sheet Section									
Dr					Cr				
RETAINED ACCOUNT									
2011 Mar	31	Bank (20 000 × R6) 6	GJ	120 000	2011 June	30	Balance	b/d	180 000
June	30	Balance	c/d	378 500			Appropriation	GJ	318 500
				498 500					498 500
					July	1	Balance		378 500

Final accounts section									
Dr					Cr				
APPROPRIATION ACCOUNT									
2011 June	30	Income tax 10	GJ	240 000	2011 June	30	Profit & loss 9	GJ	800 000
		Dividends on ordinary shares 10	GJ	241 500					
		Retained income	GJ	318 500					
				800 000					800 000

Option 2: The Retained Income at the beginning of the year less the buy-back of shares adjustment is transferred to the Appropriation account. The Retained Income (after the share buy-back adjustment) at the end of the year is transferred from the Appropriation account to the Retained Income account

Balance sheet section									
Dr					Cr				
RETAINED ACCOUNT									
2011 Mar	31	Bank (20 000 × R6) 6	GJ	120 000	2010 July	1	Balance	b/d	180 000
June	30	Appropriation	GJ	60 000					
				180 000					180 000
					2011 June	1	Appropriation	GJ	378 500

Final accounts section									
Dr					Cr				
APPROPRIATION ACCOUNT									
2011 June	30	Income tax 10	GJ	240 000	2011 June	30	Profit & loss 9	GJ	800 000
		Dividends on ordinary shares 10	GJ	241 500			Retained Income (180 000 - 120 000)		60 000
		Retained income	GJ	378 500					
				860 000					860 000

Option 3: The Retained Income at the beginning of the year is transferred to the Appropriation account. The Retained Income (before the share buy-back adjustment) at the end of the year is transferred from the Appropriation account to the Retained Income account

Balance sheet section									
Dr					Cr				
RETAINED ACCOUNT									
2011 Mar	31	Bank (20 000 × R6) 6	GJ	120 000	2011 July	1	Balance	b/d	180 000
June	30	Appropriation	GJ	180 000	2011 June	30	Appropriation	GJ	498 500
		Balance	c/d	378 500					
				<u>678 500</u>					<u>678 500</u>
					2011 July	1	Balance	b/d	378 500

The balance of the Retained Income account stays R378 500 as in Options 1 and 2

Final accounts section									
Dr					Cr				
APPROPRIATION ACCOUNT									
2011 June	30	Income tax 10	GJ	240 000	2011 June	30	Profit & loss 9	GJ	800 000
		Dividends on ordinary shares 10	GJ	241 500			Retained Income		180 000
		Retained income	GJ	498 500					
				<u>980 000</u>					<u>980 000</u>

Practice task 1

General ledger of kwik fix LTD

Balance sheet section

Dr					Cr				
Ordinary Share Capital									

Dr	Retained income										Cr

Dr	SARS (Income tax)										Cr

Dr	Shareholders for Dividends										Cr

Nominal section

Dr	Income Tax										Cr

Dr		Dividends on Ordinary Shares								Cr	

Final accounts section

Dr		Appropriation Account								Cr	

2.3 Preparation of Financial Statements for companies



Income statement

Use the following steps to prepare an income statement from a pre-adjustment trial balance:

1. Enter the pre-adjustment trial balance figures from the nominal section onto the answer sheet next to the detail.
2. Read each adjustment:
 - a) If necessary calculate the adjustment amount
 - b) Decide on which account is to be debited and which account is to be credited.
 - c) On your answer sheet reflect a (+) or a (-) in respect of each adjustment next to the already entered pre-adjustment figure.
 - i) Outstanding/accrued amounts will be added (+) and prepaid/received in advance amounts will be subtracted (-)
3. When all the adjustments have been done, calculate your final figures and write them in the column.

Remember a pre-adjustment trial balance refers to a trial balance that is NOT final and requires adjustments (entries) to be made to finalise the figures to be used in the preparation of the annual Financial Statements.

Look at the format you have been given. Do you notice any missing details? Fill them in. **THESE ARE EASY MARKS!**



Summary of the year end adjustments

Ensure that you know all possible yearend adjustments **before attempting the given activities.**

Make use of the Pre-adjustment Trial balance of Carl Stores to complete the Income Statement for the year ended 30 June 2014 and the Balance Sheet on 30 June 2014.

PRE-ADJUSTMENT TRIAL BALANCE ON 30 JUNE 2014			
BALANCE SHEET ACCOUNTS SECTION		DEBIT	CREDIT
Ordinary Share capital			351 000
Retained Income			9 100
Loan from Lowveld Bank			50 000
Land and buildings		270 000	
Equipment (at cost)		75 000	
Vehicle		100 000	
Accumulated depreciation on vehicles			30 000
Accumulated depreciation on equipment			30 500
Fixed Deposit		10 000	
Trading stock		74 000	
Debtors control		16 100	
Provision for bad debts			600
Deposit on water and electricity		1 000	
Bank		15 900	
Cash float		800	
Petty cash		300	
Creditors control			9 500
South African Revenue Services: (PAYE)			
Creditors for salaries			
Pension fund			
Medical aid fund			
NOMINAL ACCOUNTS SECTION			
Sales			550 000
Debtors allowances		10 000	
Cost of sales		320 000	
Salaries		95 000	
Wages		30 000	
Water and electricity		7 000	
Pension Fund contribution		4 000	
Medical Fund contribution		2 700	
Bad debts		1 000	
Rent income			13 000
Commission income			8 700
Packing materials		1 200	
Insurance		600	
Bank charges		5 300	
Discount allowed		1 000	
Telephone		12 500	
Interest on fixed deposit			800
Interest on debtors			200
		1 053 400	1 053 400

Make use of the following adjustments to revise on the adjustments learnt previously

- 1 Prepaid expenses: Insurance prepaid, R200
- 2 Accrued expenses: Water and electricity still due, R2 000.
- 3 **Income received in advance:** Rent income received in advance, R1 000
- 4 **Accrued income:** Interest on fixed deposit still due, R400 (**not capitalized**)
- 5 **Bank charges**, R700, interest on overdraft, R200 on late bank statement to be brought into account.
- 6 Bank Statement also showed a **RD cheque**, R1 000 (receive from debtor B. Bam in settlement of his account of R1 100)
- 7 **Interest capitalized.** Loan b/d R55 000 (1 July 2011). Total payments R15 000. Closing balance of loan R50 000.
- 8 **Depreciation:** Depreciate vehicles at 10% p.a. at cost price and Equipment at 10 % p.a. at carrying value
- 9 **Bad debts:** J Jon's debt written off as bad debt, R200
- 10 **INCREASE: 2014 Provision** for bad debts at 5 % of debtors. (17 000 × 5% =)
- 11 **Insurance claim of e.g. stock stolen:** e.g. Stock stolen valued @ R5 000. The Insurance Company is prepared to pay out R4 000 on the claim put forward
- 12 **Trading stock deficit:** Trading stock according to stock taking, R67 000.
- 13 **Consumable stores on hand:** Closing stock: Packing material, R300
- 14 **Salary of an employee omitted in error:** e.g. Gross salary of Joe Soap omitted of R10 000. SARS (PAYE), R1 600 Pension fund R500 and Medical fund R900. The owner contributed to the medical fund and pension fund Rand for Rand basis.

The degree of difficulty of these adjustments lays in the calculation of the figure but the entry stays the same! So ensure that you memorise the format.

Ensure that you know how to interpret the adjustments, how to complete the general journal entry and how it affects the ledger accounts and the financial statements

Adjustments at the end of the Financial year

ILLUSTRATION OF THE PROGRESSION OF 14 POSSIBLE YEAR-END ADJUSTMENTS FROM ADJUSTMENT TO INCOME STATEMENT AND TO BALANCE SHEET

1. Prepaid expenses Insurance prepaid, R200

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET	
Prepaid expenses(CA) B		Insurance (600 – 200)	400	NOTE 5: TRADE AND OTHER RECEIVABLES	
Insurance	2600			Prepaid Expense	200
Insurance (e) N					
Total b/d	600	Prepaid expenses	200		
		Profit and loss	400		
	<u>600</u>		<u>600</u>		

2. Accrued expenses: Electricity still due, R2 000.

Accrued expenses (CL) B		Water and electricity (7 000 + 2 000)	9 000	NOTE 9: TRADE AND OTHER PAYABLES		
	Water and electricity			2 000	Accrued Expenses	2 000
Water and Electricity(e) N						
Total b/d	7 000	Profit and loss	9 000			
Accrued expenses	2 000					
	<u>9 000</u>		<u>9 000</u>			

3. Income received in advance Rent income received in advance, R1 000

Income received advance (CL) B		Rent Income (13 000 – 1 000)	12 000	NOTE 9: TRADE AND OTHER PAYABLES		
	Rent income			1 000	Income received in advance	1 000
Rent income(I) N						
Income received in advance	1 000	Total	13 000			
Profit and loss	12 000					
	<u>13 000</u>		<u>13 000</u>			

4. Accrued income: Interest on fixed deposit still due, R400 (not capitalized)

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET	
Accrued income(CA) B		Plus Interest income (800 + 400)	1 200	NOTE 5: TRADE AND OTHER RECEIVABLES	
Interest on fixed deposit	400			Accrued Income	400
Interest on fixed deposit (I) N					
Profit and loss	1200	Total	800		
		Accrued income	400		
	<u>1 200</u>		<u>1200</u>		

5. Bank charges The bank statement was received after the pre- adjustment trial balance was drawn up. The following must be included: Bank charges R700 Interest on overdraft, R200

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET
Bank(CA) B				NOTE 6: CASH AND OTHER CASH EQUIVALENTS
Balance b/d	15 900	Bank charges	7 000	
		Interest on over draft	200	Bank (15 900 – 700 – 200)
		Balance c/d	<u>15 000</u>	15 000
	<u>15 900</u>			
Balance b/d	15 000			
Bank charges(e)N				
Total b/d	6 300	Profit on Loss	7 000	
Bank	<u>700</u>			
	<u>7 000</u>			
Interest on overdraft (e)N				
Bank	<u>200</u>	Profit on Loss	200	

6. RD cheques and discount allowed The bank statement was received after the pre- adjustment trial balance was drawn up. The following must be taken into account; RD cheque of R1000 received from a debtor, B Bam, in settlement of his account of R1100

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET
Bank (CA) B				NOTE 5: TRADE AND OTHER RECEIVABLES
Balance b/d	15 900	Discount allowed	1 000	Trade Debtors
		(1 100 – 100)		17 000
				(16 100 + 1 000 + 100)
				NOTE 6: CASH AND OTHER CASH EQUIVALENTS
				Bank (15 900 – 700 – 200 – 1 000)
				14 000
	<u>15 900</u>			
Balance b/d	14 000			
Debtors Control account (CA)B				
2011				
Balance b/d	16 100			
Bank (RD)	1 000			
Journal debits	<u>100</u>			
	<u>17 100</u>			
Discount allowed account				
Total b/d	1 100	Debtors control	100	
		Profit and Loss	1 000	
	<u>1 100</u>		<u>1 100</u>	

7. Interest capitalized. Loan b/d 55 000 (1 Jan 2009) Total payments R15 000 Closing balance of loan R50 000

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET	
Loan: Crazy Bank (CA) B					
Bank (10 000+5 000)	Balance b/d 55 000	Interest on loan	10 000	NON-CURRENT LIABILITIES	
15 000	Interest on loan 10 000	(55 000 – 15 000 – 50 000)		Loan: Crazy Bank (50 000 – 5 000)	45 000
Balance c/d <u>50 000</u>	65 000				
	Balance b/d 50 000			CURRENT LIABILITIES	
Interest on loan (I) N				Short term loan	5 000
Loan: Crazy Bank <u>10 000</u>	Profit and loss <u>10 000</u>				

The total payments for the year includes the interest charged (R10 000) for the year

8. Depreciation
 Vehicles: R100 000
 Accumulated depreciation: R30 000
Depreciation at cost price: $100\ 000 \times 10/100 = 10\ 000$

Equipment: R75 000
 Accumulated. Depreciation: R30 500
Depreciation at carrying value
 $75\ 000 - 30\ 500 = 44\ 500 \times 10/100 = 4\ 450$

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET	
Depreciation (e) N		Depreciation (10 000 + 4 450)	14 450	NOTE 3: FIXED ASSETS	
Accumulated depreciation on Vehicle 10 000	Profit on Loss 14 450			Cost price 75 000	100 000
Accumulated Depreciation on equipment <u>4 450</u>	<u>14 450</u>			Accumulated depre. <u>(30 500)</u>	<u>(30 000)</u>
				Carrying value 44 500	70 000
Accumulated Depreciation on Vehicles (-A) B				<u>Movements:</u>	
	Balance b/d 30 000			Depreciation <u>(4 450)</u>	<u>(10 000)</u>
	Depreciation <u>10 000</u>			Carrying value <u>39 050</u>	<u>60 000</u>
	40 000			Cost price 75 000	100 000
Accumulated Depreciation on Equipment (-A) B				Accumulated depre (35 950)	(40 000)
	Balance b/d 30 500				
	Depreciation <u>4 450</u>				
	34 950				

9. Bad debts J Jon's debt written off as bad debt, R200

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET			
Debtors Control (CA) B		Bad Debts (1 000 + 200)	1 200	NOTE 5: TRADE AND OTHER RECEIVABLES			
Balance b/d	16 100			Bad debts GJ	200	Trade Debtors	17 000
Bank (RD)	1 000			(journal credits)		(15 100 + 1 000 + 100 - 200)	
Journal debits	<u>100</u>			Balance c/d	<u>17 000</u>		
	<u>17 200</u>		<u>17 200</u>				
Balance b/d	17 000						
Bad debts (e) N							
Total b/d	1 000	Profit and loss	1 200				
Debtors control	<u>200</u>		<u>1 200</u>				
	<u>1200</u>						

10. INCREASE:

INCREASE: Provision for bad debts at 5 % of debtors. ($17\ 000 \times 5\% = 850$)

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET		
Provision for bad debts (-A) B		Less operating expenses Provision for bad debts adjustment (850 - 600)	250	NOTE 5: TRADE AND OTHER RECEIVABLES		
	2014			Trade debtors	17 000	
	Balance b/d			600	Less Provision for bad debts	<u>(850)</u>
	Provision for bad debts adjustment			<u>250</u>	Net Debtors	16 150
			<u>850</u>			
Debtors control(CA) B						
2014						
Balance	b/d 17 000					
Provision for bad debts adjustment (e) N						
Provision for bad debts	250	Profit and loss	250			

See the calculations when Provision for bad debts are created or increases or decreases at the end of a financial year.

10.1 Provision for bad debts

CREATE: 2012: provision for bad debts at 5% of debtors

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET	
Debtors control (CA) B		Less operating expenses Provision for bad debts adjustment	50	NOTE 5: TRADE AND OTHER RECEIVABLES	
2012 Balance b/d	1000			Trade debtors	1 000
Provision for bad debts (-A) B				Less Provision for bad debts	<u>(50)</u>
	2012 Provision for bad debts adjustment			Net Debtors	950
	50				
Provision for bad debts adjustment (e) N					
Provision for bad debts	50	Profit and loss	50		

10.2 INCREASE: 2013

Provision for bad debts from R50 to R70. ($1400 \times 5\%=70$)

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET		
Provision for bad debts(-A) B		Less operating expenses Provision for bad debts adjustment (70 - 50)	20	NOTE 5: TRADE AND OTHER RECEIVABLES		
	2013 Balance b/d			50	Trade debtors	1 400
	Provision for bad debts adjustment			<u>20</u>	Less Provision for bad debts	<u>(70)</u>
				<u>70</u>	Net Debtors	1 330
Debtors control (CA) B						
2013 Balance b/d	1400					
Provision for bad debts adjustment (e) N						
Provision for bad debts	20	Profit and loss	20			

10.3 DECREASE: 2014

Provision for bad debts from R70 to R60.

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET	
Provision for bad debts (-A) B		Plus other operating income	10	NOTE 5: TRADE AND OTHER RECEIVABLES	
Provision for bad debts adjustment	2014 Balance b/d			Trade debtors	1 200
Balance c/d				Less Provision for bad debts	(60)
	Balance b/d			Net Debtors	1 140
Debtors control(CA) B					
2014 Balance b/d	1200				
Provision for bad debts adjustment (i) N					
Profit and loss	10	Provision for bad debts	10		

11. Insurance claim of e.g. stock stolen. E.g. Stock stolen valued @ R5 000.

Insurance is prepared to pay out R4000.

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET	
Trading Stock (CA) B		Loss on stolen stock (5 000 - 4 000)	1 000	NOTE 4: INVENTORY	
Balance b/d	74 000			Loss to stolen stock	5 000
				Balance c/d	69 000
Balance b/d	69 000				
Insurance claim (CA) B				NOTE 6: TRADE AND OTHER RECEIVABLES	
Loss to stolen stock	4 000			Insurance Claim (5 000 - 4 000)	1 000
Loss to stolen stock (e) N					
Trading Stock	5 000	Insurance claim	4 000		
		Profit and Loss	1 000		
	5 000		5 000		

12. Trading stock deficit Balance of the Trading stock account is R69 000. Trading stock according to stock taking, R67 000.

GENERAL LEDGER		INCOME STATEMENT		BALANCE SHEET	
Trading stock(CA) B		Trading stock deficit (69 000 - 67 000)	2 000	NOTE 4: INVENTORY	
Balance b/d	74 000			Loss to stolen stock	5 000
				Trading stock deficit	2 000
Balance b/d	67 000			Balance c/d	67 000
Trading stock deficit (e) N				Trading stock (69 000 - 2000)	67 000
Trading stock	2 000	Profit and loss	2 000		

13. Consumable stores on hand; Closing stock: Packing material, R300			
GENERAL LEDGER		INCOME STATEMENT	BALANCE SHEET
Consumable stores on hand (CA) B		Packing material (1 200 – 300)	NOTE 4: INVENTORY Consumable stores on hand 300
Packing material	300		
Packing material (e N)			
Total	1 200		
	Consumable Stores on hand		
			300
	Profit and Loss		
			900
			<u>1 200</u>

Be careful. Does the wording of the adjustment read? After stock taking the packing material USED is R900 or after stock taking the STOCK on hand, R300.

14. Salary of an employee omitted in error: e.g. Gross salary of Joe Soap omitted of R10 000.
SARS (PAYE), R1600 Pension fund R500 and Medical fund R900.
The owner contributed to the medical fund and pension fund on a Rand for Rand basis.
(10 000 – 1 600 – 500 – 900 = 7 000)

GENERAL LEDGER		INCOME STATEMENT	BALANCE SHEET	
Creditors for salaries (CL) B		Salaries (95 000 +10 000) Pension fund contribution (4 000 + 500) Medical fund contribution (2 700 + 900)	NOTE 9: TRADE AND OTHER PAYABLES SARS (PAYE) 1 600 Pension fund (500 + 500) 1 000 Medical fund (900 + 900) 1 800 Creditors for salaries 7 000 (10 000 – 1 600 – 500 – 900)	
	Salaries GJ			7 000
SARS (PAYE) (CL) B				
	Salaries GJ			1 600
Pension Fund (CL)B				
	Salaries GJ	500		
	Pension Fund contribution			
		500		
		<u>1 000</u>		
Medical Fund (CL) B				
	Salaries GJ	900		
	Medical Fund contribution			
		900		
		<u>1 800</u>		
Salaries (e) N				
Total b/d	95 000	Profit and Loss	105 000	
Gross salaries GJ	<u>10 000</u>			
	105 000		<u>105 000</u>	
Pension Fund contribution (e) N				
Total b/d	4 000	Profit and loss	4 500	
Pension Fund	<u>500</u>			
	4 500		<u>4 500</u>	
Medical Fund contribution (e)				
Total b/d	2 700	Profit and loss	3 600	
Medical Fund contribution				
	<u>900</u>			
	3 600		<u>3 600</u>	



Do the following calculation to find the figure for CREDITORS FOR SALARIES while completing Note 9 in the following order: use the gross salary of R10 000 and subtract the

- 1 600 SARS (PAY E)
- 500 Pension fund
- 900 Medical fund
- = 7 000 Creditors for salaries

Calculations:

Ensure that you are able to do the following CALCULATIONS when attempting the year-end ADJUSTMENTS.

Let's use Rent Income to illustrate the different calculations for calculating the Rent for the year and to find the amount received in advance or that is still accrued.

The end of the financial year is on 28 February.

1	Adjustment (low level)	E.g. the total rent income received is R26 000. Take into account that one month's rent was received in advance	
	Calculation	$26\ 000 \div 13 = R2\ 000$ per month $2\ 000 \times 12 = 24\ 000$ Therefore R2 000 was received in advance.	
	Effect on the financial statements	Income statement Rent Income R24 000 $(26\ 000 \div 13 \times 12)$	Balance sheet Note 9: Income received in advance R2 000

2	Adjustment (medium level)	E.g. the tenant paid his rent one month in advance. Take into account that the rent of R2 000 increased by 10 % from 1 October 2013. Total Rent received, R27 200.																																								
	Calculation	<p>Draw a TIME LINE to find the rent for the year and the rent that was received in advance</p> <table border="1" style="margin-left: auto; margin-right: auto;"> <thead> <tr> <th colspan="12">Financial year</th> <th>prepaid</th> </tr> <tr> <th>1 Mar</th><th>Apr</th><th>May</th><th>June</th><th>July</th><th>Aug</th><th>Sept</th><th>1 Oct</th><th>Nov</th><th>Dec</th><th>Jan</th><th>Feb</th><th>Mar</th> </tr> </thead> <tbody> <tr> <td>2000</td><td>2000</td><td>2000</td><td>2000</td><td>2000</td><td>2000</td><td>2000</td><td>2200</td><td>2200</td><td>2200</td><td>2200</td><td>2200</td><td>2200</td> </tr> </tbody> </table> <p> $R2000 \times 7 = 14\ 000$ $2\ 000 + 10\% + R2\ 200 \times 5 = 11\ 000$ $+ R2\ 200 = R27\ 200$ </p>		Financial year												prepaid	1 Mar	Apr	May	June	July	Aug	Sept	1 Oct	Nov	Dec	Jan	Feb	Mar	2000	2000	2000	2000	2000	2000	2000	2200	2200	2200	2200	2200	2200
	Financial year												prepaid																													
1 Mar	Apr	May	June	July	Aug	Sept	1 Oct	Nov	Dec	Jan	Feb	Mar																														
2000	2000	2000	2000	2000	2000	2000	2200	2200	2200	2200	2200	2200																														
Effect on the financial statements	Income statement Rent Income R25 000 $(14\ 000 + 11\ 000)$	Balance sheet Note 9: Income received in advance R2 200																																								

Number 2 and 3 are almost the same however in no. 3 the Rent per month was not given as in no.2. By using the following method the amounts can still be calculated.

3	Adjustment (high level) E.g. The total amount received during the year, R27 200. Take into account that rent increased by 10% on 1 October 2013 and the tenant paid the rent for March during February 2014.																																				
Calculation	<p>Draw a TIME LINE to find the rent for the year and the rent that was received in advance</p> <table border="1" data-bbox="459 338 1390 472"> <thead> <tr> <th colspan="11">Financial year</th> <th>prepaid</th> </tr> <tr> <th>1 Mar</th><th>Apr</th><th>May</th><th>June</th><th>July</th><th>Aug</th><th>Sept</th><th>1 Oct</th><th>Nov</th><th>Dec</th><th>Jan</th><th>Feb</th> </tr> </thead> <tbody> <tr> <td>100%</td><td>100%</td><td>100%</td><td>100%</td><td>100%</td><td>100%</td><td>100%</td><td>110%</td><td>110%</td><td>110%</td><td>110%</td><td>110%</td> </tr> </tbody> </table> <p>CALCULATION: $(100\% \times 7) + (110\% \times 5) + (110\% \times 1) = 27\ 200$ $700\% + 550\% + 110\% = 27\ 200$ $1360\% \text{ (known)} = 27\ 200 \text{ (known)}$</p> <p>MAKE USE OF THE FORMULA:</p> <p>UNKNOWN is the amount prepaid and KNOWN is the total rent received</p> $\frac{\text{Unknown \%}}{\text{Known \%}} \times \frac{110\%}{1360\%} \times \frac{27\ 200}{1} = \text{R2 200 received in advance}$ <p>Or $27\ 200 - 2\ 200 = \text{R25 000 rent income for the year.}$</p>	Financial year											prepaid	1 Mar	Apr	May	June	July	Aug	Sept	1 Oct	Nov	Dec	Jan	Feb	100%	100%	100%	100%	100%	100%	100%	110%	110%	110%	110%	110%
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Example adapted from November 2011 NCS Exam paper

e.g. Worked example 2

Prepare the Income statement for the year ended 30 June 2011.

Information

1. ANEESA LTD

PRE-ADJUSTMENT TRIAL BALANCE AS AT 30 JUNE 2011

	DEBIT	CREDIT
Balance Sheet Accounts Section	R	R
Ordinary share capital		2 820 000
Retained income		684 460
Mortgage loan: Joy Bank		804 500
Land and buildings	2 097 000	
Vehicles	814 000	
Equipment	616 000	
Accumulated depreciation on vehicles		294 800
Accumulated depreciation on equipment		341 000
Trading stock	955 000	
Consumable stores on hand	15 000	
Bank	313 100	
Petty cash	3 300	
Debtors' control	396 000	
Creditors' control		487 300
SARS (Income tax)	261 800	
Provision for bad debts		18 000
Fixed deposit: Broad Bank (8% p.a.)	495 000	

This amount is the provisional tax payment.

Remember to subtract debtors' allowances from sales.

This is the interim dividend. DO NOT include on the Income Statement!

Nominal Accounts Section		
Sales		10 500 000
Debtors' allowances	145 200	
Cost of sales	7 487 000	
Rent income		176 880
Interest income (on fixed deposit)		26 630
Bad debts recovered		2 300
Directors' fees	840 000	
Audit fees	73 800	
Salaries and wages	660 000	
Packing material	23 100	
Marketing expenses	480 000	
Sundry expenses	63 770	
Bad debts	12 000	
Ordinary share dividends	404 800	
	16 155 870	16 155 870

2. ADJUSTMENTS

- A. A physical stock-taking on 30 June 2011 revealed the following inventories on hand:
- | | |
|------------------|----------|
| Trading stock | R902 150 |
| Packing material | R4 260 |
- B. Directors' fees of R22 500 are outstanding at the end of the financial period.
- C. Make provision for outstanding interest on a fixed deposit. This investment has been in existence for the entire year. Interest is not capitalised.
- D. A debtor who owes us R32 000 has been declared insolvent. His estate paid 40 cents in every rand and this has been correctly recorded. The remaining balance must be written off as irrecoverable.
- E. Provision for bad debts must be adjusted to 5% of debtors.
- F. The rent included R14 520 for July 2011. Adjust accordingly.
- G. Make provision for depreciation as follows:
- Vehicles at 15% p.a. on cost price
 - Equipment at 10% p.a. on the diminishing balance method.
 - New equipment to the value of R48 000 was purchased on 1 September 2010. This has been correctly recorded.
- H. The loan statement received from Joy Bank on 30 June 2011 reflected the following:

	R
Balance at the beginning of the financial year	1 125 000
Repayments during the year	458 000
Interest capitalised	?
Balance at the end of the financial year	804 500

- I. Income tax for the year, R150 285.

The total interest forms part of the repayment during the year.

Capitalised means the interest is added onto the loan. You need to calculate this figure.

Answer to worked example 2

1. ANEESA LTD: INCOME STATEMENT FOR THE YEAR ENDED 30 JUNE 2011

	Sales (10 500 000✓ - 145 200✓)	✓	10 354 800
	Cost of sales (7 487 000)	✓	(7 487 000)
	Gross profit	✓	2 867 800
	Other operating income	✓	164 660
F	Rent income (176 880✓ - 14 520✓✓)	✓	162 360
	Bad debt recovered (2 300)	✓	2 300
	Gross operating income		3 032 460
	Operating expenses	✓	(2 392 600)
B	Directors fees (840 000✓ + 22 500✓)	✓	862 500
	Audit fees (73 800)	✓	73 800
	Salaries and wages (660 000)	✓	660 000
A	Packing material (23 100✓ - 4 260✓)	✓	18 840
	Marketing expenses (480 000)	✓	480 000
	Sundry expenses (63 770)	✓	63 770
D	Bad debts (12 000✓ +19 200✓✓)	✓	31 200
E	Provision for bad debts adjustment (18 840 ✓ - 18 000)		840
G	Depreciation V: 122 100 ✓ E: 4 000✓ + 22 700 ✓✓	✓	148 800
A	Trading stock deficit	✓✓	52 850
	Operating profit	✓	639 860
C	Interest income✓ (26 630✓ + 12 970✓)	✓	39 600
	Profit before interest expenses/finance cost✓	✓	679 460
H	Interest expenses/finance cost ✓ (458 000 + 804 500 - 1 125 000) or (1 125 000✓ - 458 000✓ - 804 500✓)	✓	(137 500)
	Profit before tax	✓	541 960
I	Income tax ✓	✓	(150 285)
	Net profit after tax	✓	391 675



FORMAT

It is VERY important to know the format of the Income Statement!

This is the total of the operating expenses. REMEMBER to subtract this from gross operating income.

Always show your calculation work in brackets for part marks.



FORMAT

Note where these 3 items appear on the Income Statement.



The letters in this column refer to the explanations on the next page.

[52]

2. Explanations of each adjustment

A.	<p>Trading stock: The physical stocktaking of R902 150 is less than the amount in the pre-adjustment trial balance of R955 000. This means that there is a trading stock deficit of R52 850 (R955 000 – R902 150). Trading stock deficit = expense item on Income Statement Packing material: The amount on hand is subtracted from the pre-adjustment trial balance amount.</p>											
B.	<p>Directors' fees are outstanding and therefore get added to pre-adjustment figure.</p>											
C.	<p>Interest on fixed deposit = R495 000 × 8% = R39 600 for the year. The difference must be added to pre-adjustment trial balance figure.</p>											
D.	<p>Calculation of bad debts: The estate paid 40 cents therefore 60 cents in every rand must be written off. R32 000 × 0,6 = R19 200. This must be added to the pre-adjustment figure.</p>											
E.	<p>Provision for bad debts adjustments calculation. Calculate final debtors amount taking adjustment D into account: R396 000 – R19 200 = R376 800 5% of R376 800 = R18 840 Provision for bad debts must be adjusted to R18 840. It is currently R18 000. The amount of R840 by which it must be adjusted must be shown in the income statement as an expense.</p>											
F.	<p>Rent was received in advance and therefore must be subtracted from the pre-adjustment figure.</p>											
G.	<p>Depreciation on vehicles: 814 000 × 15% = R122 100 Depreciation on equipment: New equipment Bought on 1 September. The cost of the new equipment must be subtracted from the equipment balance R616 000 – R48 000 = R568 000 10% of R48 000 × 10 ÷ 12 = R4 000 Old equipment Using the diminishing balance method, subtract the accumulated depreciation from the cost price (excluding the new equipment) to determine carrying value R568 000 – R341 000 = R227 000 10% of R227 000 = R22 700 Depreciation is recorded as an expense in the income statement: R122 100 + R22 700 + R4 000 = R148 800</p>											
H.	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td rowspan="5" style="width: 30%; vertical-align: top;"> <p><i>To calculate the interest on loan on the Loan Statement:</i> R1 125 000 – R458 000 – R804 500 = R137 500 Interest on loan = 137 500</p> </td> <td colspan="2" style="text-align: center;">Loan: Joy bank</td> </tr> <tr> <td style="width: 35%;">Bank CPJ 458 000</td> <td style="width: 35%;">Balance b/d1 125 000</td> </tr> <tr> <td>Balance c/d <u>804 500</u></td> <td>Int. on loan GJ137 500</td> </tr> <tr> <td style="text-align: right;"><u>1 262 500</u></td> <td style="text-align: right;"><u>1 262 000</u></td> </tr> <tr> <td></td> <td>Balance b/d 804 500</td> </tr> </table>	<p><i>To calculate the interest on loan on the Loan Statement:</i> R1 125 000 – R458 000 – R804 500 = R137 500 Interest on loan = 137 500</p>	Loan: Joy bank		Bank CPJ 458 000	Balance b/d1 125 000	Balance c/d <u>804 500</u>	Int. on loan GJ137 500	<u>1 262 500</u>	<u>1 262 000</u>		Balance b/d 804 500
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	<u>1 262 500</u>		<u>1 262 000</u>									
		Balance b/d 804 500										
I.	<p>Income tax for the year is subtracted from the net profit before tax</p>											



All pre-adjustment trial balance figures have been entered in **bold** on the Income Statement before entering the adjustments.

PLEASE NOTE:
Depreciation is normally an involved calculation affecting both vehicles and equipment. For this reason many marks are awarded for the depreciation figure. Show all your workings so that even if one or two of your figures are wrong, you can still get some marks for calculating correctly.





Worked example 3



Balance Sheet and notes

Use the following steps to prepare a balance sheet from the given information:

1. Enter the figures from the information given onto the answer sheet next to the details.
2. Read the additional information:
 - a) If necessary calculate the adjustment amount.
 - b) Decide on which account is to be debited and which account is to be credited.
 - c) On your answer sheet reflect a (+) or a (-) in respect of each item next to the already entered pre-adjustment figure.
3. When all the additional information has been considered, calculate the final figures and write them in the column.

Look at the format you have been given. Do you notice any missing details? Fill them in. THESE ARE EASY MARKS!



Example adapted from November 2009 NCS exam paper

Practice task 3

You are provided with information relating to Qwando Limited for the financial year ended 30 June 2011.

Prepare the Retained income note. (18)

Prepare the Balance Sheet on 30 June 2011. (36)

Information

1. The following figures were taken from the financial records of the financial year ended 30 June 2011.

	R
Ordinary share capital (see information 2 below)	2 400 000
Retained income (on 1 July 2010)	738 000
Shareholders for dividends (see information 4 below)	?
Fixed deposit at Supa Bank (see information 5 below)	60 000
Mortgage Bond from Supa Bank (see information 7 below)	?
Fixed/tangible assets	3 881 000
Debtors' control	45 000
Creditors' control	85 200
Creditors for salaries	12 300
Provision for bad debts (see Information 6 below)	?
SARS (Income tax – provisional tax payments)	400 000
SARS (PAYE)	6 650
Expenses payable (accrued)	7 200
Income receivable (accrued)	7 950
Bank (favourable balance)	168 450
Trading stock	129 600
Consumable stores on hand	5 600



Use the **issued** shares to calculate the dividends.

2. Shares:

- There were 700 000 ordinary shares in issue at the beginning of the financial year.
- On 1 January 2011, 100 000 ordinary shares were issued to the public at R3,80 cents per share. This has been correctly recorded and is included in the figures above.
- On 1 June 2011, 40 000 were repurchased from a shareholder at R4,50 per share. A direct transfer was put through from the Bank account but no entry has been made in the books.

3. The net profit before tax for the year ended 30 June 2011 was calculated as R1 250 000. No entry for income tax calculated at a rate of 30% of the net profit has been made.

4. Dividends were as follows:

- Interim dividends of 20 cents per share were paid on 31 December 2010.
- Final dividends of 35 cents per share were declared on 30 June 2011. All shareholders at this date qualify for dividends.

5. One third of the total fixed deposits mature on 31 August 2011.

6. Provision for bad debts must be adjusted to 5% of debtors.

7. The loan statement from Supa Bank on 30 June 2011 reflects the following:

SUPA BANK	
LOAN STATEMENT ON 30 JUNE 2011	
Balance on 1 July 2010	R384 000
Interest charged	57 600
Monthly instalments in terms of the loan agreement (12 × R8 800) (These monthly instalments include interest on the capital repayments of the loan)	105 600
Balance on 30 June 2011	R336 000

The monthly capital repayments on the loan will **remain constant** until the loan has been paid in full on 30 June 2019.

Answers to practice task 3

	RETAINED INCOME	R
	Balance on the last day of the previous year	✓ 738 000
3	Net profit after tax for the period ✓ (1 250 000 - 30%)	✓✓ 875 000
2	Retained income on 40 000 shares repurchased (40 000 × R1,50)	✓✓ (60 000)
	Ordinary share dividends ✓	✓ (406 000)
4	Paid ✓ (interim) (700 000 ✓✓ shares × 20c ✓)	✓ 140 000
2 & 4	Recommended ✓ (final) (760 000 ✓ shares × 35c ✓)	✓ 266 000
	Balance on the last day of the current year	✓ 1 147 000

Total dividends (interim and final) are shown here.

[16]

Qwando Limited
Balance Sheet on 30 June 2011

	ASSETS		
	NON CURRENT ASSETS		3 921 000
	Fixed / tangible assets (4 021 000)		✓3 881 000
	Financial assets		
5	Fixed deposit: Supra Bank (60 000✓ - 20 000✓)		✓40 000
	CURRENT ASSETS		✓ 219 350
	Inventories (129 600✓ + 5 600)		✓ 135 200
6	Trade and other receivables (45 000✓ + 7 950✓ - 2 250✓ + 25 000)✓		✓ 75 700
5	Cash and cash equivalents (168 450 + 20 000✓ - 120 000 - 60 000)		✓ 8 450
	TOTAL ASSETS		✓ 4 140 350
	EQUITY AND LIABILITIES		
	CAPITAL AND RESERVES		✓ 3 427 000
2	Ordinary share capital (2 400 000 - 120 000)		✓ 2 280 000
2	Retained income (see note on previous page)		✓ 1 147 000
	NON-CURRENT LIABILITIES		✓ 288 000
7	Mortgage loan: Supa Bank (336 000✓ - 48 000✓)		288 000
	CURRENT LIABILITIES		✓ 425 350
	Trade and other payables (85 200✓ + 12 300 + 6 650✓ + 7 200✓)		✓111 350
4	Shareholders for dividends		✓✓ 266 000
7	Current portion of loan		✓✓ 48 000
	TOTAL EQUITY AND LIABILITIES		✓ 4 140 350



FORMAT

It is VERY important to know the format of the Balance Sheet and notes!

Fixed assets are always shown at book value on the Balance Sheet.

Amount owed by SARS to the business. This implies the business overpaid its taxes to SARS.

If the notes are not required, show all your calculation work in brackets on the Balance Sheet



This is the **final** dividend declared at the end of the year.



The numbers in this column refer to the explanations on the next page.

[38]



All given figures in information 1 have been entered in bold before entering the information 2 to 7.

Explanations of each adjustment

2.	<p>Shares:</p> <p>The new issue of shares have been properly recorded. The repurchase of 40 000 shares at R4,50. The ordinary share capital account must be reduced by the average share price ($2\,400\,000 \div 800\,000$ shares = R3)</p> <p>The retained income account will be reduced by the difference between the buyback price and average price ($R4,50 - R3 = R1,50 \times 40\,000$ shares)</p>
3.	<p>Net profit after tax must be calculated by subtracting income tax from net profit before tax. This must be entered in the retained income note.</p> <p>Tax calculation = $(R1\,250\,000 \times 30\% = R375\,000)$.</p> <p>Net profit after tax = $R1\,250\,000 - R375\,000 = R875\,000$.</p>
4.	<p>Dividends:</p> <p>Calculation of interim/paid dividends = $700\,000 \times 20$ cents = R140 000</p> <p>Calculation of final/declared dividends = $700\,000 + 100\,000$ (issued) - $40\,000$ (repurchased) = 760 000 shares</p> <p>$760\,000 \times 35$ cents = R266 000</p> <p>Total dividends = $R140\,000 + R266\,000 = R406\,000$</p>
5.	<p>Calculation of short term portion of fixed deposit:</p> <p>The portion of the fixed deposit that will be received within the next 12 months must be subtracted from financial assets and shown under cash and cash equivalents under current assets on the balance sheet. ($1/3$ of R60 000 = R20 000)</p>
6.	<p>Provision for bad debts is calculated at 5% of debtors control:</p> <p>5% of R45 000 = R2 250.</p> <p>Provision for bad debts must be subtracted from trade and other receivables.</p>
7.	<p>Repayments of the capital amount of the loan that will be made in the next 12 months must be subtracted from the non-current liabilities and shown under current liabilities as a 'current portion of loan'.</p> <p>$R105\,600$ (total repayments) - $R57\,600$ (interest) = R48 000 (capital portion of repayments for the year).</p>

Practice task 3 (continued)

RETAINED INCOME		R
Balance on the last day of the previous year		
Balance on the last day of the current year		

QWANDO LIMITED BALANCE SHEET ON 30 JUNE 2011	
ASSETS	
NON CURRENT ASSETS	
Fixed/tangible assets	
Financial assets	
Fixed deposit: Supra Bank	
CURRENT ASSETS	
TOTAL ASSETS	
EQUITY AND LIABILITIES	
CAPITAL AND RESERVES	
NON-CURRENT LIABILITIES	
Mortgage loan: Supa Bank	
CURRENT LIABILITIES	
TOTAL EQUITY AND LIABILITIES	

[38]

Photocopy this blank Balance Sheet and use it to practise doing the worked example 3 again on your own. Once you have completed the task, compare your answer to the worked example on the previous page.



Some important notes to the financial statements



FORMAT

It is VERY important to know the format of the notes to the Financial Statements. Some of them are explained below.

	TANGIBLE/FIXED ASSETS	LAND & BUILDINGS	VEHICLES	TOTAL
$A - B = C$	Carrying value at beginning of year	C	C	C
	Cost	A	A	A
	Accumulated depreciation	(B) = 0	(B)	(B)
	Movements			
	Additions	D	D	D
	Disposals at carrying value	(E)	(E)	(E)
LAND AND BUILDINGS ARE NOT DEPRECIATED. A zero will always be shown in these blocks.	Depreciation	(F) = 0	(F)	(F)
	Carrying value at end of year	J	J	J
	Cost	H	H	H
	Accumulated depreciation	(I) = 0	(I)	(I)

$C + D - E - F = J$
OR
 $H - I = J$

The total carrying value gets transferred to the Balance Sheet.

TRADE & OTHER RECEIVABLES		
Net trade debtors	M	$K - L = M$
Trade debtors	K	
Provision for bad debts	(L)	
SARS (income tax)	N	Amount overpaid to SARS.
Expenses prepaid	O	
Income accrued (receivable)	P	
	Q	$M + N + O + P = Q$ Transfer Q to the current assets section in the Balance Sheet.

TRADE & OTHER PAYABLES		
Trade creditors	R	
Expenses accrued (payable)	S	
Income received in advance	T	
Shareholders for dividends	U	Dividend declared but not yet paid (final dividend).
SARS (income tax)	V	Amount still owing to SARS.
Creditors for salaries	W	Gross salaries less deductions.
Unemployment insurance fund	X	Deductions + contributions.
Pension fund	Y	
Medical aid fund	Z	
	AA	AA: Total transferred to current liabilities section of the Balance Sheet.

2.4 Cash Flow Statements



FORMAT

It is **VERY** important to know the format of the Cash Flow Statement and notes!

Purpose of a Cash Flow Statement

The Income Statement shows the result of business' operations (net profit).

The Balance Sheet shows the financial position of the business on a specific day (ie how much the business is worth).

Neither of them shows where the business gets its funds from or how the funds are used. The emphasis is on the cash aspects/components.

The Cash Flow Statement is prepared for this purpose and shows where the funds come from and how they are used.

Basic concepts and terminology



Cash Flow Statements focus on all aspects of **CASH** surrounding a business. Remember **CASH IS KING** for Cash Flow Statements.

Concept	Definition
Cash inflow	Money coming into the business. This amount does NOT have brackets. (e.g. sale of shares)
Cash outflow	Money going out of the business. This amount HAS brackets. (e.g. bought a fixed asset for cash)

All the information needed for a cash flow statement and notes can be found on the income statement, balance sheet and notes.



Worked example 4

Preparation of the cash flow statement



Certain figures have been given on the answer sheet (**in bold**). In order to calculate the missing figures **A** to **L**, refer to additional information provided below.

Practice task 4

Prepare the cash flow statement (all relevant notes have been done for you). (15)

Remember we are looking for the flow of cash. This means you will need to calculate the **difference** between **this year's** and **last year's figures**, to determine the figures to place on the Cash Flow Statement.

Additional information

Extract from balance sheet

	2012	2011	Flow of cash	
Ordinary share capital	R471 600	R410 000	**see note below	
Retained income	R10 400	R9 000	This has no effect on a cash flow statement.	
Fixed deposit	R28 000	R23 000	(R5 000)	(Outflow)
Loan from Beta Bank (interest is not capitalised)	R74 000	R80 000	(R6 000)	(Outflow)
Bank	R35 300	R10 040	R25 260	Inflow
Cash float	R2 000	R2 000	R0	No change

** During the year the following transactions took place regarding share capital:

- 8 000 Shares were issued and the company received R79 600 from shareholders.
- Repurchased 3 000 shares at 820 cents per share

Notes to the cash flow statement

Note 1: Reconciliation between profit before tax and cash generated from operations:

		R
Profit before tax		30 000
Adjustments i.r.o. (in respect of):		21 200
Depreciation		12 000
Interest expense		9 200
Operating profit before changes in working capital		51 200
Changes in working capital		5 000
(Increase)/Decrease in inventory		(3 000)
(Increase)/ Decrease in debtors		5 600
Increase /(Decrease) in creditors		2 400
Cash generated from operations		56 200

Make sure you use the profit **before** tax from the Income Statement. If profit after tax is given, remember to add back the tax.

These figures are taken **DIRECTLY** from the Income Statement and are **ADDED** to the profit before tax to give you the operating profit before changes in working capital. Also, depreciation is **NOT** a cash expense.

Difference between last year's and this year's figures. Remember to exclude amounts owed to shareholders, accrued interest and amounts owed to or by SARS for income tax.

Transfer this figure to the Cash Flow Statement (cash flow from operating activities).

Note 2: Cash and cash equivalents



Net change is calculated as the difference between last year's and this year's figures.

ATTENTION: Watch your dates! Make sure you are using the figures from the correct year.

	Net change	2012	2011
Bank	25 260	35 300	10 040
Cash float	0	2 000	2 000
	25 260	37 300	12 040

These amounts come **DIRECTLY** from cash and cash equivalents on the Balance Sheet.

Transfer these figures to the Cash Flow Statement (net change in cash and cash equivalents).



The notes for dividends paid and tax paid can be done using either the format given below or the ledger account (not required in this question).



SARS can have a debit or credit balance at the beginning of the year and at the end of the year.

Note 3: Dividends paid

Total dividends for the year (interim + final)	(R10 000)
Amount due at the beginning of the year [dr (cr)]	(R4 500)
Amount due at the end of the year (final) [(dr) cr]	R6 000
Dividends paid	(R8 500)

This figure is **always shown in brackets**.

Last year's shareholders' for dividends amount. This figure is **shown in brackets** because it was paid during the year.

This year's shareholders for dividends amount. This figure is **NOT shown in brackets** because it is still not paid.

This is the total amount paid out for dividends this year. This figure is **shown in brackets** on the Cash Flow Statement (cash flow from operating activities)



Before you attempt a Cash Flow Statement question, ensure that you can identify the information that is given to you to determine if you have to complete notes or simply show all your working calculations.

Note 4: Taxation paid

Total tax for the year	(R13 500)
Balance due at the beginning of the year [dr (cr)]	(R1 600)
Balance due at the end of the year [(dr) cr]	R1 200
Tax paid	(R13 900)

The income tax figure from the Income Statement. This figure is **shown in brackets**.

Last year's SARS income tax balance. If the figure is under **trade and other payables it will have brackets**. If the figure is under **trade and other receivables it will not have brackets**. [(dr) cr]

This year's SARS income tax balance. If the figure is under **trade and other payables it will not have brackets**. If the figure is under **trade and other receivables it will have brackets**. [(dr) cr]

This is the total amount paid out for tax this year. This figure is **shown in brackets** on the Cash Flow Statement (cash flow from operating activities) as this was the **ACTUAL** cash that was paid.

Cash Flow Statement for the year ended ...

	NOTES	R	
Cash flow from operating activities		✓ 24 960	A
Cash generated from operations	1	✓ 56 200	B
Interest paid		(8 840)	
Dividends paid	3	✓ (8 500)	C
Income tax paid	4	✓ (13 900)	D
Cash flow from investing activities		✓ (48 700)	E
Purchase of fixed assets		(48 500)	
Proceeds from sale of fixed assets		4 800	
Increase of investment		✓✓ (5 000)	F
Decrease of investment		-	
Cash flow from financing activities		✓ 49 000	G
Proceeds from shares issued		✓ 79 600	H
Repurchase of shares		(24 600)	I
Proceeds from long-term loans		-	
Payment of long-term loans		✓ (6 000)	J
Net change in cash and cash equivalents	2	✓ 25 260	K
Cash and cash equivalents at the beginning of the year	2	✓ 12 040	L
Cash and cash equivalents at the end of the year	2	✓ 37 300	M

Operating activities:

The most common source of cash for a company. It not only involves the buying and selling of stock, but also includes paying creditors, receiving money from debtors and paying expenses.

Investing activities:

The activities that focus on the buying and selling of fixed assets and the increasing and decreasing of investments (e.g. fixed deposits).

Financing activities:

How a company is funded through loans and capital:

- The issuing of shares
- The repurchase of shares
- The obtaining of a loan
- The repayment of a loan

To check your answer, see K, L + M:

- If both balances are favourable you subtract, eg. $37\,300 - 12\,040 = 25\,260$.
- If one of the balances is an overdraft, then you add, eg. $M + (L)$.

- An overdraft is shown in brackets (). Memorise the following to determine if K is in brackets or not:

(K)		K
L	or	(L)
(M)		M

The letters in this column refer to the explanations in the Table on page 28.



[15]

Explanations of A to L

A.	Cash generated from operations – interest paid – dividends paid – income tax paid = A $R56\,200 - R8\,840 - R8\,500 - R12\,900 = R24\,960$ Inflow (Outflow) (Outflow) (Outflow) Inflow
B.	Cash generated from operations transferred from Note 1 (under Notes to the Cash Flow Statement).
C.	Dividends paid transferred from Note 3 (under Notes to the Cash Flow Statement).
D.	Income tax paid transferred from Note 4 (under Notes to the Cash Flow Statement).
E.	Purchase of fixed assets – proceeds from sale of fixed assets – increase in investment = E $- R48\,500 + R4\,800 - R5\,000 = - R48\,700$ (Outflow) Inflow (Outflow) (Outflow)
F.	This figure comes from the Extract from the Balance Sheet and is calculated by finding the difference between this year's and last year's figures: $R25\,000 - R20\,000 = R5\,000$ (Outflow) <i>Increasing the fixed deposit is an outflow as money is moving out of the bank account and into the fixed deposit account.</i>
G.	Proceeds from shares issued – repurchase of shares - payment of long-term loans = G $R79\,600 - R24\,600 - R6\,000 = R49\,000$ Inflow (Outflow) – (Outflow)
H.	Issue of new shares: The amount of R79 000 was given (inflow)
I.	Repurchase of shares: $3\,000 \times R8,20 = R24\,600$ (outflow)
J.	This figure comes from the Extract from the Balance Sheet and is calculated by finding the difference between this year's and last year's figures: $R74\,000 - R80\,000 = -R6\,000$ (Outflow)
K.	A – E + G = K ($R24\,960 - R48\,700 + R49\,000 = R25\,260$) To verify this figure check the Net Change Total in Note 2 (Cash and Cash Equivalents) under Notes to the Cash Flow Statement
L.	This figure comes from the extract from the Balance Sheet, calculated by adding the Bank figure and Cash Float figure from <u>last year</u> i.e. 2011. To verify this figure check the total of the Bank and Cash Float figure for 2011 in Note 2 (Cash and Cash Equivalents) under Notes to the Cash Flow Statement.
M.	This figure comes from the extract from the Balance Sheet, calculated by adding the Bank figure and Cash Float figure from <u>this year</u> i.e. 2012. To verify this figure check the total of the Bank and Cash Float figures for 2012 in Note 2 (Cash and Cash Equivalents) under Notes to the Cash Flow Statement.

Cash flow statement for the year ended

	Notes	R
Cash flow from operating activities		
Cash generated from operations	1	
Interest paid		(8 840)
Dividends paid	3	
Income tax paid	4	
Cash flow from investing activities		
Purchase of fixed assets		(48 500)
Proceeds from sale of fixed assets		4 800
Increase of investment		
Decrease of investment		-
Cash flow from financing activities		
Proceeds from shares issued		
Repurchase of shares		
Proceeds from long-term loans		
Payment of long-term loans		-
Net change in cash and cash equivalents	2	
Cash and cash equivalents at beginning of the year	2	
Cash and cash equivalents at the end of the year	2	

[15]

Photocopy this blank Cash Flow Statement and use it to practise doing the worked example 4 again on your own. Once you have completed the task, compare your answer to the worked example on pages 27 and 28.



2.5 Analysis and interpretation of Financial Statements



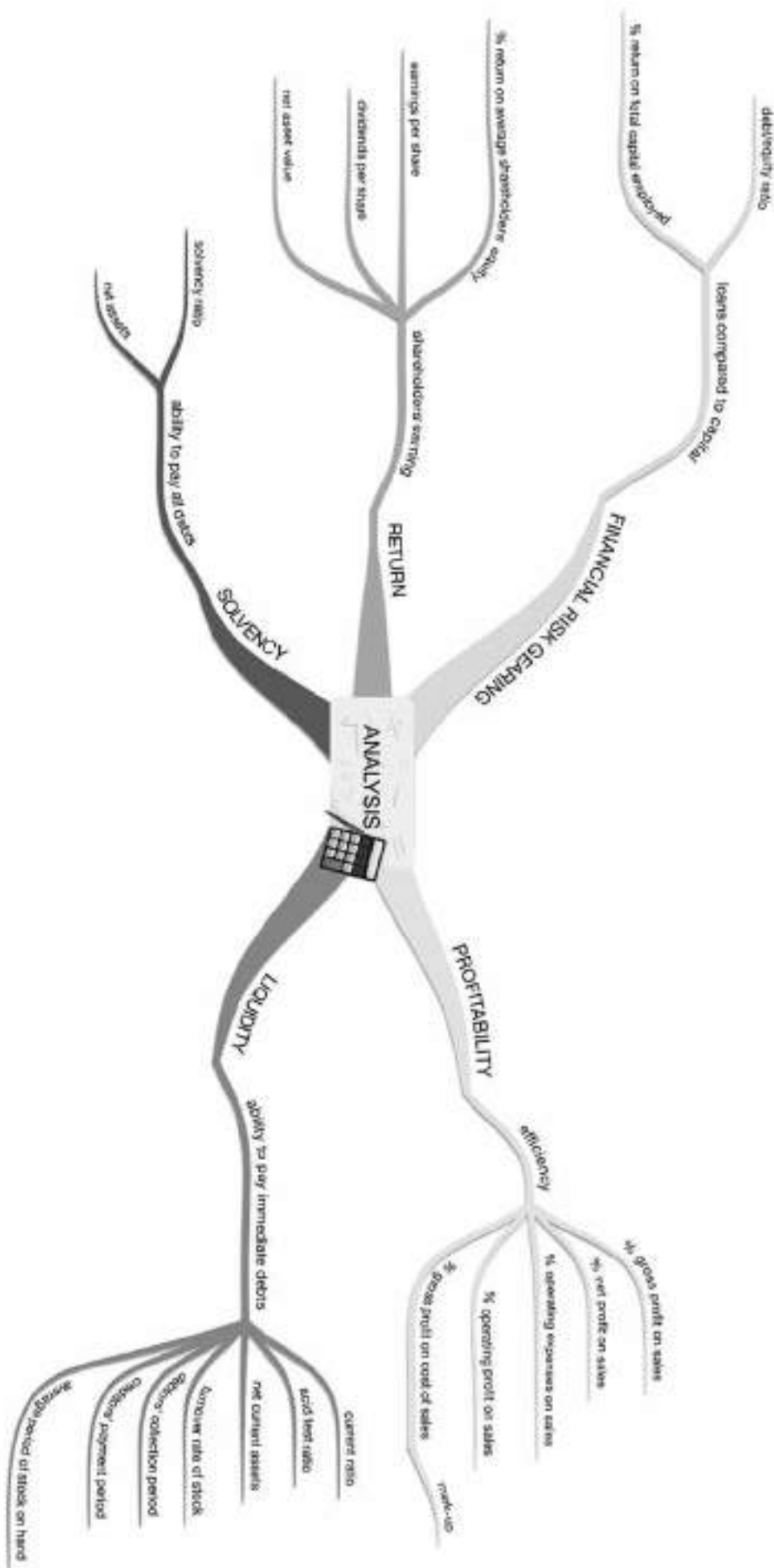
Make sure you can calculate these indicators. See page 35 for formulae.

Area of analysis	Description	Related financial indicators
Profitability	How efficient the company is in its normal operating activities	% Gross profit on sales % Net profit on sales % Operating expenses on sales % Operating profit on sales % Gross profit on cost of sales (mark-up)
Liquidity	The ability of a company to pay off its immediate (short-term) debts	Current ratio Acid test ratio Net current assets (net working capital) Turnover rate of stock Debtors' collection period Creditors' payment period Average period of stock on hand
Solvency	The ability of a company to pay off all its debts	Solvency ratio Net assets
Return	Are the shareholders earning a fair amount on their investment?	% Return on average shareholders' equity Earnings per share Dividends per share Net asset value
Financial risk Gearing	To what extent is the company financed by loans (borrowed money) compared to its own capital	Debt / equity ratio % Return on total capital employed



Follow these steps when commenting on the financial indicators:

1. Consider what the question is asking you to analyse (e.g. Liquidity). Decide on the relevant financial indicator(s).
2. Name the financial indicator(s) giving figures or ratios or percentages.
3. Compare the current year's indicator(s) with that of the previous year. Say whether it has increased or decreased.
4. If possible provide a general comment.





Use point form instead of long sentences to comment.

It means that the company has current assets of R2,10 for every R1 debt.

Earnings per share is the 'if'; if all the profit after tax was declared as dividends, the earnings would have been 35c per share. However what "really happened" is that dividends were declared of only 25c per share. The difference is the profit that the company kept called 'retained income'.

It's the 'if'! If all the profit after tax was declared a dividend, they would have earned 15c per share. However, the shareholders received more, being 20c per share. That means that some of the retained income of the previous year was used to finance the difference.



ATTENTION: Watch your dates! Make sure you use the figures from the correct year.



Worked example 5: Comment on the liquidity position of the company

Financial indicator	2010	2011
Current ratio	1,3 : 1	2,1 : 1
Acid test ratio	0,6 : 1	1,4 : 1

- Current ratio ✓ has improved from 1,3 : 1 to 2,1 : 1 ✓
- Acid test ratio ✓ has also improved from 0,6 : 1 to 1,4 : 1 ✓
- This company is in a good liquidity position and should be able to pay its short-term debt easily. ✓

[5]



Worked example 6: Comment on the earnings per share (EPS) and dividends per share (DPS) of the company

Financial indicator	2010	2011
Earnings per share (EPS)	35c per share	15c per share
Dividends per share (DPS)	25c per share	20c per share

- EPS has declined from 35c to 15c per share. ✓
- DPS has declined from 25c to 20c per share. ✓
- In 2010 their EPS was 35c while the DPS was only 25c per share. This means that the company retained 10c per share for future growth. ✓✓
- In 2011 they only earned 15c per share but gave the shareholders 20c per share meaning that none of this year's profits were retained. ✓✓

[6]



Worked example 7: Comment on the debt/equity ratio of the company

Financial indicator	2010	2011
Debt/equity ratio	0,6:1	0,4:1

- Debt/equity ratio decreased ✓ by 0,2 from 0,6 : 1 to 0,4 : 1. ✓
- By repaying the loan the company has a lower financial risk. ✓

[3]



Worked example 8: Comment on the percentage return on shareholders' equity (ROSHE) of the company

Financial indicator	2010	2011
% return on shareholders' equity (ROSHE)	18 %	24 %

- ROSHE improved ✓ by 6 % from 18 % to 24 %. ✓
- The shareholders should be pleased as a return of 24 % is higher than an alternative investment (e.g. fixed deposit). ✓

[3]

Formulae: Financial indicators



The formula for many of these indicators is given in the name of the indicator.

Financial indicator		How it is calculated - formula	Answer shown as/in
1	Gross profit on cost of sales (mark-up)	$\frac{\text{Gross profit}}{\text{Cost of sales}} \times \frac{100}{1}$	%
2	Gross profit on sales	$\frac{\text{Gross profit}}{\text{Sales}} \times \frac{100}{1}$	%
3	Operating expenses on sales	$\frac{\text{Operating expenses}}{\text{Sales}} \times \frac{100}{1}$	%
4	Operating profit on sales	$\frac{\text{Operating profit}}{\text{Sales}} \times \frac{100}{1}$	%
5	Net profit after tax on sales	$\frac{\text{Net profit after tax}}{\text{Sales}} \times \frac{100}{1}$	%
6	Solvency ratio	Total assets : Total liabilities	Ratio (x : 1)
7	Net assets (shareholders' equity)	Total assets – Total liabilities	Rands
8	Current ratio	Current assets : Current liabilities	Ratio (x : 1)
9	Acid-test ratio	(Receivables + cash) : Current liabilities OR (Current assets – inventories) : Current liabilities	Ratio (x : 1)
10	Turnover rate of stock	$\frac{\text{Cost of sales}}{\text{Average stock}}$	Times per year
11	Period for which enough stock is on hand/period of stock on hand (stock holding period)	$\frac{\text{Average stock}}{\text{Cost of sales}} \times \frac{365}{1}$	Number of days
12	Debtors average collection period	$\frac{\text{Average debtors}}{\text{Credit sales}} \times \frac{365}{1}$	Number of days
13	Creditors average payment period	$\frac{\text{Average creditors}}{\text{Credit sales}} \times \frac{365}{1}$	Number of days
14	Debt/equity ratio	Non-current liabilities : Shareholders' equity	Ratio (x : 1)
15	Return on equity (shareholders' equity)	$\frac{\text{Net profit after tax}}{\text{Average shareholders' equity}} \times \frac{100}{1}$	%
16	Return on total capital employed	$\frac{\text{Net profit before tax + interest on loans}}{\text{Average shareholders' equity + average loans}} \times \frac{100}{1}$	%
17	Earnings per share ('if')	$\frac{\text{Net profit after tax}}{\text{Number of issued shares}} \times \frac{100}{1}$	Cents
18	Dividends per share (what really happened)	$\frac{\text{Interim \& final dividends}}{\text{Number of issued shares}} \times \frac{100}{1}$	Cents
19	Net asset value per share (this is the real value of the share)	$\frac{\text{Shareholders' equity}}{\text{Number of issued shares}} \times \frac{100}{1}$	Cents



OTHER IMPORTANT FORMULAE:

To calculate the selling price (SP):

$$SP = CP \times \frac{100 + \text{mark-up}}{100}$$

Shareholders' equity =

Ordinary share capital
+ Retained income

To calculate the cost price (CP):

$$CP = SP \times \frac{100}{100 + \text{mark-up}}$$



Worked example 9

(This question shows some of the basic financial indicators that will help you earn easy marks)

You are provided with information relating to Glebo Limited for the year ended 30 June 2011.

Practice task 5

Use the given information to calculate the following financial indicators for 2011. (31)

1. % Gross profit on cost of sales (mark-up) ←
2. % Net profit on sales ←
3. % Operating profit on sales ←
4. Current ratio ←
5. Acid test ratio
6. Debt/equity ratio
7. Solvency ratio
8. Net asset value per share ←
9. Earnings per share ←

These calculations use figures taken from the Income Statement ONLY.

These calculations use figures taken from the Balance Sheet ONLY.

This calculation uses figures taken from BOTH the Income Statement and the Balance Sheet.

Information

Glebo Limited

EXTRACT FROM INCOME STATEMENT FOR THE YEAR ENDED 30 JUNE 2011

	2011
Sales	9 000 000
Cost of sales	5 625 000
Operating profit	1 423 200
Income tax	426 000
Net profit after tax	904 000

GLEBO LIMITED
BALANCE SHEET AS AT 30 JUNE 2011

	2011
ASSETS	
Non-current assets	4 626 000
Fixed assets	4 326 000
Financial assets	300 000
Current assets	2 557 000
Inventories (all trading stock)	1 640 000
Trade and other receivables (all trade debtors)	810 000
SARS (Income tax)	0
Cash and cash equivalents	107 000
TOTAL ASSETS	7 183 000
EQUITY AND LIABILITIES	
Ordinary shareholders' equity	4 123 000
Ordinary share capital (1 100 000 shares)	2 910 000
Retained income	1 213 000
Non-current liabilities	1 980 000
Mortgage loan: Jozi Bank (13% p.a.)	1 980 000
Current liabilities	1 080 000
Trade and other payables (all trade creditors)	705 000
SARS (Income tax)	32 000
Shareholders for dividends	275 000
Bank overdraft	0
Current portion of loan	68 000
TOTAL EQUITY AND LIABILITIES	7 183 000

Answer to practice task 5

1.	<p>Calculate % gross profit on cost of sales (mark-up) [4]</p> $\frac{(\text{Sales} - \text{cost of sales})}{\text{Cost of sales}} \times 100 = \frac{9\,000\,000\checkmark - 5\,625\,000\checkmark}{5\,625\,000\checkmark} \times 100$ $= \frac{3\,375\,000}{5\,625\,000} \times 100$ $= 60\%\checkmark$
2.	<p>Calculate % net profit on sales [3]</p> $\frac{\text{Net profit after tax}}{\text{Sales}} \times 100 = \frac{904\,000\checkmark}{9\,000\,000\checkmark} \times 100$ $= 10\%\checkmark$
3.	<p>Calculate % operating profit on sales [3]</p> $\frac{\text{Operating profit}}{\text{Sales}} \times 100 = \frac{1\,423\,000\checkmark}{9\,000\,000\checkmark} \times 100$ $= 15,8\%\checkmark$
4.	<p>Calculate current ratio [3]</p> <p>Current assets ÷ current liabilities</p> $= 2\,557\,000\checkmark \div 1\,080\,000\checkmark$ $= 2,4 : 1\checkmark$
5.	<p>Calculate acid-test ratio [4]</p> <p>(Current assets - stock) ÷ current liabilities</p> $= (2\,557\,000\checkmark - 1\,640\,000\checkmark) \div 1\,080\,000\checkmark$ $= 917\,000 \div 1\,080\,000$ $= 0,85 : 1\checkmark$
6.	<p>Calculate debt/equity ratio [3]</p> <p>Non-current liabilities ÷ ordinary shareholders' equity</p> $= 1\,980\,000\checkmark \div 4\,123\,000\checkmark$ $= 0,48 : 1\checkmark$

Gross profit = sales – cost of sales

In order to get the answer as a percentage, multiply by 100.

This means that 10c of every R1 sales becomes net profit.

This means that the company has R2,40 to pay off R1 debt.

When asked to calculate a ratio, always show your answer as x : 1

Answers to practice task 5 (continued)

7.	<p>Calculate solvency ratio [4]</p> <p>Total assets ÷ total liabilities = 7 183 000✓ ÷ (1 980 000✓ + 1 080 000✓) = 7 183 000 ÷ 3 060 000 = 2,3: 1✓</p>
8.	<p>Calculate net asset value per share [4]</p> $\frac{\text{Ordinary shareholders' equity}}{\text{Number of shares issued}} \times \frac{100}{1} = \frac{4\,123\,000\checkmark}{1\,100\,000\checkmark} \times \frac{100}{1}$ <p style="text-align: right;">= 374,8 cents per share✓</p>
9.	<p>Calculate earnings per share [3]</p> $\frac{\text{Net profit after tax}}{\text{Number of shares issued}} \times \frac{100}{1} = \frac{904\,000\checkmark}{1\,100\,000\checkmark} \times \frac{100}{1}$ <p style="text-align: right;">= 82,2 cents per share✓</p>

Ordinary share capital ÷ par value of shares

Multiply by 100 in order to get the answer in cents per share.

2.6 Comments on an audit report

The need for financial statements: there are several groups of people who will be interested in the financial statements of a business.

Several groups of people who will be interested	Reasons why they are interested in the financial results
<ul style="list-style-type: none"> The owners of the business (shareholders). 	<ul style="list-style-type: none"> owners are interested in the overall health of the business.
<ul style="list-style-type: none"> A potential owner. 	<ul style="list-style-type: none"> may be interested in investing money in the business.
<ul style="list-style-type: none"> The management of the business (board of directors). 	<ul style="list-style-type: none"> use the report for planning purposes, to maintain certain good practices and to improve on areas of weakness.
<ul style="list-style-type: none"> Banks who have lent money to the business. 	<ul style="list-style-type: none"> Banks are interested in whether there are enough assets in the business to cover their loans. These assets can be sold to repay the loans.
<ul style="list-style-type: none"> The employees of the business and trade unions. 	<ul style="list-style-type: none"> They are interested in whether the business is profitable and in negotiating wage increases.
<ul style="list-style-type: none"> SARS, because the company is a legal person and has to pay tax. 	<ul style="list-style-type: none"> SARS is interested in the profit or loss made and the tax that is paid on this.
<ul style="list-style-type: none"> The auditor who has to report to the shareholders by giving his opinion on whether he thinks the financial statements are a fair reflection of the business during the financial year. 	

The role of the auditor is very important for the shareholders because shareholders are not involved in the running of the business

Function of the independent auditor

- The auditor must sign** an Auditors Report which serves as an assurance to the shareholders **that the financial statements are reliable**.
- The auditor** is not required to check every transaction or to check for fraud. Her function **is to give the shareholders her opinion on** whether or not the financial records are a true and fair representation of the company's operations for that year at a specific date at the end of that financial year.
- The shareholders use the true and fair financial statements to make their **decisions**.
- If the auditor becomes **aware of fraud**, then he has a **duty to report** this to the shareholders.
- Auditors are bound by very high ethical standards and can face disciplinary proceedings if they are found to have been negligent in their work.

Quality of auditors

External Auditors should be registered professionals with professional bodies such as South African Institute of Chartered Accountants (SAICA) and the Independent Regulatory Board for Auditors (IRBA). Advantages of companies engaging registered Auditors:

- Auditors are guided by a professional code of ethics.
- Companies are assured of high quality work from qualified Auditors.
- High professional standards are maintained since auditors are answerable to their affiliate bodies.
- Disciplinary measures can be taken against Auditors who are negligent in performing their duties.
- Auditors may be deregistered from professional bodies if they commit any act of misconduct.



- Auditors can be sued for producing a misleading report.
- Auditors may lose future contracts due to the production of substandard work.

The independent auditor and the audit report

An auditor is a person who expresses **an opinion** on financial information and accounting controls. The independent auditor cannot be an employee of the company. She is appointed at the AGM (annual general meeting) by the shareholders, and not by the directors. She charges fees according to the number of hours she expects to spend on the audit.

The opinion of the independent auditor must be based on an assessment of whether the financial statements:

- Have been prepared in such a way as to give a fair representation of the company's activity
- Are understandable and not confusing to the reader
- Are prepared in accordance with GAAP
- Are prepared in accordance with the requirements of the Companies Act.

The role of internal auditors

The internal auditors ensure that the internal controls are tested and play an important role in looking for fraud or mistakes in the business. They need to check, for example, debtors, wages or computer entries in every aspect of the business.

The internal auditor will be an employee of the business organisation and will earn a salary from the company.

The independent auditor (external) will consider the checks carried out by an internal auditor.

Audit reports

Auditors will issue a report after they have completed their work to express an opinion on their findings. Such a report is addressed to the shareholders (owners of the company). The report could be:

- Qualified – a bad report with some irregularities, in which auditors have to state the kind of irregularity noted to the shareholders (qualify their statements).
- Unqualified – good report with minor irregularities if any.
- Withheld/Disclaimer – very bad report in which auditors may recommend further investigations on certain outstanding irregularities before issuing a report.

The word, "STARDIF" will help you to remember what the Code of good governance stands for!

KING CODE: CODE OF GOOD GOVERNANCE: "STARDIF"

S	T	A	R	D	I	F
Social responsibilities	Transparencies	Accountability	Responsible management	Discipline	Independence	Fairness
<ul style="list-style-type: none"> • Contributing to community in which the business operate 	<ul style="list-style-type: none"> • Does things in an open manner (no hidden agenda). 	<ul style="list-style-type: none"> • Able to explain your actions when called to as a business 	<ul style="list-style-type: none"> • Showing critical consideration for certain aspects for example taking care of the environment 	<ul style="list-style-type: none"> • Business must stick to its principles and ethics. 	<ul style="list-style-type: none"> • Business must operate without influence from outside 	<ul style="list-style-type: none"> • Being considerate to your stakeholders and giving them what they deserve.



Worked example 6

EXAMPLE OF AN UNQUALIFIED REPORT

(GOOD REPORT):

You are provided with an extract from the report of the independent auditors:

Audit opinion – To the shareholders:

We have examined the financial statements set out on pages 8 to 20.

In our opinion, the financial statements fairly present, in all material respects, the financial position of the company at 30 June 2009 and the results of their operations and cash flows for the year ended, in accordance with International Financial Reporting Standards (IFRS), and in the manner required by the Companies Act in South Africa.

Barlow & Bokwe

Chartered Accountants (SA)

Registered Accountants and Auditors

Cape Town 6 September 2009

The auditor's function is to give the shareholders who appointed him at the AGM his opinion.

The auditor is not required to check every transaction or to check for fraud.

An auditor only expresses an opinion whether or not the financial records are a true and fair representation of the company's operations for that year at a specific date at the end of that financial year.



The following questions are normally asked in an examination. Make sure that you study the above information before answering the questions.

- 1 State whether the shareholders would be satisfied or dissatisfied with this audit report. Give a reason for your answer. [3]
- 2 Explain why the auditors found it necessary to stipulate the page numbers (that is 8 to 20) in this report. [2]
- 3 Explain why the Companies Act makes it a requirement for public companies to be audited by an independent auditor. [2]
- 4 Explain TWO major consequences for Barlow and Bokwe should they be negligent in performing their duties. [4]
- 5 What actions would Barlow and Bokwe have to perform to verify the Fixed/Tangible Assets figure in the Balance Sheet? Provide THREE points. [3]
- 6 Quinton Qwando, the major shareholder and managing director, has informed the auditors that he intends to buy the unissued shares himself next year without advertising the new issue to the other shareholders or the public. What advice should the auditors give to Quinton? Briefly explain. [4]

Memorandum

1. State whether the shareholders would be satisfied or dissatisfied with this audit report. Give a reason for your answer.

Satisfied ✓

Any valid reason ✓✓

Possible responses

- The financial statements are fairly presented - this is a positive report
- This is an unqualified report
- The auditors did not mention any irregularities

- 2 Explain why the auditors found it necessary to stipulate the page numbers (i.e. 8 to 20) in this report.

They are only responsible for the pages that have been stipulated in the auditors' report ✓✓

- 3 Explain why the Companies Act makes it a requirement for public companies to be audited by an independent auditor.

The shareholders of a company need to have confidence in the company's ability to look after the investment ✓✓

- 4 Name TWO major consequences for Barlow and Bokwe should they be negligent in performing their duties.

Any two valid consequences ✓✓

Possible responses

- Can be sued
- Not be re-appointed as auditors
- Face disciplinary procedures by the professional body

- 5 What actions would Barlow and Bokwe have to perform to verify the Fixed/Tangible Assets figure in the Balance Sheet? Provide THREE points.

Three actions ✓✓✓

Possible responses

- Examine the financial records of the business – external audit
- Assess the internal control of the business
- Assess the accounting principles used by the business
- Inspect the fixed asset register

- 6 Quinton Qwando, the major shareholder and managing director, has informed the auditors that he intends to buy the unissued shares himself next year without advertising the new issue to the other shareholders or the public. What advice should the auditors give to Quinton? Briefly explain.

Advice: This is unethical and the issue of new shares should be advertised to all according to the Memorandum and Articles of Association, as this is a public company. ✓✓

Explanation: The other shareholders will be disadvantaged, as Quinton will be increasing his shareholding percentage, which will effectively reduce the returns and dividends that the others are earning. By offering the shares on the open market the company could raise more money than if they sold at an agreed price to one buyer. ✓✓

Any valid explanation.

External Auditors should be registered professionals with professional bodies such as South African Institute of Chartered Accountants (SAICA). This is to protect the shareholders and to ensure that continuous training takes place.

Remember that all fixed assets are recorded in an Asset register. Every fixed asset has its own entry in the asset register from the time bought, the yearly depreciation till the date of disposal.

It's a good idea to learn and understand "STARDIF" for this type of question:

- Transparency
- Accountability
- Responsible management
- Discipline
- Fairness



EXAMPLES OF AN UNQUALIFIED AND A QUALIFIED AUDIT REPORT

You are provided with extracts from the independent audit reports of Kwela Ltd and Pomi Ltd.

Unqualified – good report in which there are minor irregularities if any.

Extract from audit report of Kwela Ltd:

In our opinion, the financial statements fairly present, in all material respects, the financial position of this company at 28 February 2012 and the results of their operations and cash flows for the year ended in accordance with International Financial Reporting Standards, and in the manner required by the Companies Act of South Africa.

Qualified – a bad report with some irregularities in which auditors have to state the kind of irregularity noted to the shareholders (qualify their statements).

Extract from audit report of Pomi Ltd:

In our opinion, except for the effects of the company's overvaluation of its fixed assets, the financial statements fairly present the financial position of the company on 29 February 2012 and the results of their operations and cash flows for the year ended in accordance with International Financial Reporting Standards, and in the manner required by the Companies Act of South Africa.

REQUIRED:

Consider the audit reports of Kwela Ltd and Pomi Ltd.

How would these audit reports influence James in deciding in which company to buy shares? Explain in respect of each company.

Memorandum

1. How would these audit reports influence James in deciding in which company to buy shares?

Explanation on the audit report of Kwela Ltd ✓✓

- James will know that he can rely on the figures in the financial statements as the company has received an unqualified audit report
- James will know that he can rely on the figures in the financial statements as there is fair presentation in all material respects
- The report is unqualified – it is a good (i.e. reliable) report.

Explanation on the audit report of Pomi Ltd ✓✓✓

- James will know that he cannot rely on the figures in the financial statements as the company has received a qualified audit report
- James will know that he cannot rely on the figures in the financial statements as they drew attention to shortcomings in the financial statements
- James will be unhappy because the fixed assets had been overvalued in the opinion of the auditors (which means that the true value of his possible investment is not certain as indicated by the net asset value).



EXAMPLE OF A WITHHELD /DISCLAIMER AUDIT REPORT

MAR 2009

Refer to the newspaper article provided.

JSE suspends Woodview Ltd over no annual report

By Ima Snoop, 12 Feb 2009

The trading of shares of furniture company Woodview Ltd were suspended by the JSE Securities Exchange yesterday after the company failed to publish its annual report three months after the end of their financial year-end.

The CEO of Woodview Ltd put out a statement explaining that the auditors had withheld their report and that this was causing a delay.

The company postponed its AGM. The shareholders have not been informed of the reason for the postponement.

Prior to the JSE's action, the share price of Woodview Ltd dropped 30% to 140 cents per share.

The directors of Bhaga Toys Ltd are worried that a similar problem could occur in their company. Briefly explain why this would be a serious problem for the company. Provide two points

Withheld – very bad report in which auditors may recommend further investigations on certain outstanding irregularities before issuing a report.

If the auditor becomes aware of fraud, then he has a duty to report this to the shareholders.

Auditors are bound by very high ethical standards and can face disciplinary proceedings if they are found to have been negligent in their work.

Memorandum

Refer to the newspaper article provided. The directors of Bhaga Toys Ltd are worried that a similar problem could occur in their company. Briefly explain why this would be a serious problem for the company. Provide two points.

Any two valid explanations ✓✓✓ ✓✓✓

- A delay would cause shareholders to become suspicious
- Shareholders would not vote for these directors next year
- New shareholders will avoid the company and share prices could drop
- The directors would be guilty of a criminal offence. In terms of the Companies Act they have to produce financial statements within three months
- It will affect the ability to raise capital/loans in future as investors will be suspicious






Keep going!

3 Chapter

Manufacturing

The manufacturing process is divided into 3 departments:

Administration department	Factory	Selling and distribution department
<p>Office duties are performed in this department and include financing and investing activities.</p> 	<p>Raw materials are taken through the manufacturing process in order to produce finished goods.</p> 	<p>This department is responsible for the advertising, selling and delivery of the finished goods to customers.</p> 
Related costs		
Administration department	Factory	Selling and distribution department
<p>Accountant's salary Bookkeeper's salary Receptionist's salary Cleaning staff wages Office stationery Office rent Insurance on office equipment Depreciation on office equipment Office telephone</p>	<p>Direct costs Raw/direct materials Factory workers' wages/salaries (direct labour)</p> <p>Indirect costs/factory overheads Factory foreman's salary (indirect labour) Cleaning staff wages/salary (indirect labour) Indirect materials/consumable stores Factory rent Factory maintenance Factory insurance Depreciation on factory equipment</p>	<p>Sales manager's salary Sales representative's commission Salary of deliverymen Bad debts Advertising Stationery costs Rent Depreciation on delivery vehicle Cellphone costs of sales staff</p>

3.1 Important concepts of manufacturing

Costs in the manufacturing process

Concept	Explanation
Direct labour cost	Wages and salaries of those employees physically making the product or operating the machines making the product.
Direct/raw materials cost	Raw materials that have been issued to the factory and have been used to manufacture the finished goods. E.g. leather and rubber soles in the making of shoes.
Factory overhead costs	All other costs involved in the manufacturing process which increase the cost of producing the product.

Use mobile notes to help you learn these manufacturing concepts. See page ix for more information.



Stocks in a manufacturing business

Concept	Explanation
Finished goods stock	Products that are completely finished and are ready for sale.
Factory indirect materials/consumable stores stock	The indirect materials that have not yet been used and are still available to be used, e.g. cleaning materials left over.
Raw materials stock	The raw materials left over that have not yet been issued to the factory but are stored safely in the warehouse for future use.
Work-in-process stock	Products that have not been completely turned into finished goods and are still in the manufacturing process.
Fixed costs	These are costs that do not change according to number of products made. For example, the rent of the factory plant will be the same no matter whether 1 000 units are made or 100 000 units are made.
Variable Costs	These costs will increase when production increases. For example, the cost of raw materials used will be far less if 1 000 units are made compared to if 100 000 units are made.



It is important to understand that costs can be further divided into: fixed costs and variable costs.

For exam purposes it will be assumed that all factory overhead costs and admin costs will be **fixed costs**, unless otherwise stated.

For exam purposes it will be assumed that raw materials, direct labour and selling and distribution costs will be **variable costs**, unless otherwise stated.

Flow from the raw material in the store room through the factory to the finished goods in the show room.

- Study the following illustration and see the horizontal flow of funds from the storeroom to the factory and then to the show room.
- Now study the illustration vertically.
 - See how the **STORE ROOM** is presented in the general ledger as the Raw Material stock account and in Note 1 of the Production Cost Statement.
 - See how the **FACTORY** is presented in the general ledger account as Work in Process stock account and as the PRODUCTION COST STATEMENT.
 - See how the **SHOW ROOM** is presented in the general ledger account as the Finished Goods stock account and in Note 4 of the Production Cost Statement.

Storeroom

In the storeroom the raw material and the consumable stores on hand are kept

1. You have stock on hand
2. You purchase new raw materials- cash or credit
3. You transfer raw materials to the factory (called COST OF RAW MATERIAL ISSUED TO FACTORY)

Factory

1. You have uncompleted stock on hand.
2. In the factory the raw materials that you received from the storeroom are taken through the manufacturing process.
3. You have a manager, cleaners and security- indirect labour
4. You have employees who are directly involved in the product- direct labour
5. You have overhead cost; rent expense, water and electricity, depreciation, etc.
6. Then you have the completed goods that are transferred out of the factory to the selling and distribution department. This figure is the COST OF PRODUCTION OF FINISHED GOODS

Show room

1. You have finished goods on hand
2. Received finished goods from the factory,
3. You sell goods and the finished goods decreased at cost price. (Cost of Sales)

ILLUSTRATION OF ABOVE IN THE GENERAL LEDGER ACCOUNTS

Raw Material stock account	
Balance ① b/d 10	Creditors CAJ 5
Bank ② CPJ 20	Work in process ③ 40
Creditors ② CJ 30	Balance c/d 15
	60
Balance b/d 15	

Work in Process stock account	
Balance ① b/d 150	Finished Goods ⑥ GJ 205
Raw material GJ ② 40	Balance c/d 45
Direct Labour GJ ④ 85	
Factory GJ overheads 35	
	250
Balance b/d 45	

Finished goods stock account	
Balance ① b/d 100	Cost of sales 250
Work in process ② 205	Balance c/d 55
	305
Balance b/d 55	

Consumable stores on hand account	
Consumable stores on hand 3 GJ	Creditors CAJ 3
Bank CPJ 4	Factory overheads (used) 5
Creditors CJ 5	Consumable stores on hand 4
	12

Factory overheads account	
Consumable stores (used) 5	Work in Process 35
Indirect Labour ③ 15	
Water and Elec 5	
Rent expense 5	
Depreciation 5	
	35

Cost of Sales account	
Finished Goods 250	

ILLUSTRATION OF ABOVE IN THE FINANCIAL STATEMENTS

Note 1	
NOTE :1	
Opening stock	10
Plus Purchases (net)(20 + 30 - 5)	45
Plus carriage on purchases	0
Less Closing stock	(15)
= Raw material issued to factory	40
If you know the ledger accounts, you know the Production Cost Statement as well!	

Factory Production Cost Statement	
Direct materials cost	40
+ Direct labour cost	85
= Prime/Direct cost	125
+ Factory overhead cost	35
= Total cost of production	160
+ Work-in process at the beginning of the year	150
- Work-in process at the end of the year	(45)
= Total cost of production of finished goods	205
The Work in Process Account is the Production Cost Statement	

Note 4	
NOTE 4	
Opening stock	100
Plus Cost of Production of finished goods	205
Minus Closing stock	(55)
= Cost of sales	250

Study the following template and see the similarities between the General ledger accounts and the Production Statement.

If you understand the flow of the ledger accounts from the raw materials to the finished goods, you will be able to learn the format and understand the Production Statement well.

GENERAL LEDGER ACCOUNTS						PRODUCTION COST STATEMENT			
Dr						Raw material stock		Cr	
Balance	b/d	10 20	Creditors contr.	CAJ	5				
Bank	CPJ	30	Work in process	GJ	40				
Creditors contr	CJ		Balance	c/d	15				
		60			60				
Balance	b/d	15							
Dr						Work in process		Cr	
Balance	b/d	150	Finished goods	GJ	205				
Raw material	GJ	40	Balance	c/d	45				
Direct labour	GJ	85							
Factory overheads	GJ	35							
		250			250				
Balance	b/d	45							
Dr						Finished Goods		Cr	
Balance	b/d	100	Cost of Sales	GJ	250				
Work in process	GJ	205	Balance	c/d	55				
		305			305				
Balance	b/d	55							
Dr						Factory overheads		Cr	
Consumable stores		5	Work in process		35				
Indirect labour		15							
Water and elec.		5							
Rent expense		5							
Depreciation		5							
		35			35				
						Note 1: Raw material/ Direct material cost			
						Opening stock		10	
						+ Purchases(net) (20 + 30 - 5)		45	
						+ Carriage on purchases		-	
						+ Custom duties		-	
						- Closing stock		(15)	
						= Stock issued (Direct material cost)		40	
						PRODUCTION COST STATEMENT			
						Direct materials cost		40	
						+ Direct labour cost		85	
						= Prime/Direct cost		125	
						+ Factory overhead cost		35	
						= Total cost of production		160	
						+ Work-in process at the beginning of the year		150	
						- Work-in process at the end of the year		(45)	
						= Cost of production of finished goods		205	
						Note 4: Cost of finished goods(Cost of sales)			
						Opening stock		100	
						+ Cost of Production of finished goods		205	
						Closing stock		(55)	
						= Cost of sales		250	
						Note 3 Factory overhead costs			
						Consumable stores (3 + 4 + 5 - 3 - 4)		5	
						Indirect labour		15	
						Water and electricity		5	
						Rent expense		5	
						Depreciation		5	
						Total factory overheads used		35	

3.2 Production Cost Statement



Worked example 1

Example adapted from November 2010 NSC Exam Paper

You are provided with information (balances, transactions and adjustments) relating to Fatima Manufacturers owned by Fatima Fala. The business manufactures shoes.

Required

This is direct materials cost (see definition on page 39).

1. Calculate the value of the raw materials **that were issued** to the factory for the year ended 28 February 2010. [6]
2. Prepare the following notes to the Production Cost Statement for the year ended 28 February 2010:
 - 2a) Direct labour cost [5]
 - 2b) Factory overhead cost [16]
3. Prepare the Production Cost Statement for the year ended 28 February 2010. [12]
4. Using the figures in the Production Cost Statement you have just prepared, calculate the following (show your workings):
 - 4a) Raw materials cost per unit [3]
 - 4b) Total cost per unit [3]
5. You are provided with the number of units produced and the break-even point calculated for the past two years:

	2010	2009
Break-even point	19 548 units	11 300 units
Number of units produced	20 000 units	24 000 units

- 5a) Briefly explain what the term break-even point means. [2]
- 5b) Explain whether Fatima should be concerned about the break-even point for 2010. Quote figures to support your answer. [4]

Information

Fatima Manufacturers

1. OPENING BALANCES ON 1 MARCH 2009:

Raw materials stock	R160 000
Work-in-process stock	158 000
Finished goods stock	120 000
Consumable stores stock: Factory	6 000
Factory plant and equipment at cost	2 225 000
Accumulated depreciation on factory plant and equipment	450 000

2. SUMMARY OF TRANSACTIONS FOR THE YEAR ENDED 28 FEBRUARY 2010:

Purchases of raw materials on credit	R1 023 475
Carriage on purchases of raw materials	22 500
Consumable stores purchased for the factory	43 000
Cleaning materials purchased for the office	12 000
Factory plant and equipment purchased on 1 September 2009	250 000
Production wages	723 800
UIF – contribution for factory employees	
Salaries: Factory foreman	150 000
Administration	400 000
Sales staff	250 000
Water and electricity	163 000
Sundry expenses: Factory	194 680
Administration	530 000
Sales department	340 000

3. CLOSING BALANCES ON 28 FEBRUARY 2010:

Raw materials stock	R259 125
Work-in-process stock	122 900
Finished goods stock	142 500
Consumable stores stock: factory	7 000

4. ADDITIONAL INFORMATION AND ADJUSTMENTS:

- a) No entry was made for the transport of raw materials by Pops Carriers to the factory, R3 750.
- b) No entry was made for the following in respect of the **production wages** for the last week of February 2010. The entry was omitted (left out) from the wages journal:

Gross wages	R6 200
Deductions: Unemployment Insurance Fund	62
PAYE	1 240

The employer contributes 1% to the UIF.

- c) An amount of R4 200 was still outstanding on the water and electricity account for February 2010. Sixty per cent (60%) of all the water and electricity was used in the factory.
- d) Depreciation on factory plant and equipment must be brought into account at 10% per annum, according to the diminishing balance method.
- e) During the year 20 000 pairs of shoes were manufactured.

Direct labour cost

Answers to worked example 1 (see pages 40–41)

1. Value of raw materials issued:

DIRECT MATERIALS COST	
Opening balance of raw material stock	R160 000 ✓
Add: Purchase of raw materials	+ R1 023 475 ✓
Add: Carriage on purchases of raw materials	+ R22 500 ✓
Add: Transport of raw materials (adjustment A)	+ R3 750 ✓
Less: Closing balance of raw material stock	– (R259 125) ✓
Equals: Raw materials issued to the factory	= R950 600 ✓

[6]

2. NOTES TO THE PRODUCTION COST STATEMENT

2a

DIRECT LABOUR COST	R
Production wages (723 800✓ + 6 200✓)	730 000 ✓
UIF contribution	7 300 ✓
	<u>737 300 ✓</u>

[5]

2b

FACTORY OVERHEAD COST	R
Salary of foreman	150 000 ✓
Consumable stores: factory (6 000✓ + 43 000✓ – 7 000✓)	42 000 ✓
Depreciation (177 500✓✓ + 12 500✓✓)	190 000 ✓
Water and Electricity (163 000✓ + [4 200✓ × 60%]✓)	100 320 ✓
Sundry expenses: factory	194 680 ✓
	<u>677 000 ✓</u>

[16]

If there are any returns of purchases (creditors allowances), they would be subtracted from **purchases**.



Only use **FACTORY COSTS** on the Production Cost Statement. No administration and selling, and distribution costs appear on this statement.

Production wages for the year + gross wage figure in adjustment B.

As per adjustment B, the UIF contribution is 1% of the R730 000 above.

Opening balance of consumable stores stock + consumable stores purchases – closing balance of consumable stores stock.

$R2\ 225\ 000 - R450\ 000$
 $= R1\ 775\ 000 \times 10\ %$
 $= R177\ 500$
 $R250\ 000 \times 10\ % \times 6/12$
 $= R12\ 500$

(Total water and electricity already paid during the year + the amount that still has to be paid as per adjustment C) × only the portion **used in the factory** (60% as per adjustment C).



There are a number of costs that may need to be split between factory, administration and selling, and distribution.

For example: water and electricity could be split in the ratio 3 : 2 : 1.

3. PRODUCTION COST STATEMENT OF FATIMA MANUFACTURERS FOR THE YEAR ENDED 28 FEBRUARY 2010



It is VERY important to know the format of the Production Cost Statement!

	TOTAL
Direct materials cost✓	950 600✓
Direct labour cost✓	737 300✓
Prime/direct cost	1 687 900✓
Factory overhead cost✓	677 000✓
Total cost of production	2 364 900
Work-in process at the beginning of the year✓	158 000✓
	2 522 900
Work-in process at the end of the year✓	(122 900)✓
Total cost of production of finished goods	2 400 000✓

This figure comes from the answer you calculated in part 1 of this question.

This figure comes from the answer in the direct labour note in part 2 of this question.

Direct materials cost + Direct labour cost = Prime costs

This figure comes from the answer in the factory overhead cost note in part 2 of this question.

This figure comes from opening balances at the beginning of the financial year.

This figure comes from closing balances at the end of the financial year.

This final figure provides the accountant with the total cost of making the 20 000 pairs of shoes during the year (see additional information E).

Direct materials costs (see Production Cost Statement) ÷ number of shoes manufactured as per additional information E.

4. a) Raw materials cost per unit
 $R950\,600 \div 20\,000 \text{ units} = R47,53$ [3]

b) Total cost per unit
 $R2\,400\,000 \div 20\,000 \text{ units} = R120$ [3]

Total cost of production of finished goods (see Production Cost Statement) ÷ number of shoes manufactured as per additional information E.



Do not be afraid to give your own opinion when answering this type of question.

Note that there are various possible answers that could be accepted.

5. a) It tells you how many items you must make and sell before you can start making a profit.✓✓ [2]

b) **Explanation:**

Yes,✓ she should be concerned as units produced are close✓ to BEP; **or** Yes, as the BEP has increased significantly from the previous year; **or** No, she is still exceeding the BEP.

Quoting of figures:

Compare 20 000✓ units produced to BEP✓ of 19 548 or BEP is 97,7% of total units; **or** Compare BEP 19 548 to 11 300 of the previous year; **or** Compare units of 20 000 to 24 000 of the previous year – affects BEP [4]



Learn this! Formula to calculate break-even point (BEP):

$$\frac{\text{Total fixed costs}}{\text{Selling price per unit} - \text{Variable cost per unit}}$$

Practice task 1

1. Production Cost Statement calculations:

Opening balance of raw material stock		
<u>Add:</u> Purchase of raw materials	+	
<u>Add:</u> Carriage on purchases of raw materials	+	
<u>Add:</u> Transport of raw materials	+	
<u>Less:</u> Closing balance of raw material stock	-	
<u>Equals:</u> Raw materials issued to the factory	=	

[6]

2. NOTES TO THE PRODUCTION COST STATEMENT

DIRECT LABOUR COST	R

[5]

FACTORY OVERHEAD COST	R

[16]

Photocopy this blank Production Cost Statement and use it to practise doing the worked example 1 again on your own. Once you have completed the task, compare your answer to the worked example on the previous pages.



Re-do questions 4 and 5 on paper, for added practice.



3. PRODUCTION COST STATEMENT OF FATIMA MANUFACTURERS FOR THE YEAR ENDED 28 FEBRUARY 2010

	TOTAL
Primed/direct cost	
Total cost of production	
Total cost of production of finished goods	

[12]



Below is a list of suggested past examination questions for extra practice:

Topic	Paper	Question
Costing calculations and Production Cost Statement	November 2008	3
Production Cost Statement	November 2009	3
Costing calculations	February/March 2010	4
Multiple choice	November 2010	3.1
Costing calculations and concepts	February/March 2012	2
Production Cost Statement	November 2013	2.1
Break even point	November 2013	2.3



Budgets

Budgeting is an important tool for **internal control** in any business. Budgets are prepared to forecast what will happen in the future.

4.1 Key concepts

Concept	Explanation	Purpose
Cash budget	A forecast of cash receipts and cash payments.	To forecast future receipts and payments.
Projected Income Statement	A forecast of income and expenses.	To forecast future profits or losses.
Debtors' collection schedule	A schedule (plan) of how the business will collect money from its debtors.	To forecast receipts from debtors.
Creditors' payment schedule	A schedule (plan) of how the business will pay its creditors.	To forecast payments to creditors.

Sales

- A business' main source of income is sales. These can be for cash or on credit.
- Cash sales are received immediately and will be entered as a receipt on the cash budget in the month of sale.
- The money from credit sales will be collected from debtors in the future.
- The cash and credit sales may need to be calculated from the given information.



ACTUAL SALES:

These are sales that have taken place in the months before the budget period. A portion of the credit sales may be collected in the budget period.

BUDGETED SALES:

These are the estimated sales for the budget period.



This 3% is written off as a bad debt and will not form part of the debtors' collection schedule as no cash will be received from bad debts.



4.2 Debtors' collection schedule

Use the following steps when preparing a debtors' collection schedule:

1. Calculate and enter the credit sales.
2. Take each month and insert the percentage that will be received in that month.
3. Do the calculations using credit sales to work out the amount to be received from debtors.
4. Total the columns for each month.



Worked example 1

Prepare the debtors' collection schedule for July, August and September 2011 from the information below:

1. 60% of total sales are for cash.
2. Debtors are expected to pay as follows:
 - 50% in the same month as the credit sale transactions subject to a 10% discount
 - 30% in the month following the credit sales transaction month
 - 17% in the second month following the credit sale transaction month
 - 3% is expected to be written off

3. **Total sales:**

- **Actual**
 - June 2011 R160 000
- **Budgeted**
 - July 2011 R150 000
 - August 2011 R180 000
 - September 2011 R200 000

Answer to worked example 1 (see page 64)

Although June is not in the budget period, some of June's credit sales will be collected in July and August.

	Credit sales	July		August		September	
June 2011	R64 000	30%	19 200	17%	10 880		
July 2011	R60 000	50% – 10%	27 000	30%	18 000	17%	10 200
Aug 2011	R72 000			50% – 10%	32 400	30%	21 600
Sep 2011	R80 000					50% – 10%	36 000
			R46 200		R61 280		R67 800

First calculate 50% of the credit sales and then subtract the 10% discount from this figure [50% – 10% is not 40%].

Explanations

Step 1	Step 2	Step 3
Calculate and enter credit sales. Cash sales = 60% Credit sales = 40%	Insert % to be collected in each month.	Do the calculations to work out the amount of credit sales collected in each month.
June: $R160\ 000 \times 40\% = R64\ 000$ July: $R150\ 000 \times 40\% = R60\ 000$ August: $R180\ 000 \times 40\% = R72\ 000$ Sept: $R200\ 000 \times 40\% = R80\ 000$	See answer above.	June credit sales: No calculation as they are not part of this collection period July: $R64\ 000 \times 30\% = R19\ 200$ August: $R64\ 000 \times 17\% = R10\ 880$ July credit sales: July: $R60\ 000 \times 50\% = R30\ 000$ $R30\ 000 - 10\% = R27\ 000$ August: $R60\ 000 \times 30\% = R18\ 000$ Sept: $R60\ 000 \times 17\% = R10\ 200$ August credit sales: August: $R72\ 000 \times 50\% = R36\ 000$ $R36\ 000 - 10\% = R32\ 400$ Sept: $R72\ 000 \times 30\% = R21\ 600$ September credit sales: Sept: $R80\ 000 \times 50\% = R40\ 000$ $R40\ 000 - 10\% = R36\ 000$

4.3 Creditors' payment schedule (creditors' budget)

The following must be considered when the Creditors' budget is calculated:

- when and how much stock is purchased on credit and
- When is the payment due?

This forms part of the second step in the preparation of the main budget.

This info has a twofold understanding:

- That the stock balance at the beginning of the month will be the same, every month, and
- That total purchases are equal to Cost of Sales when purchases are not given.

ILLUSTRATIVE ACTIVITY:

REQUIRED:

Calculate the expected payments to creditors for credit purchases for the budgeted period January to March 2014.



The Opening stock balance will be maintained as the stock basis.

That means that the purchasing on credit during December will be paid at the end of January.

INFORMATION:

- Creditors are paid in full in the month following purchases

ACTUAL CASH purchases of trading stock	November 2013	R10 000
	December 2014	R12 000
BUDGETED CASH purchases of trading stock	January 2014	R10 000
	February 2014	R13 000
	March 2014	R14 500

ACTUAL CREDIT purchases of trading stock	November 2013	R14 000
	December 2013	R12 000
BUDGETED CREDIT purchases of trading stock	January 2014	R10 000
	February 2014	R12 000
	March 2014	R13 000

The following template is the interpretation of the instruction that the Creditors will be paid in full the following month:

1	NOV	14 000	This amount will be paid at the end of December, however this amount is not part of the budget month
2	DEC	12 000	R12 000 will be paid at the end January and forms part of the budget months
3	JAN	10 000	R10 000 will be paid at the end of January and February forms part of the budget months
4	FEB	12 000	R12 000 will be paid at the end of February and March forms part of the budget months
5	MAR	13 000	This amount will be paid at the end of April and does not form part of the budget months

SOLUTION:

CREDITORS PAYMENTS SCHEDULE: Budgeted period: Jan – Mar 2014

MONTH	CREDIT PURCHASES	BUDGETED PERIOD				
		NOV	DEC	JAN	FEB	MAR
① NOV	14 000					
② DEC	12 000			12 000		
③ JAN	10 000				10 000	
④ FEB	12 000					12 000
⑤ MAR	13 000					
Payments to creditors				* 12 000	* 10 000	* 12 000

* Creditors are paid in full in the month following purchases

EXTRACT OF THE CASH BUDGET:

CASH PAYMENTS:

CASH PAYMENTS	JANUARY	FEBRUARY	MARCH
Cash Purchases	10 000	13 000	14 500
Payments to Creditors	12 000	10 000	12 000

Example of creditor's payment schedule:

REQUIRED:

Prepare a Purchases Payment Schedule of KIMA TRADERS for January 2014 to March 2014.

INFORMATION:

SALES FORECAST:

January	R126 000
February	R130 000
March	R144 000

BALANCES AT 31 DECEMBER 2013

Trading Stock	R75 000
Creditors	R60 000



Whenever the credit purchases are not given, calculate the cost of sales from the given total sales (R6000)

E.g. Cost of Sales = 50 % on cost

Calculation:

Sales \times 100/150 =

Cost of sales (Purchases)

6000 \times 100/150 =

ADDITIONAL INFORMATION:

1. Mark-up is equal to 100% on Cost price
2. Cash purchases of trading stock amount to only 20% of all purchases
3. All credit purchases are payable in the month following the month of Purchase.
4. Stock replenishment will take place on a monthly basis and the opening balance will be maintained as a base stock.

PROCEDURE TO FOLLOW:

1. Determine the budget months:
Answer: January to March 2014.
2. Does the question give you the purchases of stock?
Answer: No, therefore Cost of sales is equal to purchases of stock.

EXPLANATIONS:

You need to make use of the Sales figures to calculate the cost of sales per month



<p>1 Mark-up is equal to 100% on Cost price. Formula: Cost price: 100% + Profit: 100% =Sales: 200%</p>	<p>The purchases of stock is not given therefore you have to calculate the cost of sales amount to determine the purchases of stock:</p>
	<p>January: Creditors' balance will be paid in January: R60 000. (the balance was the credit purchases during December)</p>
	<p>February: Make use of the sales figure of <u>January</u> to calculate the cost of sales that is equal to purchases: $126\ 000 \times 100/200 = R63\ 000$ (Cost of sales)</p>
	<p>March: Make use of the sales figure of <u>February</u> to calculate the cost of sales: $130\ 000 \times 100/200 = R\ 65\ 000$ (Cost of sales)</p>
<p>2 Cash purchases of trading stock amount to only 20 % of all purchases. Therefore credit purchase is 80% of all purchases</p>	<p>January: $63\ 000 \times 20\% = R12\ 600$ cash purchases in January $(63\ 000 \times 80\% = R50\ 400$ payment of account in February)</p>
	<p>February: $65\ 000 \times 20\% = R13\ 000$ cash purchases for February $65\ 000 \times 80\% = R52\ 000$ payment of account in March</p>
	<p>March: $72\ 000 \times 20\% = R14\ 000$ cash purchases for March</p>
<p>3 All credit purchases are payable in the month following the month of Purchase.</p>	<p>This means that the creditors will be paid the next month. Anything bought during January will be paid at the end of February.</p>
<p>4 Stock replenishment will take place on a monthly basis and the opening balance will be maintained as a base stock.</p>	<p>This means that the opening stock will stay the same every month. See the illustration below</p>

ILLUSTRATION: CALCULATION OF THE PURCHASES AMOUNT OF STOCK.

“STOCK REPLENISHMENT WILL TAKE PLACE ON A MONTHLY BASIS AND THE OPENING BALANCE WILL BE MAINTAINED AS A BASE STOCK.”

Here is an illustration what it means:

- If the opening balance is the same at every given month, then the Cost of sales will automatically be equal to the total purchases.
- So, when the stock purchased is not given, calculate cost of sales.
- Cost of Sales is equal to total purchases.
- Find the ratio between credit (eg. 80%) and cash purchases (eg. 20%) and calculate
- Complete the Creditors Payment schedule

GENERAL LEDGER OF KIMA TRADERS

DR		TRADING STOCK ACCOUNT				N		CR
Jan	1	Balance	B/d	75 000	Jan	31	(126 000 × 100/200) Cost of sales	63 000
		Bank (63 000 × 20%)		12 600			Balance	C/d 75 000
		63 000 × 80% Creditors control		50 400				
				138 000				138 000
Feb	1	Balance	B/d	75 000	Feb	28	(130 000 × 100/200) Cost of sales	65 000
		Bank (65 000 × 20%)		13 000			Balance	C/d 75 000
		Creditors control (80%)		52 000				
Mar	1	Balance	B/d	75 000	Mar	31	(144 000 × 100/200) Cost of sales	72 000
		Bank (72 000 × 20%)		14 400			Balance	C/d 75 000
		Creditors control (80%)		57 600				
Apr	1	Balance	B/d	75 000				

SOLUTION:**CREDITORS PAYMENTS SCHEDULE: Budgeted period: January to March 2014**

MONTH	PURCHASES	CREDIT PURCHASES	BUDGETED PERIOD				
			NOV	DEC	JAN	FEB	MARCH
Balance of creditors					60 000		
JAN	63 000	50 400				50 400	
FEB	65 000	52 000					52 000
MAR	72 000	57 600					
Payments to creditors					60 000	50 400	52 000

EXTRACT OF THE CASH BUDGET:**CASH PAYMENTS:**

CASH PAYMENTS	JANUARY	FEBRUARY	MARCH
Cash Purchases	12 600	13 000	14 400
Payments to Creditors	60 000	50 400	52 000

4.4 Analysis of cash budget

Depreciation and bad debts will be included in the projected income statement but NOT on the cash budget because they are non-cash items (i.e. they do not affect the cash flow of the business).



e.g. Worked example 2

Example adapted from March 2010 NSC question paper – see FEB/MARCH 2010 Paper 1 at:

<http://www.education.gov.za/Examinations/PastExamPapers/AccountingPapers2010/tabid/507/Default.aspx>

You are provided with the Projected Income Statement and additional information relating to Helen's Hair Stylists for the period April to June 2010. The business is owned by Helen Davids. Helen has also prepared a cash budget for the same time period. The financial year-end is 31 March.

Required

Answer the questions that follow.

Information

Helen's hair stylists

Projected Income Statement for April to June 2010

	APRIL	MAY	JUNE
	R	R	R
Sales of hair products	87 500	105 000	122 500
Cost of sales	50 000	60 000	70 000
Gross profit	37 500	45 000	52 500
Other operating income	122 000	122 000	162 000
Fee income from customers	120 000	120 000	160 000
Sundry income	2 000	2 000	2 000
OPERATING EXPENSES	95 350	120 072	127 372
Salary of hairdressing assistants	25 500	25 500	34 000
Wages of cleaner	3 400	3 672	3 672
Rent of premises	24 600	30 750	30 750
Consumable stores	14 400	14 400	19 200
Water & electricity	6 000	6 000	7 000
Telephone	2 200	2 200	2 200
Advertising	8 000	15 000	8 000
Motor vehicle expenses	1 400	5 600	5 600
Repairs & maintenance of equipment	3 500	3 500	3 500
Sundry expenses	2 300	2 300	2 300
Depreciation on vehicle	2 000	9 100	9 100
Depreciation on equipment	2 050	2 050	2 050
OPERATING PROFIT	64 150	46 928	87 128
Interest income	3 315	0	0
	67 465	46 928	87 128
Interest on loan	750	625	500
NET PROFIT	66 715	46 303	86 628

Additional information**1. Line of business:**

Helen gave up her job to start this business in 2004. She invested her life savings of R800 000 in this business. The business styles hair for its customers. They also sell hair products to the public.

2. Employees:

Helen employs three hair stylists. She has planned to expand the business by employing a fourth stylist from 1 June 2010. She also employs a cleaner.

3. Business premises rented:

The rent is calculated on a fixed amount per square metre. She currently rents 60 square metres, but will increase this floor space as from 1 May 2010 due to expansion.

4. Fixed deposit:

The fixed deposit of R468 000 is for 12 months and will mature on the 30 April 2010.

Questions

Refer to the Projected Income Statement to identify/calculate the following:

- The monthly salary paid to each hair stylist. (2)
- The % increase in wages that the cleaner will receive during the projected period. (2)
- The % interest rate on the fixed deposit. (4)
- The rental per square metre, and the number of additional square metres she will rent from 1 May 2010. (4)
- As the internal auditor you compare the following projected figures to the actual figures at the end of April. Provide four comments that you would include in your internal auditor's report in respect of scenarios A, B and C below.

		Projected April 2010	Actual April 2010
A	Telephone	2 200	4 150
B	Water & electricity	6 000	4 900
C	Fee income	120 000	136 800
	Consumable stores	14 400	15 120

Answers to worked example 2 (see page 78)

- Calculation of monthly salary paid to each hair stylist: [2]

$$R25\,500 \div 3 = R8\,500 \checkmark \checkmark$$

$$\text{or } R34\,000 \div 4 = R8\,500$$

Explanation to help you understand how to get to the answer above:

- There are 3 hairstylists in April and May and 4 hairstylists in June.
- Therefore divide salary (April or May) by 3 hairstylists ($R25\,500 \div 3 = R8\,500$)
- OR Divide salary (June) by 4 hairstylists ($R34\,000 \div 4 = R8\,500$)

2. Calculation of the % increase in wages that the cleaner will receive during the projected period: [2]

$$272 \div 3\,400 \times 100 = 8\% \checkmark \checkmark$$

Explanation to help you understand how to get to the answer above:

- Calculate the increase in wages by deducting the wage of May from wage of April (R3 672 – R3 400 = R272)
- Calculate the % increase (R272 ÷ R3 400 × 100 = 8%)

3. Calculation of % interest rate on the fixed deposit: [4]

$$3\,315 \checkmark \div 468\,000 \checkmark \times 12 \text{ months} \checkmark \times 100 = 8,5\% \checkmark$$

OR

$$3\,315 \times 12 \text{ months} = R39\,780$$

$$\frac{39\,780}{468\,000} \times 100 = 8,5\%$$

Explanation to help you understand how to get to the answer above:

Interest on fixed deposit = R3 315 (interest income in Projected Income Statement)

Fixed deposit = R468 000 (see information no. 4)

$$\frac{3\,315}{468\,000} \times \frac{100}{1} \times 12 \text{ (months)}$$

$$= 8,5\%$$

4. Calculation of rental per square metre: [2]

$$24\,600 \div 60 = R410 \checkmark \checkmark$$

Explanation to help you understand how to get to the answer above:

Rent expense for April = R24 600 (see Projected Income Statement)

R24 600 is the amount paid for 60 square metres.

To calculate rental per square metre you have to divide the total rent by 60

$$R24\,600 \div 60 = R410$$

- Calculation of the number of additional square metres she will rent from 1 May 2010: [2]

$$30\,750 \div 410 = 75 \text{ sq metres or } 60 \times 30\,750 \div 24\,600 = 75 \text{ sq metres}$$

$$\text{Increase} = 75 - 60 = 15 \text{ sq metres} \checkmark \checkmark$$

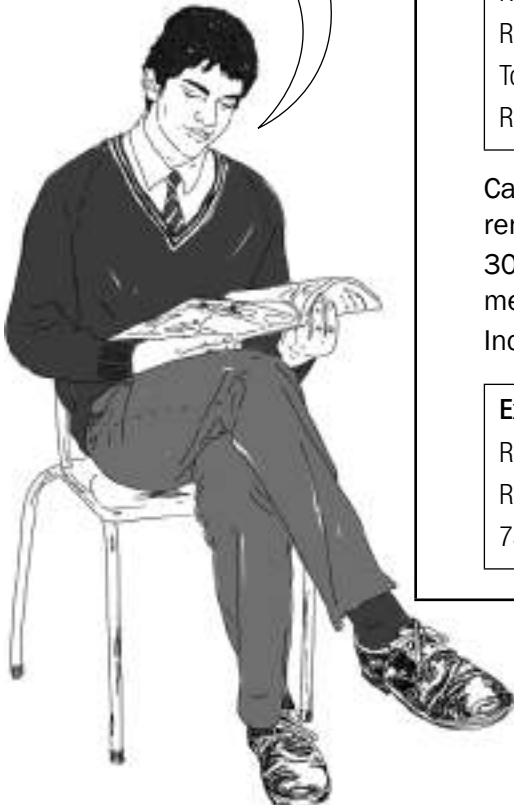
Explanation to help you understand how to get to the answer above:

Rent expense for May = R30 750 (see Projected Income Statement)

$$R30\,750 \div R410 = 75 \text{ square metres}$$

$$75 - 60 \text{ (original square metres)} = 15 \text{ additional square metres}$$

For internal control purposes it is important to compare actual with budgeted figures. In this way possible problems relating to expenses or income can be corrected.



5. Provide four comments that you would include in your internal auditor's report in respect of scenarios A, B and C above. [8]

A	Comment on telephone: The telephone costs are higher than the expected amount by R1 950. ✓✓
B	Comment on water & electricity: The water & electricity costs are R1 100 less than the expected amount. ✓✓
C	Comment on fee income & consumable stores: There was a good increase ✓ in fee income of R16 800 ✓ (R136 800 – R120 000) which shows that the business is popular with its customers. The consumable stores (e.g. shampoos, conditioners) increased slightly by R720 (R15 120 – R14 400) because the business had more customers. ✓✓

Re-do questions 1–5 on paper, for extra practice.



When commenting on actual figures use the following steps:

1. Compare actual with budgeted figures and state whether the actual figure is more or less than the budgeted figure.
2. Decide and state whether the expense or income item has been well controlled or not (within budget or not).



You will get a mark for steps 1 and 2. These are easy marks.



Below is a list of suggested past examination questions for extra practice:

Topic	Paper	Question
Projected Income Statement	February/March 2009	3
Projected Income Statement	February/March 2010	6
Cash Budget	February/March 2011	1
Cash Budget	February/March 2012	5
Cash Budget	November 2013	5.2



Keep going!

5

Chapter

Reconciliations

Reconciliation is a form of internal control where two sets of information are compared and, when there are differences, these are corrected or explained.

Bank reconciliation	Debtors' reconciliation	Creditors' reconciliation
The balance in the bank account in the business' general ledger should be the same as the balance on the bank statement received from the bank. When these are not the same, they need to be reconciled.	The balance of the debtors' control account should be the same as the total of the debtors list. When these are not the same, they need to be reconciled.	The balance of the creditors' control account should be the same as the total of the creditors' list. The statements received from the creditors must match each creditors balance in the business' books. When these are not the same, they need to be reconciled.

Use mobile notes to help you learn these reconciliation concepts. See page ix for more information.



5.1 Bank reconciliation

A summary of all possible DIFFERENCES between the CRJ/CPJ and the Bank Statement. Make sure that you know how to record all the different transactions before attempting to answer the Grade 12 CAPS Reconciliation questions.						
1. Bank Charges and interest charged on the Bank Statement– The ABSA Bank charged the following: Tax levy R10 Service fees R20 Cash deposit fee R30 Interest R40	CPJ – May 2014					
	BS	ABSA Bank (10 + 20 + 30)	60	60	Bank charges	
	BS	ABSA Bank	40	40	Interest on overdraft	
2. Interest earned/received on the Bank Statement The bank statement showed interest received on current account, R50	CRJ – May 2014					
	BS	ABSA Bank	50	50	Interest on current account	
3. Direct deposit on the Bank Statement E.g. A tenant, E Baloyi, paid his rent directly into the bank account, R800.	CRJ – May 2014					
	BS	E Baloyi	800	800	Rent Income	
4. Stop orders/Debit orders on the Bank Statement The bank statement showed a stop order, R367, in favour of Santam for a payment on an insurance premium.	CPJ – May 2014					
	BS	Santam	367	367	Insurance	
5. Cheques issued in CPJ but not presented for payment The following cheques do not appear on the bank statement no. 67, R200 and no. 69, R300.	Bank Reconciliation statement – May 2014					
					Debit	Credit
	Debit outstanding cheques:					
67				200		
69				300		
6. Deposits in CRJ but do not appear on Bank Statement The deposit made on the last day of month does not appear on the bank statement, R9000	Bank Reconciliation statement – May 2014					
					Debit	Credit
	Credit late deposit					9 000
7. CHEQUES DISHONoured – insufficient funds Unpaid cheque, R170 – this cheque was received from P Pillay in settlement of his account of R183 and deposited on 24 May 2002. It was dishonoured because of insufficient funds	CPJ – May 2014					
	DS	P Pillay (RD cheque)	170	170	Debtors control	

<p>8. POST-DATED CHEQUES: received and deposited</p> <p>Unpaid cheque, R157 – this cheque was received from a tenant, B Bud and deposited inadvertently on 21 May 2014 It was dishonoured because it was dated 21 July 2014</p>	CPJ – May 2014 – May 2014				
	BS	B Bud (RD cheque)	157	157	Rent Income
<p>9. POST-DATED CHEQUES: Issued</p> <p>Entry in the CPJ which did not appear on the Bank Statement:</p> <p>The business issued a post-dated cheque no. 303 to a Factory to secure the popular stock to be delivered, R6 000, dated 25 July.</p>	Bank Reconciliation statement – May 2014				
	Debit outstanding cheques: 303 (25 July 2014)			Debit 6 000	Credit
<p>10. STALE CHEQUE: Cheque issued, (cheque is older than 6 months)</p> <p>Entry on Bank Reconciliation statement on 30 April 2014 which did not appear on the Bank Statement: May 2014</p> <p>Cheque no 120 was issued to Shezi Stat on 20 November 2013 for Stationery, R100.</p>	CRJ – May 2014				
	120	Shezi Stat (Cancel stale cheque)	100	100	Stationery
<p>11. STALE CHEQUE: Received and dishonoured</p> <p>Entry on Bank Statement which did not appear in CRJ or CPJ:</p> <p>Unpaid cheque, R160 – this cheque was received from a debtor, J. Nel and deposited inadvertently on 25 May 2014. It was dishonoured because it was dated 25 May 2013</p>	CPJ – May 2014				
	DS	J Nel (RD cheque)	160	160	Debtors control
<p>12. LOST CHEQUE: issued (Only issue new cheque if instructed to do so →)</p> <p>a. cancel lost cheque in CRJ b. issue new cheque in CPJ c. record new cheque as “debit outstanding cheque” in the Bank Reconciliation Statement</p> <p>Cheque no. 255, R500 was lost by PNA and they asked for a new cheque. Cheque no 255 to be cancelled and replaced by cheque 365. The cheque was a payment for Printing made</p>	CRJ – May 2014 (a) cancel lost cheque				
	255	PNA (Cancel lost cheque)	500	500	Printing
	CPJ – May 2014 (b) Issue a new cheque				
	365	PNA	500	500	Printing
	Bank Reconciliation Statement – May 2014 (c) Record the new cheque as outstanding				
Debit outstanding cheques			Debit 500	Credit	

ERRORS MADE BY BUSINESS IN THE CRJ AND CPJ	CPJ – May 2014				
13. ERRORS IN CRJ/ or CPJ : Amount less than it should be → Cheque no 253 on Bank Statement showed and amount of R664, while the amount in the CPJ was R646. It was a payment to Makro for goods.	453	Makro (understated, 654-545)	18	18	Trading stock
14. ERRORS IN CRJ/ or CPJ :	CRJ – May 2014				
Amount more than it should be → Cheque no 244 on Bank Statement showed and amount of R250, while the amount in the CPJ was R258. It was a payment to Investec for rent.	244	Investec (overstated, 258 - 250)	8	8	Rent Expense
ERRORS MADE BY BANK ON BANK STATEMENT	Bank reconciliation statement – May 2014				
15. Cheque drawn by other client and erroneously debited to our bank account. Cheque no.2 230, R1500, on the Bank Statement was a cheque drawn by another client, ZITHA Stores, debited to our account.	Credit cheque no. 2230 wrongly debited			Dr.	Cr.
					1500
16. Deposit wrongly credited to our bank account	Bank reconciliation statement – May 2014				
The deposit on the 15 May 2014, R2000, showed on the Bank Statement was a deposit made by the owner into his own bank account and the Bank has erroneously recorded the deposit in his business' Bank account	Debit deposit wrongly credited			Dr.	Cr.
				2 000	

Format of the Bank Reconciliation statement			
C	BANK RECONCILIATION STATEMENT ON 31 March 2012		
		DEBIT	CREDIT
	Credit balance as per Bank Statement		8 000
	Credit deposit not credited by bank		3 000
	Debit outstanding cheques:		
	124	4 000	
	170	1 000	
	Debit deposit wrongly credited (errors made by Bank)	1 500	
	Credit cheque wrongly debited		500
	Debit balance as per Bank account		5 000
	11 500	11 500	

Always start with the balance of the Bank Statement and end with the calculated balance of the Bank account

The debit and credit totals of the Bank Reconciliation statement must be equal e.g. R11 500

5.2 Debtors' reconciliation

These are the steps the bookkeeper will need to follow to correct differences between the debtors' control account and debtors' list:

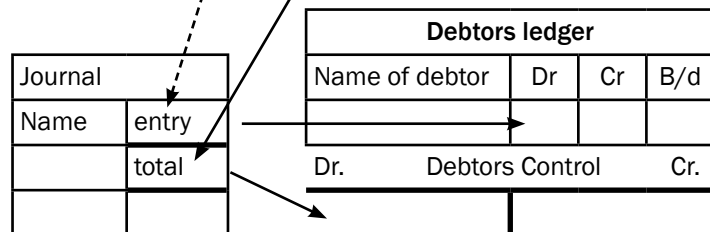
- a) Check entries in the journals against the source documents.
- b) Check casting (totalling) of journals.
- c) Check posting from journals to general and debtors ledgers.

A. Procedure to follow when the balance of the debtors control account and the debtor's account do not correlate.

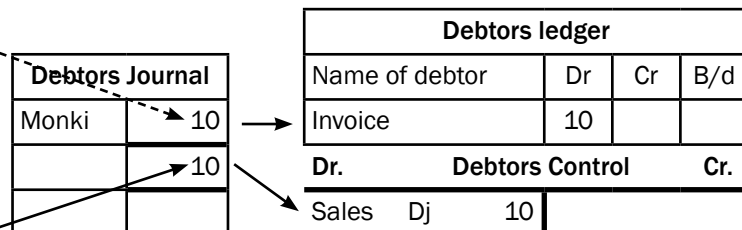
1. The **ENTRY** in the journal will be posted on a **daily basis** to the **debtors ledger** and the **TOTAL** at the bottom of the journal will be **posted at the end of the month** to the **control account**
2. When the balance in the Debtors control account does not correlate with the total of the Debtors list, you need to establish where the error is. Is the error in the control account or in the list of debtors?
3. Is the error in the original ENTRY or is it in the TOTAL of the Journal? If the ENTRY is incorrect the TOTAL will also be wrong, so the control account and the list must be corrected.
4. Study the following examples.

The following rules will assist you when you compare the Debtors Control account with the list of Debtors. The list of debtors is made up by the balances of the debtors from the Debtors Ledger.

4.1 Example: The ENTRY is posted daily to the Debtors ledger (Debtor's list) and the TOTAL is posted to the control account at the end of the month.



4.2 Example: Sold goods to Monki for R10 and issued an invoice.



The ENTRY goes to the debtors ledger or/to the List of Debtors

The TOTAL of the Debtors Journal is posted to the Control account at the end of the month.

5. The following are some of the types of errors and omissions that could arise:

- Errors on source documents
- Recording errors in Subsidiary Journals
- Incorrect posting from the Journals to the General ledger and Debtors- or Creditors ledger.
- Incorrect additions in the lists of debtors and creditors.
- Incorrect addition of Journal totals – too much (overcast) – too little (undercast)

Basic rule:

Debtors Journal		Debtors Ledger (Debtors List)			
	Entry		Dr	Cr	Balance
	50	Invoice	Entry		
	60		50		
	Total	GENERAL LEDGER:			
	110	Dr.	Debtors Control (A)		Cr.
		total			
		Sales	110		

BASIC RULES:

- The individual entry goes to the debtor's account in the Debtors Ledger.
- The Total of the journal will be posted to the Debtors Control account.
 - The ENTRY goes to the Debtors Ledger on a daily basis.
 - The TOTAL is posted to the Debtors Control account at the end of the month.
- When reading the transaction, you need to establish where the error occurred.
 - If the **error is the ENTRY**, then the TOTAL will automatically be incorrect as well. Then the Debtors list and the Debtors Control must be corrected. E.g. The entry in the DJ was incorrectly recorded as R56 instead of R50.

Debtors Journal		Debtors Ledger (Debtors List)			
	Entry		Dr	Cr	Balance
	56 X	Invoice	Entry		
	60		56 X	- 6	
	Total	GENERAL LEDGER:			
	116 X	Dr.	Debtors Control (A)		Cr.
		total			
		Sales	116 X		
			(116 - 6)		

- If the TOTAL was incorrectly added, then there is no error in the ENTRY and the error will be only corrected in the Debtors control account. E.g. The total of the DJ was incorrectly totaled as R100 instead of R110.

Debtors Journal		Debtors Ledger (Debtors List)			
	Entry		Dr	Cr	Balance
	50	Invoice	Entry		
	60		50		
	Total	GENERAL LEDGER:			
	100 X	Dr.	Debtors Control (A)		Cr.
		total			
		Sales	100 X		
			(100 + 10)		

- If the ENTRY is correct then the TOTAL will also be correct. So you need to establish where the error is. The **error will be in the posting** to the ledgers.
- If the ENTRY was not posted to the Debtor ledger, then the ENTRY will be recorded.
E.g. The amount of R50 in the DJ was not posted to the debtor's account.

Debtors Journal	
	Entry
	50
	60
Total	
	110

Debtors Ledger (Debtors List)			
	Dr	Cr	Balance
Entry	- X		
50			
Dr.	Debtors Control (A)		Cr.

Sales total

110	110
-----	-----

- If the ENTRY was recorded but the amount was wrongly recorded. UNDER CAST:
E.g. The amount of R50 in the DJ was posted to the debtor's account as R30.
(therefore the account was undercasted by $R50 + R30 = R20$)

Debtors Journal	
	Entry
	50
	60
Total	
	110

Debtors Ledger (Debtors List)			
	Dr	Cr	Balance
Entry	30 X		
+ 20			
Dr.	Debtors Control (A)		Cr.

Sales total

110	110
-----	-----

- If the ENTRY was recorded but the amount was wrongly recorded. OVER CAST:
E.g. The amount was R50 in the DJ was posted to the debtor's account as R59.
(therefore the account was over casted by $R59 - R50 = R9$)

Debtors Journal	
	Entry
	50
	60
Total	
	110

Debtors Ledger (Debtors List)			
	Dr	Cr	Balance
Entry	59 X	- 9	
Dr.	Debtors Control (A)		Cr.

Sales total

110	110
-----	-----

- If the ENTRY was posted but to the wrong side of the account. The ENTRY was recorded on the credit side instead of the debit side therefore the ENTRY will be recorded on the debit side twice - cancel the wrong entry on the credit side and once more to have the entry on the correct side.

E.g.: The amount of R50 in the DJ was posted to the debtor's account in the Debtors Ledger however the ENTRY was recorded on the credit side of the account (or the wording can read; the R50 was recorded on the credit side.)

Debtors Journal		Debtors Ledger (Debtors List)			
	Entry	Dr	Cr	Balance	
	50	50 +	50 X		
	60	50			
	Total	Dr. Debtors Control (A)		Cr.	
	110	Sales total		110	

e.g. Worked example 1

Example adapted from March 2012 NSC question paper.

Crystal Traders sells glassware for cash and on credit.

Required

Study the information provided and answer the questions that follow.

- Calculate the correct closing balance of the debtors' control account on 31 March 2011. [5]
- Calculate the correct amounts owing by the following debtors of Crystal Traders:
 - R Jansen
 - S Wonder
 - P Collins
 [12]

Information

- Balance of debtors' control account on 31 March 2011 is R200 000
- Balances per Debtors' Ledger on 31 March 2011:

M Carey	R64 500
R Jansen	R41 200
S Wonder	R23 000
C Dion	R51 500
P Collins	R7 900
TOTAL	R188 100

- The following errors and omissions were discovered and must be corrected:
 - The debtors' journal has been **overcast** by R2 600.
 - An invoice issued to S Wonder for R1 800 had not yet been recorded in the books of Crystal Traders.
 - Stock sold on credit to P Collins was incorrectly charged to the account of R Jansen, R8 300.
 - An invoice issued to P Collins for R6 000 had been posted to the wrong side of his account.
 - A cheque of R13 500, originally received from R Jansen in settlement of an invoice of R15 000, was returned by the bank due to insufficient funds. No entries have yet been made.

Can you see that the Debtors' control account and the Debtors' Ledger are not the same?

Overcast means that the journal has been added up incorrectly and the amount is too big.
Undercast means that the journal has been added up incorrectly and the amount is too small.

F. Goods sold on credit to S Wonder for R5 800 were correctly recorded in the debtors' journal but incorrectly posted as R8 500 to S Wonder's account in the Debtors' Ledger.

Answers to worked example 1 (see page 89)

1. Calculate the correct closing balance of the debtors' control account on 31 March 2011.

$$200\,000 \checkmark - 2\,600 \checkmark (A) + 1\,800 \checkmark (B) + 15\,000 \checkmark (E) \\ = 214\,200 \checkmark$$

[5]

2. Calculate the correct amounts owing by the following debtors of Crystal Traders:

	Workings	Answer
R Jansen	R41 200 + 15 000 ✓✓ (E) - 8 300 ✓ (C) =	R47 900 ✓
S Wonder	R23 000 + R1 800 ✓ (B) - 2 700 ✓✓ (F) =	R22 100 ✓
P Collins	R7 900 + 12 000 ✓✓ (D) + 8 300 ✓ (C) =	R28 200 ✓

[12]

- 3.

	ERROR	EXPLANATION
A	The debtors' journal has been overcast by R2 600.	The debtors' control balance is R2 600 too much. This must be deducted from the debtors' control balance.
B	An invoice issued to S Wonder for R1 800 had not yet been recorded in the books of Crystal Traders.	This was not recorded so it needs to be entered in the debtors' control account and in the account of S Wonder on the debtors' list. Debtors' control (+R1 800) S Wonder (+R1 800)
C	Stock sold on credit to P Collins was incorrectly charged to the account of R Jansen, R8 300.	This must be removed from R Jansen and added to P Collins on the debtors' list. R Jansen (-R8 300) P Collins (+R8 300)
D	An invoice issued to P Collins for R6 000 had been posted to the wrong side of his account.	Correct it on P Collins' account in the debtors' list. It should have been entered on the debit side but was entered on the credit side. Cancel the credit of R6 000 by debiting (+R6 000) Record the correct entry on debit side (+R6 000)
E	A cheque of R13 500, originally received from R Jansen in settlement of an invoice of R15 000, was returned by the bank due to insufficient funds. No entries have yet been made.	No entries were made. This needs to be recorded in the debtors' control account and in the account of R Jansen in the debtors' list. Debtors' control (+R13 500) → bank amount Debtors' control (+R1 500) → discount cancelled R Jansen (+R15 000)
F	Goods sold on credit to S Wonder for R5 800 were correctly recorded in the debtors' journal but incorrectly posted as R8 500 to S Wonder's account in the Debtors' Ledger.	Debtors' control account is correct. S Wonder's account is incorrect and must be corrected. It was entered in the Debtors' Ledger as R8 500 instead of R5 800. Too much was posted to the debit side of S Wonder's account in the Debtors' Ledger. The difference of R2 700 must be credited (subtracted) from S Wonder's account.

5.3 Debtors' age analysis

Introduction

Any business must keep a careful control of all the accounts in the Debtors Ledger. The debtor's credit controller has the responsibility to monitor a debtor's credit rating before extending any credit to the debtor. The debtor's clerk's responsibility includes that no debtors exceed their credit limit and that payments are regularly received according to their agreement with them.

Before any order can be despatched to a debtor, the debtor's clerk must first approve of the credit sale. The debtor's clerk must verify the balance of the debtor's account and the agreed credit limit allowed for that debtor.

Debtor's Age analysis is used where the debtor's ledger account is broken down into time periods so that it is clear how long an amount has been outstanding.

When calculating age analysis there are TWO RULES to apply:

- **Returns are subtracted from the latest sale.**
- **Payments are subtracted from the oldest outstanding balance.**

A credit note is subtracted from the most recent invoice issued because goods usually can be returned within a certain number of days, e.g. 7 days.

A receipt will be issued for the payment and for discount allowed. This amount will be subtracted from the oldest amount owed by the debtor.

Reasons for debtors age analysis

- To ensure that Debtors honour the agreement of e.g. 30 days.
- To charge interest on overdue balances according to the agreement.
- To take legal action if the account is not settled within a certain period, e.g. more than 90 days.
- To minimise debts to be written off.
- To ensure liquidity in the business and a proper cash flow.
- To be aware of debtors who honour their credit agreement and those who do not.
- To follow up on those debtors who signed a payment plan due to previous late payments.
- To follow up on possible errors that could be on a debtor's statement where the debtor paid the correct amount without letting the business know of the statement error.

Example of a debtor's statement and age analysis

Study the following statement to understand the calculation of age analysis. A possible format was used for the breaking down of Moja and Sons account into time periods, February to May. Take into account the TWO RULES.

- **Returns are subtracted from the most recent invoice**
- **Payments are subtracted from the oldest outstanding balance**

(TAX NO: 456123)					
KIMA WHOLESALERS 45 Dove street, Pretoria 1000					
NO. 77					
STATEMENT OF ACCOUNT					
TO: Moja and Sons Mahlangu Street Timbato			DATE: 31 May 2014		
TERMS: CREDIT PERIOD: 30 days			CREDIT LIMIT: R5 000		
<ul style="list-style-type: none"> • 10% discount on settlement of account within 14 days of purchase • Interest at 5% per month will be charged on amounts owing for 60 days or more 					
Date	Description	Debit	Credit	Balance	
01-03-2014	Balance brought forward			800	
07-03-2014	Invoice 102	2 500		3 300	
28-03-2014	Receipt no 533		500	2 800	
03-04-2014	Invoice 125	2 400		5 200	
08-04-2014	Credit note C66		600	4 600	
29-04-2014	Receipt 575		400	4 200	
01-05-2014	Invoice 130	1 200		5 400	
09-05-2014	Invoice 131	700		6 100	
30-05-2014	Receipt 621		1500	4 600	
	Receipt 621 (discount)		150	4 450	
Age Analysis:	Current	30 Days	60 Days	90 Days	120 Days
	1 900	1 800	800	0	0



Remember the rule:
Subtract payments from the longest outstanding balance.

Current month means the month of the statement

The Table below was used to calculate the age analysis

Steps to follow to see how the Age analysis was calculated:

Draw a template with months																																																			
Record the invoices according to the month that you have received the stock																																																			
The payment of R500 (March) must pay off the balance of R800. (800 – 500 = 300 still outstanding) So R300 will come off from the next payment.																																																			
The R400 (April) receipt must 1st pay off the R300 in Feb (400-300 = R100) The R100 paid some of the debt of March																																																			
The R1500 and discount R150 (May), paid off some of the debt of March																																																			
	<table border="1" style="width: 100%; border-collapse: collapse; text-align: center;"> <thead> <tr> <th style="width: 25%;">Transactions:</th> <th style="width: 12.5%;">May</th> <th style="width: 12.5%;">April</th> <th style="width: 12.5%;">March</th> <th style="width: 12.5%;">February</th> </tr> </thead> <tbody> <tr> <td>Balance</td> <td></td> <td></td> <td></td> <td style="text-align: right;">800</td> </tr> <tr> <td>Invoices</td> <td style="text-align: right;">1 200 + 700</td> <td style="text-align: right;">2 400</td> <td style="text-align: right;">2 500</td> <td></td> </tr> <tr> <td>Returns</td> <td></td> <td style="text-align: right;">(600)</td> <td></td> <td></td> </tr> <tr> <td><i>Total purchases per month</i></td> <td style="text-align: right;">1 900</td> <td style="text-align: right;">1 800</td> <td style="text-align: right;">2 500</td> <td style="text-align: right;">800</td> </tr> <tr> <td><i>Receipts and discounts</i></td> <td></td> <td></td> <td></td> <td></td> </tr> <tr> <td>Mar: payment by debtor R500</td> <td style="text-align: right;">-</td> <td style="text-align: right;">-</td> <td style="text-align: right;">-</td> <td style="text-align: right;">(R500)</td> </tr> <tr> <td>Apr: payment by debtor R400</td> <td style="text-align: right;">-</td> <td></td> <td style="text-align: right;">(100)</td> <td style="text-align: right;">(300)</td> </tr> <tr> <td>May: R1 500 + 150</td> <td style="text-align: right;">-</td> <td style="text-align: right;">-</td> <td style="text-align: right;">(1 650)</td> <td style="text-align: right;">-</td> </tr> <tr> <td>Balance</td> <td style="text-align: right;">1 900</td> <td style="text-align: right;">1 800</td> <td style="text-align: right;">750</td> <td style="text-align: right;">0</td> </tr> </tbody> </table>	Transactions:	May	April	March	February	Balance				800	Invoices	1 200 + 700	2 400	2 500		Returns		(600)			<i>Total purchases per month</i>	1 900	1 800	2 500	800	<i>Receipts and discounts</i>					Mar: payment by debtor R500	-	-	-	(R500)	Apr: payment by debtor R400	-		(100)	(300)	May: R1 500 + 150	-	-	(1 650)	-	Balance	1 900	1 800	750	0
Transactions:	May	April	March	February																																															
Balance				800																																															
Invoices	1 200 + 700	2 400	2 500																																																
Returns		(600)																																																	
<i>Total purchases per month</i>	1 900	1 800	2 500	800																																															
<i>Receipts and discounts</i>																																																			
Mar: payment by debtor R500	-	-	-	(R500)																																															
Apr: payment by debtor R400	-		(100)	(300)																																															
May: R1 500 + 150	-	-	(1 650)	-																																															
Balance	1 900	1 800	750	0																																															

Check your answer: 1 900 + 1 800 + 750 = R4 450

Take note: The total of the analysis must be equal to the total balance on the statement and debtor's ledger account.



Worked example 2: Debtors' age analysis

Study the debtors' age analysis below and answer the questions that follow:

	Total	Current	30-60 days	61-90 days	More than 90 days
B Barney	R5 900	R1 800	R2 400	R1 200	R500
D Donald	R4 600	R1 400	R3 200		
Z Ndlovu	R3 000	R3 000			
Total	R13 500	R6 200	R5 600	R1 200	R500

This is the balance of the debtors' control account in the general ledger.

Credit terms

- Debtors are given 60 days from statement date (end of the month) in which to settle their debts.
- Debtors settling within 60 days will be granted a discount of 10%.
- Debtors older than 60 days are charged interest of 12.5% p.a.

Required

1. Which debtor(s) are not adhering to (meeting) the credit terms?
Why? (2)
2. If Z Ndlovu settled her account after receiving her statement, and within the credit terms, how much would she be required to pay? (4)
3. If these were the only 3 debtors, what would the balance on the debtors' control account be? (2)
4. Is this business controlling their debtors effectively?
Explain, quoting figures. (4)

[12]

Re-do questions 1 – 4 on paper, for extra practice.



It is important for you to answer "yes" or "no" BUT it is your explanation that will get you the marks.



Answers to worked example 2 (see page 93)

1. Which debtor(s) is/are not adhering to (meeting) the credit terms? Why?
B. Barney ✓
He owes amounts for longer than the credit terms of 60 days. ✓ [2]
2. If Z Ndlovu settled her account after receiving her statement, and within the credit terms, how much would she be required to pay?
 $R3\ 000 ✓ - 10\% (R300) ✓✓ = R2\ 700 ✓$ [4]
3. If these were the only 3 debtors, what would the balance on the debtors' control account be?
Total of debtors' accounts = balance on debtors' control account.
 $R13\ 500 ✓✓$ [2]
4. Is this business controlling their debtors effectively? Explain, quoting figures.
The answer to this question could be yes or no.
Yes ✓, because only one of the 3 debtors is outstanding. ✓✓✓
or
No ✓, because the amount outstanding for more than 60 days is R1 700 out of the total of R13 500 owed by the debtors. ✓✓✓ [4]

5.4 Creditors reconciliation with the creditor's statement

- a) At the end of each month a creditor's reconciliation is drawn up when the statement is received from a creditor and compared against the creditor's ledger account in the Creditors Ledger.
- b) The comparison must be done to ensure that all the details of the transactions with the creditor are correct prior to any payments being done.
- c) Ensure that you are aware that in the books of the creditor you are a debtor. So when you interpret the statement received from the Creditor, you read it as if you read a Debtors control account. In that way this section becomes very easy. Look and see that for every debit entry in your books, the creditor will credit the transaction. So, know the FORMAT of both the CONTROL ACCOUNTS and know the SOURCE DOCUMENTS.



Example

- Creditor gives you an invoice and you receive the invoice (renumber the invoice)
- You sent goods back to Creditor and issue a debit note and the creditor acknowledges the return and issues a credit note
- You pay your account by cheque and the Creditor acknowledges it by issuing a receipt

Study the following schematic illustration

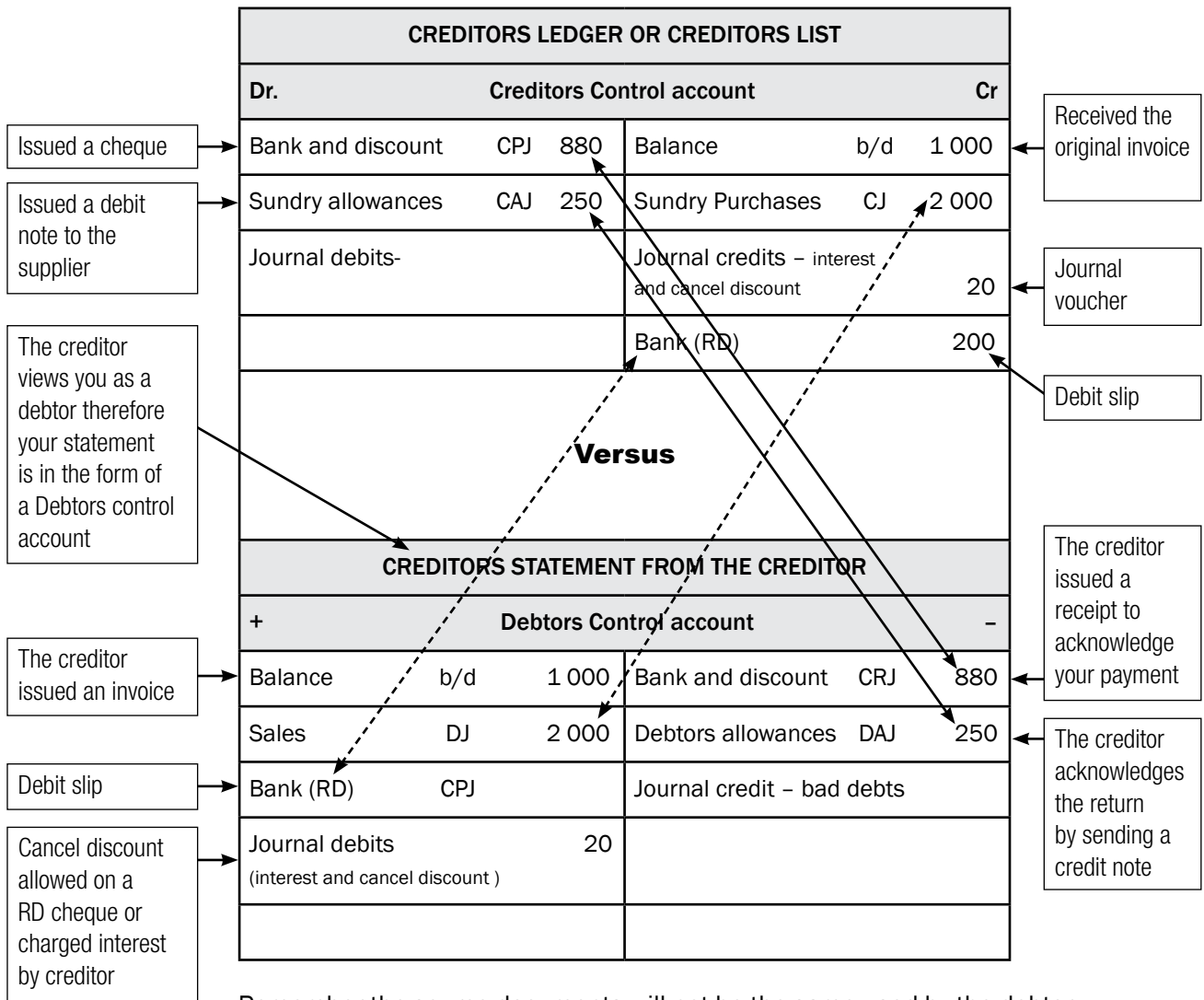
CREDITOR'S LEDGER				
In the books of the business Bongi & Co	Folio	Debit -	Credit +	Balance
Account Rendered			1 000	
Invoice received	CJ		2 000	3 000
Debit note issued	CAJ	250		2 750
Cheque counter foil	CPJ	880		1 870

CREDITORS STATEMENT OF BONGI AND CO				
In the books of the Creditor: Kima Wholesalers	Folio	Debit +	Credit -	Balance
Balance brought forward			1 000	
Invoice issued	DJ	2 000		3 000
Credit note issued	DAJ		250	2 750
Receipt issued	CRJ		880	1 870

Diagrammatic connections between the two tables:

- A dashed arrow points from the 'Account Rendered' row in the Creditor's Ledger to the 'Balance brought forward' row in the Creditors Statement.
- A dashed arrow points from the 'Invoice received' row in the Creditor's Ledger to the 'Invoice issued' row in the Creditors Statement.
- A dashed arrow points from the 'Debit note issued' row in the Creditor's Ledger to the 'Credit note issued' row in the Creditors Statement.
- A dashed arrow points from the 'Cheque counter foil' row in the Creditor's Ledger to the 'Receipt issued' row in the Creditors Statement.
- A solid arrow points from the 'Debit + 250' cell in the Creditors Statement to the 'Debit - 250' cell in the Creditor's Ledger.
- A solid arrow points from the 'Credit - 880' cell in the Creditors Statement to the 'Debit - 880' cell in the Creditor's Ledger.

SCHEMATIC ILLUSTRATION OF THE CORRELATION BETWEEN THE CREDITOR AND DEBTOR



Remember the source documents will not be the same used by the debtor and the creditor. The one receives and the other one issues.



Example

Example adapted from November 2011 NSC question paper

CREDITORS' RECONCILIATION

A statement received from a creditor, Kairo Suppliers, on 28 February 2011, reflects that Ace Traders owes them R11 390. According to Ace Traders, the amount outstanding is only R7 910.

REQUIRED:

Use the Table in the ANSWER BOOK to indicate the differences that were discovered when comparing the account in the Creditors' Ledger with the statement received from Kairo Suppliers.

Write only the amounts in the appropriate column and a plus (+) or minus (-) sign to indicate an increase or decrease in the balance. Calculate the correct balance/total at the end.

INFORMATION:

On investigation, it was found that:

1. A cheque for R3 000 issued by Ace Traders has not yet been recorded in the statement received from Kairo Suppliers.
2. The cheque in settlement of the January account was not received by Kairo Suppliers within 7 days; therefore the discount of R500 recorded by Ace Traders in the Creditors' Ledger must be cancelled.
3. Returns recorded as R810 in the Creditors' Ledger of Ace Traders were recorded as R900 in the statement received from Kairo Suppliers. Ace Traders had miscalculated the cost of goods returned.
4. An invoice received from Kairo Suppliers was correctly recorded as R7 700 by Ace Traders. However, in the statement received from Kairo Suppliers it was incorrectly recorded as R770.
5. An invoice for R3 500 received from Kairo Suppliers was incorrectly recorded as a credit note by Ace Traders.

Explanation of the transactions:

	Error	Explanation
1.	A cheque for R3 000 issued by Ace Traders has not yet been recorded in the statement received from Kairo Suppliers.	This cheque was paid to the creditor however the amount has not been subtracted yet from the balance on the statement. The balance owing to the Creditor, Kairo Suppliers, must decrease by R3 000. (The statement is like the Debtors Control account. Increase on the dr side and decrease on the cr side) This payment must be deducted in the Reconciliation/Creditors Statement (-R3 000)
2.	The cheque in settlement of the January account was not received by Kairo Suppliers within 7 days; therefore the discount of R500 recorded by Ace Traders in the Creditors' Ledger must be cancelled.	Ace Traders claimed R500 discount when he settled his account. (Bank and discount is on the debit side of the creditors control account). Kairo Suppliers refused the discount because the payment was received after 7 days. To cancel the discount the amount must be credited. (Creditors control increases on the credit side) The entry must be done in the debtors ledger and added
3.	Returns recorded as R810 in the Creditors' Ledger of Ace Traders were recorded as R900 in the statement received from Kairo Suppliers. Ace Traders had miscalculated the cost of goods returned.	Ace Traders has recorded R810 in the Creditors ledger instead of R900. Undercasted by $900 - 810 = R90$. Returns are recorded on the debit side of Creditors control account. (Creditors control account decreases on the debit side.) R90 must be subtracted in the Creditors ledger
4.	An invoice received from Kairo Suppliers was correctly recorded as R7 700 by Ace Traders. However, in the statement received from Kairo Suppliers it was incorrectly recorded as R770.	The creditors ledger was correct but the statement is wrong/ undercast by $R7700 - R770 = R6 930$. Any mistakes on the statement are corrected in the Reconciliation statement however the question reads that the Statement must be corrected. The statement must increase; (+R6 930)

E.	An invoice for R3 500 received from Kairo Suppliers was incorrectly recorded as a credit note by Ace Traders.	<p>The Creditors statement is correct.</p> <p>The Creditors ledger is incorrect; the invoice of R3 500 received is recorded as returns. This means the correct amount was recorded on the wrong side of the account, To cancel the R3 500 on the debit side, R3 500 must be credited to cancel the wrong entry and another R3 500 must be recorded to record the invoice received.</p> <p>No entries were made.</p> <p>This double entry (R3 500 +R3 500 = R7 000) needs to be recorded on the credit side of the Creditors ledger</p>

Use the Table to indicate the differences that were discovered when comparing the account in the Creditors' Ledger with the statement received from Kairo Suppliers.

Write only the amounts in the appropriate column and a plus (+) or minus (-) sign to indicate an increase or decrease in the balance. Calculate the correct balance/total at the end.

	Creditors' Ledger of Ace Traders	Statement from Kairo Suppliers
Balance	R7 910	R11 390
1		- 3 000
2	+500	
3	- 90	
4		+ 6 930
5	+3 500 ✓ +3 500 ✓ OR +7 000	
Balance/Total	15 320	15 320



Below is a list of suggested past examination questions for extra practice:

TOPIC	PAPER	QUESTION
Bank reconciliation	February/March 2009	1.1
Bank reconciliation	November 2010	2
Creditors reconciliation	February/March 2009	1.2
Debtors control account and Age analysis	February/March 2010	1
Debtors reconciliation, age analysis and internal control	February/March 2012	6
Debtors reconciliation	November 2013	1.3



Inventories

6.1 Inventory systems

A business can decide which of the following two **inventory systems** to use to record and control their inventory:

SYSTEM	IMPORTANT POINTS
Perpetual	<ul style="list-style-type: none"> a) Entries are made in a Balance Sheet account called trading stock (an asset account) every time goods are bought and sold. b) Cost of sales needs to be calculated and recorded every time goods are sold. c) When stock is purchased the trading stock account is debited with the cost price (the asset is increasing). d) When stock is sold the trading stock account is credited with the cost price (the asset is decreasing). e) Any additional costs when purchasing stock are debited to the trading stock account (e.g. carriage on purchases). f) This system is better for the internal control of inventory.
Periodic	<ul style="list-style-type: none"> a) Businesses would decide to use this system when it is not always feasible to calculate cost of sales every time goods are sold. b) Stock purchases are recorded in a nominal account called purchases (an expense account). c) Additional expenses when purchasing stock (e.g. carriage on purchases) are recorded separately in a nominal account called carriage on purchases (an expenses account). d) Cost of sales is therefore only calculated periodically by using the formula: Opening stock + purchases + carriage on purchases + import duties + customs duties – closing stock = cost of sales.



Inventories (trading stock) are goods that are bought in order to be resold at a profit. Stock is always recorded in the books at cost price.

6.2 Inventory valuation methods

The business may not change its stock valuation method unless the business has a very good reason to do so (e.g. the change will ensure that the inventory is better valued).

→ A business can decide which of the following two **stock valuation methods** to use in order to value its inventory:

METHOD	IMPORTANT POINTS
Specific Identification method	<ul style="list-style-type: none"> a) This is the simplest form of stock validation, where every item is assigned a specific cost price. b) This system is relevant when large commodities are sold and every unit has its own cost price, e.g. vehicles, machinery, etc. c) That means that this system requires that the cost price must be identified of every commodity sold or when stocktaking is done. d) Specific identification is a more manually intensive method in managing the stock. e) So every item in stock will be recorded at the specific price originally bought. f) The disadvantage of this method is that the price of a vehicle can be manipulated. For example a red Ford 1.6 was bought at the beginning of the year for R100 000 and during the year the dealer bought a white Ford 1.6 at an increased cost price of R130 000. When the red car got sold the dealers can manipulate the price by recording the cost price as R130 000. So the profit was manipulated by showing a smaller profit than the true profit. The dealers can do the opposite as well when they want to show a higher profit.
FIFO	<ul style="list-style-type: none"> a) FIFO stands for First In First Out. b) Businesses that sell goods which have a limited shelf life (e.g. milk or cellphones) often prefer to use this system. c) This means that the oldest stock is sold first and that the stock left at the end will always be the most recently bought stock. d) Under this method the stock on hand will be valued at the most recent prices.
Weighted average	<ul style="list-style-type: none"> a) Under this system the value of the stock on hand is not calculated on the most recent prices because all prices on stock purchased are averaged. b) Weighted average is calculated by dividing the total cost of stock purchased by the total number of units purchased. c) Under this method the stock on hand will not be valued at the most recent prices.



Worked example 1

You are provided with the information relating to Kima Appliances. The following stock appeared on their stock cards. Study the template of the number of stock bought at purchase price and the selling price of all the stock sold.

INFORMATION

The items below were in stock and some sold: January to December 2014

Date		LG			Samsung			Bosch			Total value of stock
		No	Cost price	Total	No	Cost price	Total	No	Cost price	Total	
Jan	Opening stock	2	@R1 000	R2 000	3	@R2 000	R6 000	4	@R3 000	R12 000	= R 20 000
April	Purchases	3	@R1 200	R3 600	2	@R2 100	R4 200	2	@R3 300	R6 600	= R 14 400
Value of total stock											R 34 400
		No	Cost price	Selling price	No	Cost price	Selling price	No	Cost price	Selling price	
Jan to	Sales	1	@R1 000	R2 000	3	@R2 000	R12 000	3	@R3 000	R18 000	= R 32 000
Dec.	Sales	2	@R1 200	R4 800				1	@R3 300	R6 600	= R 11 400
Value of total sales											R 43 400

*REQUIRED:

Make use of the Specific Identification stock method to calculate:

- Number of unsold units. ←
- Value of unsold units
- Cost of Sales
- Gross profit

You need to tick off the stock sold to calculate the stock on hand. (Closing stock)

Answers to worked example 1

1. Number of unsold units:

LG:	1	@ R1 000 (1 sold)
LG:	1	@ R1 200 (2 sold)
Samsung:	2	@ R2 100
Bosch:	1	@ R3 000 (3 sold)
	<u>1</u>	@ R3 300 (1 sold)
	<u>6</u>	unsold units

2. Value of unsold units:

LG:	1	@ R1 000(1 sold)	R 1 000
LG:	1	@R1 200 (2 sold)	R 1 200
Samsung:	2	@R2 100	R 4 200
Bosch:	1	@R3 000 (3 sold)	R 3 000
	<u>1</u>	@R3 300 (1 sold)	<u>R 3 300</u>
	<u>6</u>	unsold units	<u>R12 700</u>

Answers to worked example 1 continued (see page 101)

3. Cost of Sales (Goods sold at cost price)

LG: sold	1	@ R1 000	R 1 000
LG: sold	2	@R1 200	R 2 400
Samsung: sold	3	@R2 000	R 6 000
Bosch: sold	3	@R3 000	R 9 000
	<u>1</u>	@R3 300	<u>R 3 300</u>
	Cost of sales of 10 sold units		<u>R21 700</u>

4. Gross profit:

$$\begin{aligned} \text{Sales} - \text{Cost of Sales} &= \text{Gross profit} \\ R43\,400 - 21\,700 &= R21\,700 \end{aligned}$$



Worked example 2

Example adapted from March 2011 NSC question paper.

You are provided with information relating to Energy World for the year ended 28 February 2010. They sell energy drinks to retailers.

Required

Refer to the information relating to the energy drinks and calculate the following:

- Value of the closing stock using the FIFO and weighted-average methods. [14]
- Cost of sales using the FIFO and weighted-average methods. [11]
- Gross profit using the FIFO and weighted-average methods. [6]

Information

Manager: Dirk	Product: Energy drinks		
	Units	Rand	Amount
Sales	2 720	R21,20	R57 664
Opening stock	320	R9,00	R2 880
Purchases	4 800		R58 560
April 2008	1 100	R10,50	R11 550
October 2009	2 500	R12,42	R31 050
January 2010	1 200	R13,30	R15 960
Closing stock	2 400	?	?

Answers to worked example 2 (see page 102)

1. Calculate the value of the closing stock using the FIFO and weighted-average method.

FIFO	WEIGHTED AVERAGE
(Jan 2010) 1 200 units × R13,30 = R15 960✓✓ (Oct 2009) 1 200 units × R12,42 = R14 904✓✓ 2 400 units (closing stock) = R30 864 ✓ The most recent stock bought is what is left (closing stock).	Step 1 Opening stock = R2 880✓ Purchases = R58 560✓ Total cost = R61 440✓ Weighted average = R61 440 ÷ (320 + 4 800 units) = R61 440✓ ÷ 5 120✓ units = R12✓ per unit Step 2 ∴ 2 400✓ units (closing stock) × R12✓ = R28 800 ✓

Explanation of the calculations above

- The closing stock is 2 400 units.
- Using the FIFO method means that 1 200 units bought in January 2010 and 1 200 units of the 2 500 units bought in October 2009 are left in stock, representing the closing stock of 2 400 units.
- Step 1** is to calculate the weighted average by dividing the total cost of stock purchased by the total number of units purchased.
- Step 2** uses the weighted average to calculate the value of the closing stock by multiplying the cost per unit by 2 400.

[14]

2. Cost of sales using the FIFO and weighted-average method.

FIFO	WEIGHTED AVERAGE
320 units × R9 = R 2 880✓ 1 100 units × R10,50 = R11 550✓ 1 300 units × R12,42 = R16 146✓ Cost of sales <u>R30 576</u> ✓ OR Opening stock R2 880 + Purchases R58 560 - Closing stock (R30 864) = Cost of sales <u>R30 576</u>	Step 1 320✓ units + 4 800✓ units - 2 400✓ units = 2 720✓ units sold Step 2 ∴ 2 720✓ units sold × R12✓ (weighted average) = R32 640✓ Cost of sales

EXPLANATION OF THE CALCULATIONS ABOVE

- Using the FIFO method means that the oldest stock has been sold first, that is 320 units of opening stock + 1 100 units purchased in April 2008 + 1 300 units of the 2 500 units purchased in October 2009 making up the total of 2 720 units sold.
- Step 1** is the calculation of the number of units sold.
- Step 2** uses the weighted average to calculate the value of the stock that has been sold, namely 2 720 units.

[11]



The cost of sales is the cost price of all the goods that **have been sold**.

3. Gross profit using the FIFO and weighted-average method.

FIFO	WEIGHTED AVERAGE
Gross profit = sales – cost of sales	
R57 664✓ – R30 576✓ = R27 088✓	R57 664✓ – R32 640✓ = R25 024✓
Explanation of the calculations above	
<p>The sales figure was given in the question and is the same in both methods.</p> <p>The cost of sales figures were calculated by you in question 2 on page 67.</p> <p>You will notice that the gross profit figure is different in the 2 methods because the cost of sales was calculated differently.</p>	

[6]

Method to approach examination questions on stock validation

Learners do not know how to extract and record the relevant information from the stock validation question.

Learners usually know how to calculate gross profit and cost of sales, etc. however they cannot apply that knowledge to the information that is given.

The following is found to assist and to make this question in the examination a breeze:

- It is important that you memorise the format of the TRADING ACCOUNT using the periodic stock method
- It doesn't matter how they present the question in the exam, after drawing up the Trading account with two columns on the debit and on the credit side, just find the opening stock and closing stock and all the other figures and record the figures on your template.

Calculations

DR	TRADING ACCOUNT				CR	
	Amount	Units		Amount		Units
+ Opening stock			Closing stock			= Cost of sales (units)
+ Purchases (net)			Sales(net)			= gross profit
+ Carriage on purchases						
+ Custom Duties						
Total amount and units of all the stock that could be sold						

- To be able to answer all the questions, you need to draw the Trading account with TWO COLUMNS; ONE FOR THE RAND AMOUNT AND ONE FOR THE UNITS.

- Need to memorise that opening stock
 - plus **net** purchases (purchases minus Creditors allowances)
 - plus carriage on purchases
 - plus custom duties
 - minus closing stock is equal to **COST OF SALES**
 - Need to memorise that Opening stock
 - plus net purchases
 - plus carriage on purchases
 - plus custom duties
 - minus closing stock
 - minus **net** sales (sales minus debtors allowances)
 - is equal to **GROSS PROFIT**.
- OR** Sales (net) – Cost of sales = Gross profit.

Record all the figures from the question in the Trading account and then start to answer the questions.

Draw the following before attempting the question on stock validation

'(Net)' reminds you to subtract returns from the purchases

Stock validation is all about the calculation of the closing stock!

Sales minus returns

Number of items in stock

Dr.		Trading account				Cr		
		R	units			R	units	
+	Opening stock R10	100	10	-	Closing stock	?	25	= Cost of sales 10 + 90 - 25 = 75
+	Purchases (net)	1 330	90	-	Sales (net)	3 000	75	= gross profit
	@R12	480	40		@40 × 75			
	@R15	450	30					
	@R20	400	20					
+	Carriage on purchases @ R2 p unit × 90	180						
+	Custom duties @ 0,50c per unit × 90	45						
		1 655	100					

Total value of all the items that can be sold

Total units that can be sold are 10 + 90 = 100

75 units should be sold. Compare it with the Sales units sold to detect if any units were stolen

Possible questions: Learn formats and understand	
Value of the closing stock: FIFO	25 units: Start with the stock purchased recently. $20 \times R20 = 400$ $5 \times R15 = 75$ $25 \times R2 = 50$ Carriage on purchases per unit $25 \times R0,50 = 13$ (12,50) custom duties per unit Closing stock = R538
Value of closing stock: Weighted Average	Total the debit side's amount and unit column $R1655 \div 100 \text{ units} = R16,55$ average price per unit Closing stock is $25 \times R16,55 = R413,75$ (R414)
Cost of sales: Need to memorise the format! FIFO	Opening stock + Purchases(net) + Carriage on purchases + Custom duties – closing stock = Cost of sales $100 + 1330 + 180 + 45 - 538 = R1117$ (FIFO)
Gross profit: FIFO	Sales (net) – cost of sales = Gross profit $3\ 000 - R1117 = R1\ 883$
5. Mark -up: know the formula $\frac{\text{Gross profit}}{\text{Cost of sales}} \times \frac{100}{1} = \%$	$\frac{1883}{1117} \times \frac{100}{1} = 168,58\%$ Most of the times you need to explain why the profit markup was not achieved of e.g. 200%. Reason is because of seasonal sales and cash discounts.
Rate of stock turnover $\frac{\text{Cost of sales}}{\text{Average stock}} = \text{times}$	$\frac{1117}{(100 + 538)/2} =$ $\frac{1117}{319} = 3,5 \text{ times}$ The stock is replaced 3,5 times per year
Period of stock on hand $\frac{\text{Average stock}}{\text{Cost of sales}} \times \frac{365}{1} = \text{days}$	$\frac{319}{1117} \times \frac{365}{1} = 104,24 \text{ days}$ Stock is on the shelf for 104 days before it is sold. This ratio assists a business to determine when to order stock.

(NSC FEB/MARCH 2009 Exam paper)**Activity 1****Inventory regulation****(35 marks; 20 minutes)**

You are provided with information in respect of Magic Soccer Balls Shop for the year ended 28 February 2009. The business is owned by Peter Pule.

The business uses the perpetual inventory system and the FIFO method of valuing stock.

REQUIRED:

- 2.1** Explain the meaning of the term 'FIFO'. (2)
- 2.2** The selling price of soccer balls was kept constant throughout the year. Calculate the selling price per soccer ball. (3)
- 2.3** The owner, Peter Pule, is aware that some soccer balls were stolen from the storeroom in April 2008. No entry has been made.
- Calculate the number of balls that are missing. (stock stolen from the opening stock @ R110) (5)
 - What entry would you make in the books to record this? (2)
- 2.4** Value the stock on hand at the year-end according to the FIFO method. (7)
- 2.5** Calculate following:
- Cost of sales (5)
 - Gross profit for the year. (3)
- 2.6** Peter is not sure when to place his next order of soccer balls.
- How long can he expect the closing stock to last? Provide figures or a calculation to support your answer. (4)
 - What advice will you offer Peter about his purchases of stock? Provide two points. (4)

INFORMATION:

Accounting records relating to the soccer balls:

Details	Date	No. of balls	Unit price	Total
Opening stock	1 March 2008	750	R110	R 82 500
Purchases		2 480		R 340 800
	20 May 2008	800	R150	R 120 000
	25 October 2008	1 200	R120	R 144 000
	16 December 2008	480	R160	R 76 800
Closing stock	28 February 2009	1 100	?	?
Sales	1 March 2008 to 28 February 2009	2 100	?	R 430 500

[35]

ANSWER

2.1	Explain the meaning of the term 'FIFO'.	2
2.2	The selling price of soccer balls was kept constant throughout the year. Calculate the selling price per soccer ball.	3

Get all the info from the Trading account

Calculate the total number units that can be sold minus closing stock and compare that with the sales units.

The Closing stock will be the stock that you recently bought.

Opening stock + Purchases (net) + Carriage on purchases + custom duties – closing stock = cost of sales (make sure you memorised the formula)
 Stock stolen must be taken into account when you calculate the Cost of sales amount.

Stock holding period or called Period of stock on hand

2.3	<p>Calculate the number of balls that are missing.</p> <p>What entry would you make in the books to record this?</p>	7
2.4	<p>Value the stock on hand at the end of the year according to the FIFO method.</p>	7
2.5	<p>Calculate cost of sales.</p> <p>Calculate gross profit for the year.</p>	8
2.6	<p>How long can he expect the closing stock to last? Provide figures or a calculation to support your answer.</p> <p>What advice would you offer Peter about his purchases of stock? Provide two points.</p>	8

TOTAL MARKS
35

(NSC FEB/MARCH 2009 Exam paper)

Calculations for Activity 1

1. Draw the Trading account
2. Record the figures from the question in the trading account
3. Do you need to calculate on FIFO or weighted average method?
4. If Weighted average: add the totals at the bottom for the Rand and units and divide to find the average price to calculate the value of the closing stock
5. If FIFO: find number of units of stock and see which stock is last purchased
6. If FIFO: need to calculate the carriage on purchases per unit to be added on to the closing stock per unit.

Possible format for all the calculations.

Trading account for calculation purposes								
		R	units			R	units	
+	Opening stock @ R110	82 500	750	-	Closing stock	151 200	1 100	= Cost of sales $750 + 2\,480 - 1\,100 = 2\,130$ units supposed to be sold
					@160	76 800	480	
					@120 FIFO	74 400	620	
+	Purchases (net)	340 800	2 480	-	Sales(net)	430 500	2 100	= gross profit
	@R150	120 000	800		R430 500			
	@R120	144 000	1 200		$\div 2\,100 =$			
	@R160	76 800	480		R205			
+	Carriage on purchases @R							
+	Custom duties@							
	Total units at cost price that can be sold	423 300	3 130					

Any stock stolen? Yes, according to the stock 2 130 must be sold but the Sales shows only 2100 were sold

The following is part of your rough work and possible calculations

2.1 First in first out

2.2 Sales per unit; $R430\,500 \div 2\,100 \text{ unit} = R205$

2.3 A. Opening stock units: 750
Purchases units + 2 480
Closing stock units – (1 100)

Equals to the 2 130 units that must be sold however the actual sales were 2 100 units.

So $2\,130 - 2\,100 = 30$ soccer balls stolen.

B. Debit stolen stock and credit purchases

2.4 1 100 stock on hand: $480 \text{ units} \times R160 = R76\,800$

$1\,100 - 480 = 620 \text{ units} \times R120 = R74\,400$

Value of closing stock = R151 200

2.5 Cost of sales: $82\,500 + 340\,800 - 151\,200 - (30 \times 110 = 3\,300) = 268\,800$

Gross profit: $430\,500 - 268\,800 = 161\,700$

2.6 Period of stock on hand ratio:

(Most of the time these questions are asked in the examination questions. Therefore: know your formula! See Solutions of this activity.)

ANSWER

QUESTION 2		
2.1	<p>Explain the meaning of the term 'FIFO'.</p> <p>First-in first-out ✓✓ OR The oldest soccer balls are the ones that are sold first</p>	2
2.2	<p>The selling price of soccer balls was kept constant throughout the year. Calculate the selling price per soccer ball.</p> <p>✓ ✓ ✓ $R430\,500 / 2\,100 \text{ balls} = R205 \text{ each}$</p>	3
2.3	<p>Calculate the number of balls that are missing.</p> <p>Total balls available = $750 \checkmark + 2\,480 \checkmark - 1\,100 \checkmark$ = 2 130 balls Number sold = 2 100 balls ✓ Number stolen = 30 balls ✓</p> <p>What entry would you make in the books to record this? ✓ Debit Trading stock deficit/Loss due to theft R3 300 ✓ Credit Trading stock R3 300</p>	7
2.4	<p>Value the stock on hand at the end of the year according to the FIFO method.</p> <p>✓ 480 balls at R160 ✓ = R 76 800 ✓ ✓ 620 balls at R120 ✓ = R 74 400 ✓ TOTAL = R151 200 ✓</p>	7

<p>2.5 Calculate cost of sales</p> <p>Opening stock R 82 500 ✓ Purchases 340 800 ✓ Stolen - 3 300 ✓ Closing stock - 151 200 ✓ Cost of sales R268 800 ✓</p> <p>Calculate gross profit for the year.</p> <p>Sales R430 500 ✓ Cost of sales -268 800 ✓ Gross profit 161 700 ✓</p>	8
<p>2.6 How long can he expect the closing stock to last? Provide figures or a calculation to support your answer.</p> <div style="border: 1px solid black; padding: 5px; margin: 10px 0;"> <p>Any valid evidence provided e.g. ✓✓ Figures ✓✓</p> $\frac{\text{Closing stock}}{\text{Cost of sales}} \times \frac{365}{1} = \text{days}$ $\frac{151\,200}{268\,800} \times \frac{365}{1} = 205 \text{ days/6,7 months}$ </div> <p>On average, 175 balls are sold per month – stock will last 6,3 months OR Cost of sales for the year is R268 800 (R22 400) – final stock is R151 200 – stock could last 6,8 months</p> <p>What advice will you offer Peter about his purchases of stock? Provide two points. Any two valid points, e.g. ✓✓ ✓✓</p> <ul style="list-style-type: none"> • Purchase in smaller quantities more often • Only order when they reach their minimum stock level (re-order level) • They are holding too much stock. 	8

(NSC NOVEMBER 2009 exam paper)



Activity 2

Inventory valuation and control (40 marks; 24 minutes)

You are provided with information relating to Banyana Traders, owned by David Hambeck, for the financial year ended 28 February 2009. The business is situated in Johannesburg.

David buys and sells soccer balls and jerseys. The business uses the periodic inventory system.

The soccer balls are bought from South African suppliers, and the soccer jerseys of different clubs and countries are imported from overseas.

David employs salespersons to control each item of stock:

- James controls and sells the soccer balls
- Cyril controls and sells the soccer jerseys

David has decided on the following accounting policies for valuing inventory:

- Soccer balls – Weighted-average method
- Soccer jerseys – First-in-first-out method (FIFO)

REQUIRED:

- 2.1** Although this business has done well; David is considering closing it down and investing his capital in fixed property. State TWO points that he should consider before making a final decision. (4)
- 2.2** David suspects that a number of soccer balls have been shoplifted. Calculate the number of soccer balls stolen. (5)
- 2.3** Use the relevant information to calculate the closing stock value of:
- Soccer balls (using the weighted-average method) (6)
 - Soccer jerseys (using the FIFO method) (6)
- Show your workings to earn part-marks. (5)
- 2.4** Calculate the following for soccer jerseys (you may prepare a Trading Account to calculate these figures):
- Cost of sales
 - Mark-up % on cost
 - Stock turnover rate
- 2.5** If David decides to continue with this business, what advice would you offer him? State TWO points and quote financial indicators or specific information from the question to support your answer. (6)

INFORMATION:

1. Inventories:

The stocks were valued as follows at the beginning and end of the financial year: Date	Soccer balls			Soccer jerseys		
	No. of units	Per unit	Total value	No. of units	Per unit	Total value
01/03/08	1 200	R120	R144 000	520	R320	R166 400
28/02/09	900	?	?	250	?	?

2. Purchases:

During the financial year ended 28 February 2009, the following stock items were purchased:

Date of purchases	Soccer balls			Soccer jerseys		
	No. of units	Per unit	Total value	No. of units	Per unit	Total value
31/03/08	1 300	R120	R156 000	400	R200	R 80 000
30/06/08	900	R150	R135 000	600	R225	R135 000
30/09/08	1 000	R175	R175 000	1 400	R255	R357 000
02/01/09	200	R180	R 36 000	100	R300	R 30 000
Totals	3 400		R502 000	2 500		R602 000

3. Carriage on purchases:

During the year, the business paid a total of R30 200 to transport soccer balls to the shop. The price of the soccer jerseys includes carriage.

4. Sales:

Items	Details	Total
Soccer balls	3 500 units at R320 each	R1 120 000
Soccer jerseys	2 770 units at R400 each	R1 108 000

5. Financial indicators:

Items	Mark-up % on cost	Stock turnover rate
Soccer balls	48,5%	3,9 times p.a.
Soccer jerseys	?	? times p.a.

[40]

Calculations for Activity 2

- Draw the Trading account
- Record the figures from the question in the trading account
- Do you need to calculate on FIFO or weighted average method?
- If Weighted average: add the totals at the bottom for the Rand and units and divide to find the average price to calculate the value of the closing stock
- If FIFO: find number of units of stock and see which stock is last purchased
- If FIFO: need to calculate the carriage on purchases per unit to be added on to the closing stock per unit.

ANSWER SHEET

2.1	Although this business has done well, David is considering closing it down and investing his capital in fixed property. State TWO points that he should consider before making a final decision.	4
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2.2	Calculate the number of soccer balls stolen.	5
2.3	Calculate the closing stock value of soccer balls using the weighted average method:	11

2.4	Calculate the following for Soccer jerseys (you may prepare a Trading Account to calculate these figures): Calculate cost of sales: Calculate mark-up% on cost: Calculate stock turnover rate:	14
2.5	If David decides to continue with this business, what advice would you offer him? State TWO points and quote financial indicators or specific information from the question to support your answer.	6

TOTAL MARKS
40

Calculations for Activity 2

SOCCER BALLS		Trading account				WEIGHTED AVERAGE		
		R	units			R	units	
+	Opening stock @R	144 000	1 200	-	Closing stock 900 × R147	132 300	900	= Cost of sales Units 1 200 + 3 400 - 900 = 3 700 (SUPPOSED TO BE SOLD) ↑
+	Purchases(net) @R120 @R150 @R175 @R180	502 000 156 000 135 000 175 000 36 000	3 400 1 300 900 1 000 200	-	Sales (net) @ R320	1 120 000	3 500	= gross profit
+	Carriage on purchases @R	30 200						
+	Custom duties @ R							
	Total units at cost price that can be sold	676 200	÷ 4 600 = R147 weighted average per unit					

$$3\,700 - 3\,500 = 200 \text{ stolen}$$

Calculations for Activity 2

SOCCER JERSEYS		Trading account				FIFO		
		R	units			R	units	
+	Opening stock @R	166 400	520	-	Closing stock: @R300 × 100 @R255 × 150	68 250 30 000 38 250	250 100 150	= Cost of sales units
+	Purchases(net) @R200 @R225 @R255 @R300	602 000 80 000 135 000 357 000 30 000	2 500 400 600 1 400 100	-	Sales (net) @R400 × 2 772	1 108 000	2 772	= gross profit
+	Carriage on purchases @R	-	-					
+	Custom duties @	-	-					
	Total units at cost price that can be sold	768 400	3 020					

Answers for Activity 2

QUESTION 2														
2.1	<p>Although this business has done well, David is considering closing it down and investing his capital in fixed property. State TWO points that he should consider before making a final decision.</p> <p>Good answer = 2 marks; Poor answer = 1 mark; Incorrect = 0 marks ✓✓ ✓✓ Any two valid points, e.g. Soccer World Cup will be in SA soon – keep the business operational until then. Property prices are not doing well at the moment – move into this later. Financial implication to the business, future prospects Implications for staff – retrenchment</p>	4												
2.2	<p>Calculate the number of soccer balls stolen.</p> <p>1 200 ✓ + 3 400 ✓ – 3 500 ✓ – 900 ✓ = 200 ✓</p>	5												
2.3	<p>Calculate the closing stock value of soccer balls using the average method:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%;">Stock at beginning of year</td> <td style="width: 25%;">R144 000</td> <td style="width: 25%; text-align: right;">1 200</td> </tr> <tr> <td>Purchases during the year</td> <td>R502 000</td> <td style="text-align: right;">3 400</td> </tr> <tr> <td>Carriage on purchases</td> <td style="border-bottom: 1px solid black;">R 30 200</td> <td style="text-align: right;">-</td> </tr> <tr> <td></td> <td style="text-align: right;">R676 200 ✓</td> <td style="text-align: right;">÷ 4 600 ✓ = R147</td> </tr> </table> <p>= 900 ✓ × 147 ✓ = R132 300 ✓</p> <p>Calculate the closing stock value of soccer jerseys using the FIFO method:</p> <p>100 × R300 = R30 000 ✓✓</p> <p>$\frac{150}{250} \times R255 = \frac{R38 250}{R68 250} \checkmark \checkmark$</p>	Stock at beginning of year	R144 000	1 200	Purchases during the year	R502 000	3 400	Carriage on purchases	R 30 200	-		R676 200 ✓	÷ 4 600 ✓ = R147	11
Stock at beginning of year	R144 000	1 200												
Purchases during the year	R502 000	3 400												
Carriage on purchases	R 30 200	-												
	R676 200 ✓	÷ 4 600 ✓ = R147												
2.4	<p>Calculate the following for Soccer jerseys (you may prepare a Trading Account to calculate these figures):</p> <p>Calculate cost of sales:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%;">Opening stock ✓</td> <td style="width: 50%; text-align: right;">166 400</td> </tr> <tr> <td>Purchases ✓</td> <td style="text-align: right;">602 000</td> </tr> <tr> <td>Less closing stock ✓</td> <td style="text-align: right; border-bottom: 1px solid black;">(68 250)</td> </tr> <tr> <td>Cost of sales ✓</td> <td style="text-align: right;">700 150</td> </tr> </table> <p>Calculate mark-up% on cost:</p> <p>= $\frac{(1 108 000 \checkmark - 700 150 \checkmark)}{700 150 \checkmark} \times 100$ 1</p>	Opening stock ✓	166 400	Purchases ✓	602 000	Less closing stock ✓	(68 250)	Cost of sales ✓	700 150					
Opening stock ✓	166 400													
Purchases ✓	602 000													
Less closing stock ✓	(68 250)													
Cost of sales ✓	700 150													

	<p>OR</p> $\frac{407\ 850}{700\ 150} \times \frac{100}{1}$ <p>= 58,3 % ✓✓</p> <p>Calculate stock turnover rate:</p> $\frac{\text{Cost of sales}}{\text{Average stock}}$ $= \frac{7\ 00\ 150}{(68\ 250 + 166\ 400) / 2}$ $= \frac{700\ 150}{117\ 325} = 5,97 \text{ times } \checkmark\checkmark$	14
	<p>2.5 If David decides to continue with this business, what advice would you offer him? State TWO points and quote financial indicators or specific information from the question to support your answer.</p> <p>Good answer = 2 marks; Satisfactory answer = 1 mark; Incorrect = 0 marks Appropriate financial indicator/figures = 1 each Any two valid points ✓✓✓ ✓✓✓</p> <ul style="list-style-type: none"> • Implement tighter control measures over soccer balls – 200 balls were stolen • The business is carrying a lot of stock, particularly soccer balls – 900 on hand at end of year • Selling price must change if cost increases • The stock for soccer balls must be turned over quicker – 3,9 times per annum. 	6

Re-do questions 1 – 3 on paper, for extra practice.



Below is a list of suggested past examination questions for extra practice:

Topic	Paper	Question
FIFO and weighted average	February/March 2010	2
Weighted average calculations	November 2010	1.2
FIFO calculations	February/March 2012	1.2
Stock validation	November 2013	6.2



Value Added Tax

Value Added Tax (VAT) is the tax charged on goods and services supplied and is charged at the current rate (standard rate) of 14%. VAT is an important part of the income generated by the government to cover government expenditure.

Who has to register as a VAT Vendor?

A person or business that supplies goods or services can register as a vendor (trader).

All businesses with a turnover of more than R1-million must register as a vendor (trader). This is **COMPULSORY REGISTRATION**.

Businesses with a turnover of less than R1-million can register if they want to. This is **VOLUNTARY REGISTRATION**.

The benefits of registering as a VAT Vendor

The business is able to claim back the amount of VAT paid on goods and services bought (VAT input).

Items on which VAT is not charged

Zero-rated items: Items charged at 0% VAT, but this can be changed by the government at any time. Examples are fresh fruit and vegetables, brown bread, milk, maize, rice, lentils and cooking oil.

VAT-exempt items: Items on which no VAT is charged. Examples are interest, rates, export services, educational services and childcare services.

VAT input

VAT input is the VAT paid by a business on the purchases of goods and services (which can be claimed back from SARS).

VAT output

VAT output is the VAT collected by the business on the sale of all goods and services (which needs to be paid over to SARS).

Use mobile notes to help you learn these key VAT concepts.



7.1 VAT calculations

VAT output – VAT input = amount payable to SARS (see example 2, page 72)

VAT inclusive calculations:
(see example 1 below)

When VAT is included in an amount (VAT inclusive) the calculation for VAT will be **the amount** $\times \frac{14}{114}$

VAT exclusive calculations:
(see example 1 below)

When VAT is excluded (VAT exclusive) the calculation for VAT will be **the amount** $\times \frac{14}{100}$



The following calculations are very important. LEARN THEM WELL!



Worked example 1: Trendy Suppliers

Trendy Suppliers uses a fixed mark up of 40% on cost. The business is registered as a VAT vendor. The current VAT rate is 14%.

Calculate the following:

1. VAT charged by Trendy Suppliers on one dress. [3]
2. Selling price of one dress exclusive of VAT. [6]
3. VAT charged to the customer on one dress. [3]
4. VAT charged by Trendy Suppliers on one pair of jeans. [3]
5. Selling price of one pair of takkies inclusive of VAT. [9]

Information

The following items were purchased during the month from Trendy Suppliers.

100 dresses @ R285 each (VAT inclusive)

80 pairs of jeans @ R180 each (VAT exclusive)

60 pairs of takkies @ R110 per pair (VAT exclusive)

Answers to worked example 1

1. VAT charged by Trendy Suppliers on one dress. [3]

$$R285 \checkmark \times \frac{14}{114} \checkmark = R35 \checkmark$$

2. Selling price of one dress exclusive of VAT.

$$\text{Cost price} = R285 \checkmark - R35 \checkmark (\text{VAT}) = R250 \checkmark$$

$$\text{Selling price} = R250 \checkmark \times \frac{140}{100} \checkmark = R350 \checkmark$$

[6]

Remember:

Inclusive is $14 \div 114$

Remember:

Mark up = 40% on cost price

Answers to worked example 1 (continued from page 120)

3. VAT charged to the customer on one dress:

Selling price = R350 (as calculated in No 2 above) ←

$$\text{VAT charged} = \text{R}350 \checkmark \times \frac{14 \checkmark}{100} = \text{R}49 \checkmark$$

[3]

Remember:

Exclusive is $14 \div 100$

4. VAT charged by Trendy Suppliers on one pair of jeans:

$$\text{R}180 \checkmark \times \frac{14 \checkmark}{100} = \text{R}25,20 \checkmark \leftarrow$$

[3]

Remember:

Exclusive is $14 \div 100$

5. Selling price of one pair of takkies inclusive of VAT:

Cost price = R110

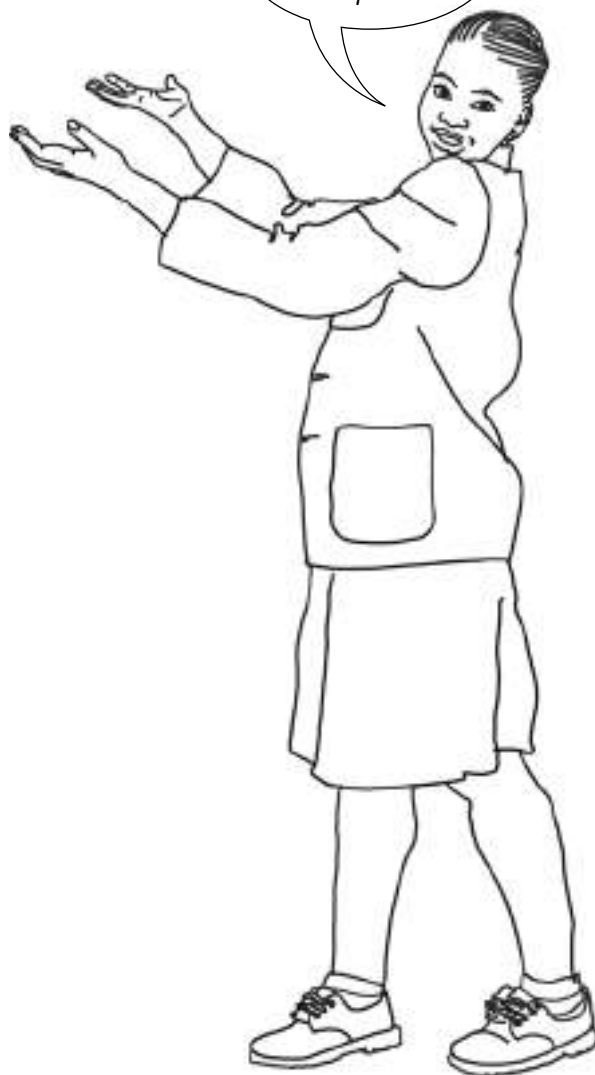
$$\text{Selling price} = \text{R}110 \checkmark \times \frac{140 \checkmark}{100} = \text{R}154 \checkmark \text{ (exclusive of VAT)}$$

$$\text{VAT} = \text{R}154 \checkmark \times \frac{14 \checkmark}{100} = \text{R}21,56 \checkmark$$

$$\text{VAT inclusive amount} = \text{R}154 \checkmark + \text{R}21,56 \checkmark = \text{R}175,56 \checkmark$$

[9]

Re-do questions 1 – 5 on paper, for extra practice.



e.g. Worked example 2: Mizi Stores

Mizi Stores, owned by Mia Mizi, is registered for VAT.
 Calculate the amount of VAT to be paid over to SARS for the period ending 28 February 2011. [17]

Information for this period ending 28 February 2011

- a) Total sales (cash and credit) (VAT inclusive) R60 000
- b) New computer bought (for office use) (VAT inclusive) R12 000
- c) Trading stock bought (VAT exclusive) R20 000
- d) Credit notes issued to customers (VAT inclusive) R 1 500

Answers to worked example 2

	VAT output	VAT input
a) Total sales: $60\ 000 \checkmark \times \frac{14 \checkmark}{114}$	R7 368,42 \checkmark	
b) New computer bought: $12\ 000 \checkmark \times \frac{14 \checkmark}{114}$		R1 473,68 \checkmark
c) Trading stock bought: $20\ 000 \checkmark \times \frac{14 \checkmark}{100}$		R2 800 \checkmark
d) Credit notes issued: $1\ 500 \checkmark \times \frac{14 \checkmark}{114}$		R184,21 \checkmark
	R7 368,42\checkmark	R4 457,89\checkmark
VAT payable to SARS: $R7\ 368,423 \checkmark - R4\ 457,893 \checkmark = R2\ 910,53 \checkmark$ Total VAT output - Total VAT input = VAT payable to SARS		

[17]



7.2 VAT Control Account

There are different formats of completing the Input and Output VAT accounts however the correct information does end up in the VAT Control account. It is not likely you will be asked to do the Input or Output VAT account in the examination. The VAT Control Account is more likely to be asked.

Learners need to be able to complete the VAT Control account with all the relevant transactions without completing the Input VAT Control and Output VAT Control accounts.

Format of possible entries in the VAT control account

GENERAL LEDGER									
Dr.		VAT CONTROL ACCOUNT (CL)				B		Cr.	
2014 May	3	Debtors Control	DAJ	56	2014 May	1	Bank	CRJ	4 200
	8	Discount allowed (claim VAT back from discount allowed amount)	GJ	8		2	Debtors Control	DJ	1 400
	12	Bad debts	GJ	28		9	Discount allowed (cancel the VAT claim)	GJ	8
	4	Bank	CPJ	700		10	Drawings	GJ	126
	6	Creditors control	CJ	280		11	Donations	GJ	42
	5	Petty cash	PCJ	21		7	Creditors control	CAJ	98
	31	Balance	c/d	4 781					
				5 874					5 874
					2014 June	1	Balance	b/d	4 781

- VAT Control account can have a debit balance or a credit balance.
- A debit balance means that SARS owes the business money and that your Input VAT was more than your Output VAT.
- A credit balance means that the business owes SARS money.

Amount owing to SARS

Schematic illustration of how all the entries from Output VAT Account and Input VAT account are recorded in the VAT Control Account

DR		OUTPUT VAT ACCOUNT ()		B		CR	
2014 May	31	DAJ	56	2014 May	31	Bank	4 200
Debtors Control							
Discount allowed (claim VAT back from discount allowed amount)		GJ	8			Debtors Control	1 400
Bad debts		GJ	28			Discount allowed (cancel the VAT claim)	8
VAT control						Drawings	126
						Donations	42

- The output VAT account is a current liability.
- It is the amount owing to SARS
- The account increases on the credit side

DR.		INPUT VAT CONTROL				B		DR	
2014 May	31	Bank	CPJ	700	2014 May	31	Creditors control	CAJ	98
		Creditors control	CJ	280					
		Petty cash	PCJ	21					

- The Input VAT account is a current asset.
- It is the amount that SARS owes the business.
- The Input VAT account increases on the debit side.

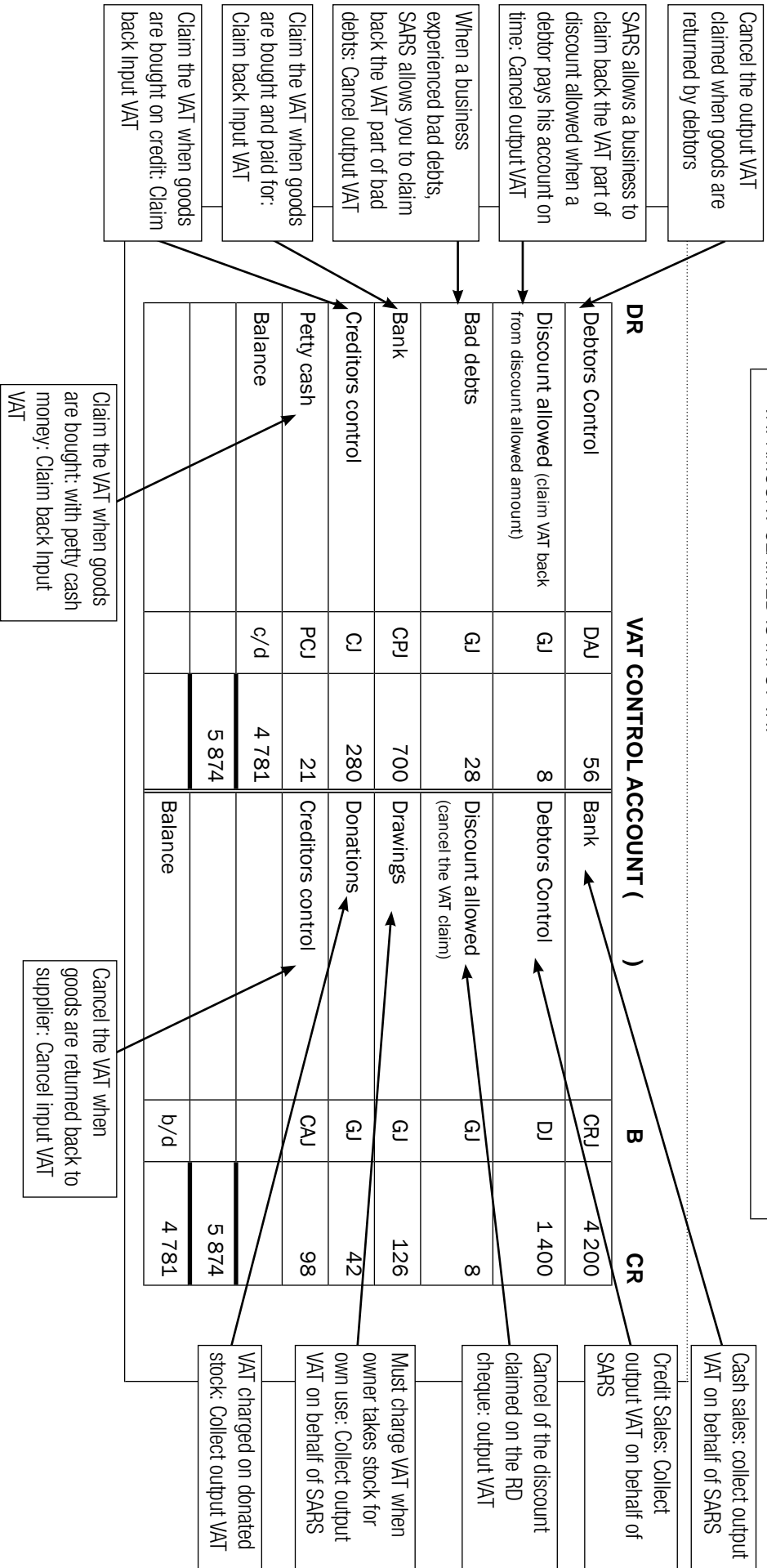
DR		VAT CONTROL ACCOUNT ()		B		CR	
2014 May	31	DAJ	56	2014 May	31	Bank	4 200
		Debtors Control					
		Discount allowed (claim VAT back from discount allowed amount)				Debtors Control	1 400
		Bad debts				Discount allowed (cancel the VAT claim)	8
		Bank				Drawings	126
		Creditors control				Donations	42
		Petty cash				Creditors control	98
		Balance					
							5 874
						Balance	4 781
							5 874
							4 781

Ensure that you know all the possible transactions and how the transactions are recorded in the VAT Control account.

Conclusion of the vat control account with all possible entries

Take into account that the VAT CONTROL ACCOUNT is done to establish if the amount collected on behalf of SARS is more than the amount claimed from SARS.

- VAT COLLECTED IS OUTPUT VAT
- VAT AMOUNT CLAIMED IS INPUT VAT





Below is a list of suggested past examination questions for extra practice:

TOPIC	PAPER	QUESTION
Calculations using General Ledger accounts	November 2010	1.3
Concepts and calculations	February/March 2012	1.1



Fixed assets

8.1 Introduction to Fixed assets

- All fixed assets purchased by a business are not intended for resale but to be used in the operation of the business to assist in generating a profit.
- Fixed assets are recorded at the price the asset was purchased called COST PRICE (GAAP principle, called Historical cost.)
- Separate records are kept for every fixed asset purchased in an asset register. Full details of every asset is recorded on the asset register and the depreciation for the financial year is calculated and recorded in the asset register and kept up to date at all times.
- Fixed assets are depreciated at cost price/ straight line method or at carrying value/ diminishing balance/ or called book value method.
- For internal control purposes, the assets and the registers are regularly monitored.
- When the asset is sold the asset register is updated; additional depreciation calculated, to whom it was sold and closed off as the asset does not belong to the business anymore.
- At the end of each financial year all the relevant fixed assets are depreciated. Any depreciation on assets sold during the year, form part of the depreciation amount disclosed in the Income Statement.

8.2 Asset register

Required:

Complete the following asset registers.

Information:

hint Cost price – accumulated depreciation = book value/CARRYING VALUE

Fixed assets can only be depreciated till the fixed asset reach the scrap value of R1, therefore the CARRYING VALUE of the fixed asset cannot be less than R1.



e.g. Example

Vehicle purchased: Cost price R80 000

Equipment: Cost price: R20 000

Transaction:

- A. Depreciation on vehicles must be brought into account at 20% per annum on cost price.
- B. Depreciation on equipment must be calculated at 10% per annum on carrying value.

A. DEPRECIATION AT COST PRICE:

Schie Traders		No.1	
Asset register			
General ledger account: <i>Vehicle account (B 6)</i>			
Item: <i>TOYOTA delivery van 3 litre</i>		Date purchased: <i>1 March 2009</i>	
From whom purchased: <i>Toyota Whiteriver</i>		Cost price: <i>R80 000</i>	
Percentage Depreciation: <i>20 % p.a. at cost price/straight line method</i>			
Details of depreciation			
Details	Annual depreciation calculations	Accumulated depreciation	Book value or known as "Carrying value"
End of first year			
End of second year			
End of third year			
End of fourth year			
End of fifth year			

DEPRECIATION AT CARRYING VALUE:

Schie Traders No.2
Asset register

General ledger account: Equipment account (B 7)

Item: *Office computer*

Date purchased:

From whom purchased: *DARRYN FURNITURES* Cost price: R20 000

Percentage Depreciation: 10% p.a. at carrying value/book value or called diminishing value

Details of depreciation

Details	Annual depreciation calculations	Accumulated depreciation	Book value or known as "Carrying value"
End of first year			
End of second year			
End of third year			
End of fourth year			
End of fifth year			

8.3 Residual value/or called scrap value of R1

Introduction

At the end of each financial year the asset register will be updated by calculating depreciation on all fixed assets. The total depreciation will then be recorded in the General Journal as the depreciation for the year. Depreciation is a legal way of decreasing the net profit so that less tax can be paid. However when the fixed asset reaches the end of its lifespan no more depreciation can be calculated. Depreciation can only be calculated till the asset reaches a carrying value of R1.

(Cost price minus Accumulated depreciation = carrying value)



Take note of the following scenarios.

- The R1 scrap value applies when an asset is depreciated. A Vehicle with a carrying value of R1 cannot be depreciated the following year.
(cost price minus accumulated depreciation = carrying value
 $R100\ 000 - R\ 99\ 999 = R1$)

DR	VEHICLE ACCOUNT	CR
	Balance b/d 100 000	

DR	ACCUMULATED DEPRECIATION	CR
		Balance b/d 99 999

- When an asset is sold that has a carrying value of R1, the cost price and the total accumulated depreciation of the vehicle sold will be closed off to the Asset disposal account.

ASSET DISPOSAL			
Vehicle	100 000	Accum. depreciation	99 999
Profit on sale of asset	39 999	Bank	40 000
	139 999		139 999

Because of the scrap value of R1, the profit is R39 999

In practice the scrap value principle is NOT applied when a fixed asset is sold that has not reached its R1 carrying value yet.

- However when an asset is sold that HAS NOT reached its carrying value of R1 yet but will soon, the scrap value principle (carrying value of R1) is not applied in practice.

e.g. Example

Vehicle is sold for R40 000 cash.

Cost price of vehicle: R100 000

Accumulated depreciation: R 90 000

Carrying value = R 10 000

Depreciation is calculated at 20% on Cost price

- Additional depreciation: $100\ 000 \times 20\% = R20\ 000$
- The carrying value is already R10 000 and that means that depreciation can only be R10 000.
- A fixed asset cannot be depreciated less than the cost price of the vehicle. (And not R9 999!)

ASSET DISPOSAL			
Vehicle	100 000	Accum. depreciation	100 000
Profit on sale of asset	40 000	Bank	40 000
	140 000		140 000

Because the principle of R1 is not applied, the profit is R40 000

8.4 Note to the Balance Sheet and Asset disposal

1. Know the format and the steps to follow when an asset is sold.
2. Know all the ledger accounts involved in calculating the
 - Additional depreciation when an asset is sold;
 - Depreciation of all the existing fixed assets at the end of the financial year (except Land and buildings).
 - Completion of Note 3 in the Balance sheet

Note 3 to the Balance sheet:

3. Property , plant and equipment	Land and buildings	Vehicles	Equipment	Total
Cost Price			60 000	
- Accumulated Depreciation			(20 000)	
= Carrying value on the last day of the previous year			40 000	
Movements:				
+ Additions at cost price			30 000	
- Disposals at carrying value (book value)			(5 000)	
- Depreciation for the year			(15 000)	
= Carrying value on the last day of current year			50 000	
Cost Price			85 000	
- Accumulated Depreciation at end of year			(35 000)	
= Carrying value on the last day of current year			50 000	

There are different formats of Note 3; however they have the same entries. Make sure that you use the format of one of the approved text books.



Steps to follow when disposing a fixed asset:

1. Find the cost price of fixed asset sold and move/transfer it to the Asset Disposal account.
2. Calculate any additional depreciation on fixed asset sold
3. Move/Transfer the total depreciation on fixed asset sold to Asset Disposal account.
4. Record the selling price of fixed asset sold in the Asset Disposal account.
5. Calculate the profit or the loss on sale of fixed asset sold.
6. At end of year, record the depreciation of the remaining fixed assets and new assets at the end of financial year.

General Ledger accounts

- Study the following General Ledger accounts.
- Ensure that you understand all the ledger accounts well.
- The entries are examples of all possible transactions in the applicable general ledger accounts when fixed assets are bought or sold.

- The procedure at the end of the financial year is also illustrated.

General Ledger of Star Traders

DR				VEHICLES (FA)				B1		CR	
2013 Mar	1	Balance	B/d	180 000	2013 Dec	31	Asset disposal	GJ			100 000
May	10	Creditors control	CJ	150 000	2014 Feb	28	Balance	c/d			280 000
Oct	10	Bank	CPJ	50 000							
				380 000							380 000
2014 Mar	1	Balance	B/d	280 000							

DR				ACCUMULATED DEPRECIATION ON VEHICLES (-A)				B2		CR	
2013 Dec	31	Asset Disposal (20000 + 5000)	GJ	25 000	2013 Mar	1	Balance	B/d			60 000
		Balance	C/d	40 000	Dec	31	Depreciation (additional)	GJ			5 000
				65 000							65 000
2014 Feb	28	Balance	C/d	50 000			Balance (Accu. Depreciation. of the remaining vehicles)	B/d			40 000
				50 000	2014 Feb	28	Depreciation (end of year)	GJ			10 000
					Mar	1	Balance	b/d			50 000

DR				ASSET DISPOSAL (calculation)				B3		CR	
2013 Dec	31	Vehicles	GJ	100 000	2013 Dec	31	Accumulated depreciation on vehicles	GJ			25 000
		Profit on sale of asset	GJ	5 000			Debtors control	GJ			80 000
				105 000							105 000

NOTE: Debtors control – when a vehicle was sold on credit
 Bank – when a vehicle was sold for cash
 Creditors control – when a vehicle was traded in to a second-hand dealer
 Drawings – When owner took asset for own purposes
 Donation – When a vehicle was donated.



NB Asset Disposal account must be closed off. (The Asset Disposal account will never have a balance because the difference will either be a profit on sale of asset or a loss on sale of asset)

DR				DEPRECIATION (e)				N		CR	
2013 Dec	31	Accumulated depreciation on vehicles (additional)	GJ	5 000	2014 Feb	28	Profit and loss (depreciation for the whole year)	GJ			35 000
2014 Feb	28	Accumulated depreciation on vehicles (end of year)	GJ	10 000							
		Accumulated depreciation on equipment	GJ	20 000							
				35 000							35 000

DR				PROFIT ON SALE OF ASSET (i)				N		CR	
2013 Dec	31	Profit and loss account	GJ	5 000	2014 Feb	28	Asset disposal	GJ			5 000

DR				LOSS ON SALE OF ASSET (e)				N		CR	
2013 Dec	31	Asset disposal	GJ	0	2014 Dec	31	Profit and loss account	GJ			0

Example 2 on note 3 in the Financial Statements

REQUIRED:

Complete Note 3 of the Balance sheet

INFORMATION:

Make use of the format and complete Note 3 from the financial Statements.

Name of Company _____

BALANCE SHEET AT _____

	Notes	
ASSETS		
Non-current assets		
Property, plant and equipment	3	

NOTES TO THE BALANCE SHEET

3. Property, plant and equipment	Vehicles
Cost Price	
Accumulated Depreciation	
Carrying value on the last day of the previous year	
Movements:	
Additions at cost	
Disposals at carrying value (book value)	
Depreciation for the year	
Carrying value on the last day of current year	
Cost Price	
Accumulated Depreciation	
Carrying value on the last day of current year	

Memorandum of example 1

Calculation of Depreciation and cost price and carrying value

SCHIE TRADERS

NO.1

Asset register

Percentage Depreciation: 20 % p.a. at cost price/straight line method

Details of depreciation

Details	Annual depreciation Calculations	Accumulated depreciation	Book value or known as "Carrying value"
End of first year	$80\,000 \times 20\% = 16\,000$	16 000	64 000
End of second year	$80\,000 \times 20\% = 16\,000$	32 000	(80 000 - 32 000) 48 000
End of third year	$80\,000 \times 20\% = 16\,000$	48 000	32 000
End of fourth year	$80\,000 \times 20\% = 16\,000$	64 000	16 000
End of fifth year	$80\,000 \times 20\% = 16\,000$ 15 999	(64 000 + 15 999) 79 999	(80 000 - 79 999) R1

(80 000 - 16 000)

Cannot depreciate R16 000, because of the scrap value of R1. Therefore can only depreciate R15 999

SCHIE TRADERS

NO.2

Asset register

Percentage Depreciation: 10 % p.a. at carrying value/ book value or called diminishing value

Details of depreciation

Details	Annual depreciation Calculations	Accumulated depreciation	Book value or known as "Carrying value"
Cost price R20 000			
End of first year	$20\,000 \times 10\% \times 6/12 = 1\,000$	1 000	19 000
End of second year	$19\,000 \times 10\% = 1\,900$	(2 000 + 1 900) 2 900	(20 000 - 2 900) 17 100
End of third year	$17\,100 \times 10\% = 1\,710$	4 610	15 390
End of fourth year	$15\,390 \times 10\% = 1\,539$	6 149	13 851
End of fifth year	$13\,851 \times 10\% - 1\,385,10$	7 534,10	12 465,90

Memorandum of example 2

REQUIRED:

Complete the note to the financial statements by using the given ledger accounts

Name of Company _____

BALANCE SHEET AT _____

	Notes	
ASSETS		
Non-current assets		230 000
Property, plant and equipment (at carrying value)	3	230 000

NOTES TO THE BALANCE SHEET

3. Property, plant and equipment	Vehicles
Cost Price	180 000
Accumulated Depreciation	(60 000)
Carrying value on the last day of the previous year	120 000
Movements:	
Additions at cost (150 000 + 50 000)	200 000
Disposals at carrying value (100 000 - 25 000)	(75 000)
Depreciation for the year (5 000 + 10 000)	(15 000)
Carrying value on the last day of current year	230 000
Cost Price	280 000
Accumulated Depreciation	(50 000)
Carrying value on the last day of current year	230 000

Check your answer!
These must be the same.

SCHEMATIC ILLUSTRATION OF FIXED ASSETS IN A BUSINESS									
ASSET REGISTERS					GENERAL LEDGER ACCOUNTS				
DEPRECIATION AT COST PRICE					VEHICLES				
ASSET REGISTER OF VEHICLE SOLD					ASSET REGISTER OF REMAINING VEHICLE				
Cost price: R30 000 Depreciation: 20% at Cost price					Cost price: R70 000 Accumulated depreciation: R30 000				
Date	Depreciation	Accu Depr	CV		Date	Depreciation	Accu Depr	CV	
28 Feb '10	$30\,000 \times 20\% \times 8/12 = 4000$	4 000	26 000		28 Feb '12	$70\,000 \times 20\% \times 12/12 = 14\,000$	44 000	26 000	
28 Feb '11	$30\,000 \times 20\% \times 12/12 = 6000$	10 000	20 000		28 Feb '12	$50\,000 \times 20\% \times 6/12 = 5\,000$	5 000	45 000	
1 Sept '11	$30\,000 \times 20\% \times 6/12 = 3000$	13 000	17 000						
ASSET REGISTER OF REMAINING NEW VEHICLE					ASSET REGISTER OF REMAINING NEW VEHICLE				
Cost price: R50 000 bought 6 months ago					Cost price: R50 000 bought 6 months ago				
Date	Depreciation	Accu Depr	CV		Date	Depreciation	Accu Depr	CV	
28 Feb '12	$50\,000 \times 20\% \times 6/12 = 5\,000$	5 000	45 000		28 Feb '12	$50\,000 \times 20\% \times 6/12 = 5\,000$	5 000	45 000	
DEPRECIATION AT CARRYING VALUE					DEPRECIATION				
ASSET REGISTER OF COMPUTER/EQUIPMENT					ASSET REGISTER OF REMAINING NEW VEHICLE				
Cost price: R10 000 depreciation: 20% on CV					Cost price: R50 000 bought 6 months ago				
Date	Depreciation	Accu Depr	CV		Date	Depreciation	Accu Depr	CV	
28 Feb '10	$10\,000 \times 20\% \times 12/12 = 2000$	2 000	8 000		28 Feb '12	$50\,000 \times 20\% \times 6/12 = 5\,000$	5 000	45 000	
28 Feb '11	$8\,000 \times 20\% \times 12/12 = 1600$	3 600	6 400						
28 Feb '12	$6\,400 \times 20\% \times 12/12 = 1280$	4 880	5 120						
DEPRECIATION AT CARRYING VALUE					DEPRECIATION				
ASSET REGISTER OF COMPUTER/EQUIPMENT					ASSET REGISTER OF REMAINING NEW VEHICLE				
Cost price: R10 000 depreciation: 20% on CV					Cost price: R50 000 bought 6 months ago				
Date	Depreciation	Accu Depr	CV		Date	Depreciation	Accu Depr	CV	
28 Feb '10	$10\,000 \times 20\% \times 12/12 = 2000$	2 000	8 000		28 Feb '12	$50\,000 \times 20\% \times 6/12 = 5\,000$	5 000	45 000	
28 Feb '11	$8\,000 \times 20\% \times 12/12 = 1600$	3 600	6 400						
28 Feb '12	$6\,400 \times 20\% \times 12/12 = 1280$	4 880	5 120						
DEPRECIATION AT CARRYING VALUE					DEPRECIATION				
ASSET REGISTER OF COMPUTER/EQUIPMENT					ASSET REGISTER OF REMAINING NEW VEHICLE				
Cost price: R10 000 depreciation: 20% on CV					Cost price: R50 000 bought 6 months ago				
Date	Depreciation	Accu Depr	CV		Date	Depreciation	Accu Depr	CV	
28 Feb '10	$10\,000 \times 20\% \times 12/12 = 2000$	2 000	8 000		28 Feb '12	$50\,000 \times 20\% \times 6/12 = 5\,000$	5 000	45 000	
28 Feb '11	$8\,000 \times 20\% \times 12/12 = 1600$	3 600	6 400						
28 Feb '12	$6\,400 \times 20\% \times 12/12 = 1280$	4 880	5 120						



Appendix: Past Grade 12 exam papers

The 2014 Life Sciences exams have a new format in line with CAPS. The Department of Basic Education has offered an example of the Accounting Paper, Answer Book and marking memoranda.

Use the exam paper, answer book and marking memoranda to help you prepare for your exams:

1. Before attempting the exam, **photocopy** the Answer Books so that you can use it more than once. Remember: if you want to succeed at Accounting, you must **practise, practise, practise!**
2. **Answer the questions** in the Accounting exam paper. Write your answers in the Answer Book.
3. Treat them as “real” exams by preparing yourself as if these were real exams, so have pens, pencils, an eraser and a calculator with you. **Time yourself** so you complete each paper within the 3 hours that is allocated to it.
4. This exercise is meant to test your own knowledge – so **don’t cheat** yourself by looking up the answers in the memo before you’ve finished each exam.
5. Use the memoranda to **check whether or not your answers are correct**. Note where you have got answers wrong – these are the sections of the curriculum on which you need to do more work. Go back to your textbooks and to the relevant sections of this study guide, and **spend time learning** the sections for which you got the lowest marks.
6. When you feel you have improved your knowledge in the areas you were weakest in in your first attempt, **go through each exam again**, using your photocopied Answer Books to record your answers. Check the memo again to see if you’ve improved.
7. And remember: Accounting success depends on **practise, practise, practise**. Repeat this exercise as often as you can so that you fly in your year-end exams!



**NATIONAL
SENIOR CERTIFICATE**

GRADE 12

**ACCOUNTING
EXEMPLAR 2014**

MARKS: 300

TIME: 3 hours

This question paper consists of 21 pages and an 18-page answer book.

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INSTRUCTIONS AND INFORMATION

Read the following instructions carefully and follow them precisely.

1. Answer ALL the questions.
2. A special ANSWER BOOK is provided in which to answer ALL the questions.
3. Show workings in order to achieve part-marks.
4. You may use a non-programmable calculator.
5. You may use a dark pencil or blue/black ink to answer the questions.

NOTE TO TEACHERS

This Exemplar is intended to give teachers and learners an understanding of the standard and format of questions that are regarded as valid for the Grade 12 NSC Accounting examinations (CAPS) from 2014.

Teachers are also referred to:

- The Examination Guidelines for further information on structure and standards required
- The analysis grids for evidence of compliance with weighting of content, cognitive levels and degrees of challenge

NEW CAPS CONTENT

The following questions contain new content according to the CAPS:

- QUESTION 2 covers Creditors' Reconciliation, the preparation of which is a Grade 11 topic which may be examined in Grade 12
- QUESTION 3 covers a Company Cash Budget and includes repurchase (buy-back) of shares
- QUESTION 4 focuses on repurchase (buy-back) of shares and its effect on the Balance Sheet, Notes and relevant financial indicators
- QUESTION 5 is a standard cash flow and interpretation question which includes aspects relating to repurchase (buy-back) of shares

DOUBLE TESTING

It is not desirable practice for question papers to contain 'double testing' of topics across questions. However, as the topic of repurchase (buy-back) of shares might give rise to concerns or queries from teachers regarding acceptable treatment, this topic has been repeated in several contexts in this Exemplar. Refer to the Examination Guidelines for further explanation.

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6. Use the information in the table below as a guide when answering the question paper. Try NOT to deviate from it.

QUESTION 1: 40 marks; 25 minutes	
Main topic of the question:	This question integrates:
Manufacturing	Managerial accounting Production Cost Statement Analysis and interpretation of unit costs and break-even point Managing resources Internal control and internal audit Ethics
QUESTION 2: 30 marks; 20 minutes	
Main topic of the question:	This question integrates:
Creditors' Reconciliation	Financial accounting Reconciling a Creditors' Ledger Account to a Creditors' Statement Managing resources Internal control and internal audit
QUESTION 3: 50 marks; 30 minutes	
Main topic of the question:	This question integrates:
Cash Budget	Managerial accounting Analyse and interpret a cash budget Managing resources Internal control and internal audit
QUESTION 4: 50 marks; 30 minutes	
Main topic of the question:	This question integrates:
Repurchase (buy-back) of shares	Financial accounting Shareholders' equity section of Balance Sheet and Notes Analysis and interpretation: Net asset value
QUESTION 5: 70 marks; 40 minutes	
Main topic of the question:	This question integrates:
Cash flow and interpretation of information	Financial accounting Cash Flow Statement Analysis and interpretation of financial information Independent auditor's report Internal control Ethics and professional body
QUESTION 6: 60 marks; 35 minutes	
Main topic of the question:	This question integrates:
Income Statement, fixed assets and stock	Financial accounting Preparation of Income Statement Managing resources Asset disposal account Inventory valuation: FIFO and weighted average Internal control problem-solving

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QUESTION 1: MANUFACTURING (40 marks; 25 minutes)

1.1 ACE CALCULATORS

The business produces one type of basic school calculator. The business uses the periodic inventory system.

REQUIRED:

- 1.1.1 Indicate the cost accounts that would be affected by the following in a manufacturing business:
- (a) Rent paid for factory buildings
 - (b) Overtime paid to factory workers
 - (c) Commission paid to salespersons
 - (d) Cost of raw materials used in the production
 - (e) Salary of internal auditor
- 1.1.2 Prepare the Production Cost Statement for the year ended 28 February 2013. (10)
- 1.1.3 30 000 calculators were produced during the financial year. Calculate the cost of production per unit. (3)

INFORMATION:

Information extracted from the financial records on 28 February 2013:

	R
Administration cost	485 000
Direct/Raw material cost	1 161 000
Factory overhead cost	810 000
Selling and distribution cost	245 000
Direct labour cost	?
Prime cost	1 797 000
Total cost of production of finished goods	2 460 000
Work-in-process (1 March 2012)	102 000
Work-in-process (28 February 2013)	?
Finished goods stock (1 March 2012)	202 800
Finished goods stock (28 February 2013)	500 200
Sales (26 500 calculators at R130 each)	3 445 000
Cost of sales	?

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QUESTION 2: CREDITORS' RECONCILIATION AND INTERNAL CONTROL (30 marks; 20 minutes)

Organic Traders buys and sells organic products. A statement received on 28 July 2013 from a creditor, Aqua Wholesalers, reflects a different amount owing by Organic Traders than the amount in the Creditors' Ledger of Organic Traders.

REQUIRED:

- 2.1 Make a list of the changes to Aqua Wholesalers' account in the Creditors' Ledger, which the bookkeeper should process to correct the errors or omissions. Give a brief description in the Details column and show the changes to the balances in the Amount column. (12)
- 2.2 Prepare a Creditor's Reconciliation Statement in respect of Aqua Wholesalers for July 2013. (10)
- 2.3 The owner of Organic Traders is unhappy with the errors which occurred and resulted in inaccurate records in their books. Briefly explain TWO measures that Organic Traders can implement in order to maintain good control over their creditors and to avoid this from happening in future. (4)
- 2.4 Organic Traders is experiencing cash problems and is currently in a position where they are not able to pay their creditors on time. Aqua Wholesalers has granted them a credit limit of R40 000. All their current creditors require them to pay within 30 days and they allow their customers credit terms of 60 days. Suggest TWO ways in which the liquidity position can be improved. (4)

INFORMATION:

CREDITORS' LEDGER OF ORGANIC TRADERS

CL4. AQUA WHOLESALERS			
		Debit	Credit
2013			
July 1	Balance brought forward		17 680
July 6	Cheque 6321	16 796	884
	Discount	884	NIL
July 8	Invoice 2590		17 932
July 10	Debit note 89	593	17 339
July 14	Invoice 2810		25 490
July 16	Journal Voucher 450	1 800	41 029
July 17	Debit note 102	1 482	39 457
July 19	Invoice 1067		420
July 22	Cheque 6410	18 000	11 967
July 29	Invoice 3066		32 604
			44 571

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1.2 MALOMA DAIRY

You are provided with information for the year ended 28 February 2013. This dairy is owned by Mark Maloma. The business produces flavoured milk which is sold in bottles.

INFORMATION:

The number of units produced and sold increased from 420 000 bottles in 2012 to 540 000 bottles in 2013.

The following figures apply to the 2013 financial year:

	TOTAL	PER UNIT
Sales (540 000 x R6,60)	R3 564 000	R6,60
Variable costs	R1 458 000	R2,70
Fixed costs	R972 000	R1,80

- 1.2.1 Calculate the break-even point and comment on the level of production for the year. (7)
- 1.2.2 Despite the fact that the factory workers were given a 10% wage increase, the direct material cost per unit has dropped by 50 cents per unit. What could have caused the difference? What comment would you make to Mark about the control of this item? (3)
- 1.2.3 The fixed costs per unit dropped from R1,90 in 2012 to R1,80 in 2013. Should Mark be satisfied with this? What comment would you make to Mark about the control of this item? Provide figures to support your answer. (4)
- 1.2.4 You are the internal auditor and you have noticed that the business is using bottles bought from Apex Products as containers for the flavoured milk. The contract with Apex Products was signed by the office manager, Alex Fynn. While working late one night, you noticed that Apex Products delivered a laptop to Mr Fynn. (8)
 - Will this be a concern to you? Give a reason for your answer.
 - Explain what action you would take as internal auditor. State THREE points.

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Statement received from Aqua Wholesalers:

Aqua Wholesalers			
PO Box 453; Stellenbosch 7599; Tel: 021 851 5679			
Date of statement: 25 July 2013			
Credit limit: R40 000			
Organic Traders PO Box 219 Stellenberg, 7550			
2013		Debit	Credit
			Amount
July 1	Balance brought forward		17 680
July 6	Receipt 1436		884
July 8	Invoice 2590	17 932	18 816
July 10	Credit note 1038		539
July 10	Credit note 1042		3 900
July 16	Invoice 2810	25 904	40 281
July 17	Debit note 102		1 482
July 19	Credit note 141		420
July 22	Cheque 6410		18 000
	Discount		900
			19 479

ADDITIONAL INFORMATION:

1. Aqua Wholesalers rejected the discount claimed by Organic Traders on 6 July and indicated that the payment was received too late to qualify for the discount.
2. There is a disagreement over the goods returned by Organic Traders as per debit note DN 89. The error has been made by Organic Traders. Aqua Wholesalers' credit note CN 1038 is correct.
3. Aqua Wholesalers have reflected credit note 1042 on 10 July. This, however, relates to another one of their customers, Orgo Stores, and not to Organic Traders.
4. Invoice 2810 was correctly recorded by Organic Traders.
5. Aqua Wholesalers purchased goods on credit from Organic Traders. The bookkeeper was instructed to transfer their debit balance of R1 800 in the Debtors' Ledger to the Aqua Wholesalers account in the Creditors' Ledger. However, she did the entry wrong (refer to Journal Voucher 450. Aqua Wholesalers have also forgotten to record this entry.
6. Credit note 141 for R420 received from Aqua Wholesalers was incorrectly recorded as Invoice 141 in the Creditors' Ledger.
7. Organic Traders have forgotten to claim their discount on 22 July. There was also a subtraction error of R10 000 in the Creditors' Ledger account on 22 July.
8. Note that Aqua Wholesalers' statement is prepared on 25 July 2013.

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QUESTION 3: CASH BUDGET

(50 marks; 30 minutes)

As the accountant of Blossom Traders Ltd you are reviewing the Cash Budget for the three months ending 30 September 2013, which will be presented to the directors.

REQUIRED:

- 3.1 Explain to the shareholders what the main difference is between a *projected income statement* and a *Cash Budget*. (2)
- 3.2 Name TWO items that could be included in 'other operating expenses'. (2)
- 3.3 Complete the Debtors' Collection Schedule for July and August 2013. (8)
- 3.4 Calculate the following: (3)
 - 3.4.1 The % increase in sales in September 2013
 - 3.4.2 The rent income amount for September 2013. Note that the company is budgeting for a 12% increase in rent starting 1 September 2013. (2)
 - 3.4.3 The total sales for August 2013 (4)
 - 3.4.4 The amount that will be paid to creditors during September (4)
 - 3.4.5 The amount that will be paid for interim dividends in September 2013 (4)
 - 3.4.6 What the buy-back of shares will cost the company in September 2013 (3)
 - 3.4.7 The interest that will be received for September 2013 (4)
- 3.5 In August, there is an amount that will be paid for income tax. (2)
 - 3.5.1 What does this amount represent, since the financial year-end of this company is annually at the end of February? (2)
 - 3.5.2 How will this amount be calculated? (2)
- 3.6 The shareholders are unhappy with the way the collection of debtors has been handled. (2)
 - 3.6.1 Explain why you believe the shareholders feel this way regarding the collection from debtors. (2)
 - 3.6.2 Suggest TWO measures that can be introduced to improve the situation. (2)

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3.7 At the end of June, the following figures were identified. The directors have asked that you explain to them why the budgeted and actual amounts of certain items differ significantly. Explain what you would say to them about each of the following items. Explain ONE point of advice in each case.

	JUNE 2013	
	Budgeted	Actual
Advertising	R5 200	R8 000
Training of employees	R12 000	NIL
Rent income	R8 500	R2 000

(6)

INFORMATION:

- Credit sales:** 40% of all sales are on credit. Debtors are given 30 days in which to settle their debts. However, trends over the past year reveal that debtors pay as follows:

 - 40% within the same month of sale, subject to a 5% discount
 - 35% in the month following the sale, that is 30 days
 - 20% in the second month following the sale, that is 60 days
 - 5% of debts are written off after 60 days
- Stock purchases:**

 - The business works on a fixed stock base where the stock sold in a month is replaced at the end of that month.
 - The business uses a mark-up of 60% on cost.
 - 80% of stock is purchased on credit and creditors are paid in 30 days.
- Fixed deposit:**
The business has three fixed deposits with Reliable Bank to the value of R675 000 at an interest rate of 8,0%. One of these fixed deposits, worth R375 000, matures in September.
- Shares:**

 - The company has 250 000 shares in issue and the authorised share capital has a balance of R1 500 000.
 - The company is planning on issuing a further 40 000 shares during August 2013 at a price of R10,00 per share.
 - One of the shareholders passed away earlier in the year. This shareholder owns 55 000 shares. It was decided to buy back the shares from the deceased estate during September 2013 at a price of R15,50 each.
- Dividends:**
At the end of September, an interim dividend of 40 cents per share will be paid on shares held at the end of September.

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**BLOSSOM TRADERS LTD
CASH BUDGET FOR THREE MONTHS ENDING 30 SEPTEMBER 2013**

	2013 JULY	2013 AUGUST	2013 SEPTEMBER
RECEIPTS			
Cash sales	1 200 000	1 200 000	1 440 000
Collections from debtors	?	?	804 800
Ordinary share capital (new shares)		400 000	
Rent income	8 500	8 500	?
Fixed deposit maturing			375 000
Interest on fixed deposit	4 500	4 500	?
Sundry income			?
	1 893 300	2 339 000	2 635 700
PAYMENTS			
Purchase of stock	?	?	300 000
Payments to creditors	?	?	
Directors' fees	6 000	6 000	6 000
Salaries and wages	520 000	520 000	520 000
Audit fees	7 500	7 500	7 500
Income tax		46 000	
Advertising	5 200	5 200	5 200
Dividends on ordinary shares			?
Buy-back of shares			?
Other operating expenses	?	?	?
	1 758 700	1 804 700	2 835 200
Surplus (deficit)	134 600	534 300	(199 500)
Opening bank balance	(28 000)	106 600	640 900
Closing bank balance	106 600	640 900	441 400

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**QUESTION 4: REPURCHASE OF SHARES AND INTERPRETATION
(50 marks; 30 minutes)**

You are provided with information relating to Prospect Limited for the year ended 31 March 2013. The CEO, Ronnie Phosa, together with his children, owns 150 000 shares in the company.

Where explanations or comments are required, you are required to quote figures or financial indicators to support your explanations.

REQUIRED:

- 4.1 Shareholders' equity section of the Balance Sheet on 31 March 2013. (6)
- 4.2 Notes to:
 • Ordinary share capital (13)
 • Retained income (15)
- 4.3 Calculate the net asset value per share on 31 March 2013 after the repurchase of the shares from the Gaptu family. (4)
- 4.4 The Gaptu family were keen to sell their shares because they were unhappy with the low pay-out policy that the directors were following in deciding on dividends. In your opinion, are their complaints valid, or not? Explain. (4)
- 4.5 Have the Gaptu family been offered a fair value for their shares? Explain. (3)
- 4.6 In your opinion, will the repurchase of the shares from the Gaptu family benefit the remaining shareholders, or not? Explain. (5)

INFORMATION:

- The ordinary share capital on 1 April 2012 consisted of:
 - 250 000 ordinary shares issued in the 2010 financial year at R5,00 per share
 - 150 000 ordinary shares issued in the 2011 financial year at R7,00 per share.
- Retained income on 1 April 2012 amounted to R1 960 000.
- The following changes occurred to share capital during the 2013 financial year:
 - On 1 October 2012, 100 000 new ordinary shares were issued at R9,00 per share. These shareholders are not entitled to interim dividends.
 - On 31 March 2013, the directors decided to repurchase 220 000 ordinary shares from members of the Gaptu family who were no longer interested in being shareholders. These shareholders had originally bought most of their shares on the JSE at different prices and at different times. The repurchase price was R10,70 per share. These shareholders are entitled to all dividends for the 2013 financial year.

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4. Additional information for the past two financial years:

	2013	2012
Net income after tax	R1 600 000	R2 200 000
Ordinary shareholders' equity at year-end	?	R4 260 000
Number of shares in issue at year-end	?	400 000 shares
Market price per share on the JSE	1 040 cents	1 040 cents
Net asset value per share	?	1 065 cents
Earnings per share	356,6 cents	488,9 cents
Interim dividends	70 cents	90 cents
Final dividends	102 cents	140 cents

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QUESTION 5: CASH FLOW AND INTERPRETATION (70 marks; 40 minutes)

You are provided with information relating to Bellco Limited for the year ended 31 August 2013.

- 5.1 A company's published annual report comprises five main parts.

Choose a description from COLUMN B that matches a component in COLUMN A. Write only the letter (A–E) next to the question number (5.1.1–5.1.5) in the ANSWER BOOK.

COLUMN A (Components of the annual report)	COLUMN B (Description)
5.1.1 Income Statement	A a written verbal explanation of operations of the company during a financial year
5.1.2 Balance Sheet	B reflects whether or not the shareholders can rely on the financial statements
5.1.3 Cash Flow Statement	C reflects the profit/loss of the company
5.1.4 Directors' report	D reflects the effect of the operating, financial and investing activities on the cash resources
5.1.5 Independent auditor's report	E reflects the net worth of the company

- 5.2 Complete the Cash Flow Statement for the year. Show workings in brackets. (22)
- 5.3 Calculate the following financial indicators for 2013:
- 5.3.1 Acid-test ratio (4)
- 5.3.2 % return on average shareholders' equity (4)
- 5.3.3 Debt-equity ratio (3)
- 5.3.4 % return on average capital employed (use net income before tax) (4)
- 5.4 The directors are pleased that the operating efficiency of the business has improved. Quote and explain TWO financial indicators to support their opinion. (4)

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- 5.5 According to the Companies Act (Act 61 of 1973), the directors may repurchase shares only if the liquidity of the business is acceptable. Quote and explain THREE financial indicators that provide evidence that they have complied with the Act. (6)
- 5.6 The directors want to establish another branch in a different area next year. They will need finance of R1,5 million to do this. One of the directors has suggested that they finance the expansion by increasing loans instead of issuing new shares.
- Quote and explain TWO financial indicators to support his opinion.
 - Explain TWO other factors, with advice, that the directors should consider before embarking on this expansion. (10)
- 5.7 Refer to the extract of the independent auditor's report under Information 6:
- Explain in your own words why it is necessary for the independent auditors to mention internal controls under the section on Directors' Responsibility. (2)
 - Under the section on Independent Auditor's Responsibility, they mention something about 'ethical requirements'. Give a practical example of this. (2)
 - Is their final opinion good, or not? Explain. (2)
 - Why is it necessary for the independent auditor to have the qualification CA (SA) behind his name? Explain. (2)

INFORMATION:

1. Extract from the Balance Sheet for the year ended 31 August:

	2013	2012
Fixed assets	12 138 000	12 357 000
Investments (4% p.a.)	250 000	600 000
Current assets	3 465 000	3 200 000
Trading stock	1 720 000	2 250 000
SARS (Income tax)	65 000	0
Trade and other receivables (excluding SARS)	1 140 000	940 000
Cash and cash equivalents	540 000	10 000
TOTAL ASSETS	15 853 000	16 157 000
Shareholders' equity	11 011 400	8 595 000
Share capital	8 960 000	6 360 000
Retained income	2 051 400	2 235 000
Loan from Unity Bank (11% p.a.)	3 000 000	5 400 000
Current liabilities	1 841 600	2 162 000
Trade and other payables (excluding SARS and shareholders)	920 000	1 260 000
SARS (income tax)	0	72 000
Shareholders for dividends	921 600	620 000
Bank overdraft	0	210 000
TOTAL EQUITY AND LIABILITIES	15 853 000	16 157 000

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2. Extracts from the Income Statement and Notes for the year ended 31 August 2013:

Depreciation	R1 010 000
Operating profit	3 062 000
Interest expense	462 000
Net profit before tax	2 600 000
Net profit after tax	1 820 000
Interim dividends paid	770 000
Final dividends declared	921 600

3. **Shares issued and repurchased:**
- 1 000 000 ordinary shares were in issue at the end of the previous financial year, 31 August 2012.
 - 400 000 ordinary shares were issued on 1 September 2012.
 - 120 000 ordinary shares were repurchased on 28 February 2013 from the estate of a shareholder who had died. The shares were repurchased at R2,60 above the average issue price.

4. **Changes to fixed assets:**

New vehicles and equipment were bought during the year for R880 000. Unused vehicles were sold at book value during the year.

5. **Financial indicators for the past two years:**

	2013	2012
Solvency ratio	3,3 : 1	2,1 : 1
Current ratio	1,9 : 1	1,5 : 1
Acid-test ratio	?	0,4 : 1
Turnover rate of stock	8,7 times	6,6 times
% return on average shareholders' equity	?	15,6%
Net asset value per share	860,3 cents	859,5 cents
Earnings per share	135,8 cents	114,2 cents
Dividends per share	127 cents	30 cents
Debt-equity ratio	?	0,6 : 1
% return on average capital employed	?	12,4%
% gross profit on cost of sales	62,2%	58,3%
% operating expenses on sales	37,9%	44,5%
% operating profit on sales	10,1%	7,3%

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6. Extract from the independent auditor's report. Note that this is NOT a complete report.

<p>REPORT OF THE INDEPENDENT AUDITOR</p> <p>We have audited the annual financial statements of Bellco Limited ... as set out on pages 52 to 64.</p> <p>Directors' Responsibility for the Financial Statements</p> <p>The company's directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and the requirements of the Companies Act of South Africa, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.</p> <p>Independent Auditor's Responsibility</p> <p>Our responsibility is to express an opinion on the financial statements based on our audit.</p> <p>We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.</p> <p>Opinion</p> <p>In our opinion, the annual financial statements present fairly, in all material respects, the financial position of Bellco Limited as at 31 August 2013, and its financial performance and cash flows for the 52 weeks then ended in accordance with International Financial Reporting Standards and the requirements of the Companies Act of South Africa.</p> <p>MSANE & CHARTER Director: MPJ Msane Registered Auditor; Chartered Accountant (SA) 15 September 2013</p>	<p>70</p>
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QUESTION 6: INCOME STATEMENT, FIXED ASSETS AND STOCK (60 marks; 35 minutes)

6.1 **KLOOF COMPUTERS (PTY) LTD**

You are provided with information relating to Kloof Computers (Pty) Ltd for the year ended 30 June 2013.

REQUIRED:

- 6.1.1 Refer to Adjustments and Additional Information 5. Calculate the profit/loss on the disposal of the office computers sold on 31 March 2013. (6)
- 6.1.2 Refer to Adjustments and Additional Information 6. Calculate the value of stock on hand of the:
 - Hyva laptops, according to the specific identification method (3)
 - ABX printers, according to the FIFO method (5)
 - Silvo printing paper, according to the weighted-average method (5)
- 6.1.3 Prepare the Income Statement for the year ended 30 June 2013. (32)

INFORMATION:

(a) Items extracted from the Pre-adjustment Trial Balance on 30 June 2013:

Balance Sheet accounts section	Debit	Credit
Land and buildings	930 000	
Equipment	510 100	
Accumulated depreciation on equipment		231 000
Trading stock	281 000	
Loan from Highway Lenders (13% p.a.)		300 000
SARS (provisional tax)	194 000	
Debtors' control	32 000	
Provision for bad debts		2 000
Nominal accounts section		
Sales		3 700 000
Cost of sales	2 100 000	
Staff costs (salaries, wages and commission)	180 000	
Directors' fees	120 000	
Commission income		36 000
Interest on loan	29 000	
Sundry expenses (including packing materials)	45 000	
Asset disposal		7 000

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(b) **Adjustments and additional information:**

- Commission income of R2 350 is owed to the business.
- Packing materials of R1 700 are on hand at the end of the year. Packing materials are included in Sundry expenses.
- One of the two directors has been paid his fees for 6 months. The fees were increased by 10% half-way through the financial year. Provide for fees owing. Both directors earn the same annual fees.
- Interest at 13% p.a. is owed on the loan. This interest is not capitalised. The loan was taken out several years ago. A payment of R100 000 was made on 31 December 2012. This has been properly recorded.
- Equipment comprises:

	Cost on 30 June 2013	Accumulated depreciation on 1 July 2012	Depreciation rate
General equipment	418 000	183 000	20% on diminishing-balance method
Office computers	92 100	48 000	33% on cost
	<u>R510 100</u>	<u>R231 000</u>	

NOTE: One of the office computers was sold on 31 March 2013. The selling price was credited to the Asset Disposal account but no other entry has been made. The cost price of this computer was R18 600 and the accumulated depreciation at the beginning of the year was R9 400.

Depreciation is to be written off at the rates reflected above.

- The business uses the perpetual inventory system. Stock records show:

Item	Valuation method	Stock on hand on 30 June 2013	Value on 30 June 2013
Hypa laptops	Specific Identification: R10 500 each	20 computers	?
ABX printers	FIFO	46 printers	?
Silvo printing paper	Weighted average	600 reams	?

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NOTE: Two of the Hypa laptops included in the stock figures above were donated to Bontu Primary School and Bontu High School. No entry has been made for these donations.

The following information relates to trading stock of printers and paper:

	ABX printers			Printing paper		
	Quantity	Price	Total	Quantity	Price	Total
Opening stock	20	R700	R14 000	1 200	R33	R39 600
PURCHASES	204		R153 040	5 400		R205 800
Aug. 2012	100	R730	R73 000	1 500	R40	R60 000
Jan. 2013	70	R750	R52 500	2 000	R30	R60 000
May 2013	34	R810	R27 540	1 800	R46	R82 800
SUBTOTAL	224		R187 040	6 600		R246 400
Sales	176	R1 500	R267 000	6 000	R69	R419 000
Closing stock	48		?	600		?

- The income tax assessment for the year reflected that the business owed SARS an amount of R37 000 on 30 June 2013.

6.2 **PROBLEM-SOLVING**

To try and increase the sales of laptops, the directors of Kloof Computers (Pty) Ltd decided to employ three newly qualified salespersons on a trial period for one month.

These salespersons would not be restricted to working at the shop premises. They were employed to visit potential customers who might be interested in laptops and printers.

The salespersons would each be paid the following:

- A fixed basic monthly salary of R7 000
- 10% commission on sales made by them
- A travel allowance of R2,00 per kilometre travelled in their private cars.

The business normally makes a gross profit of R6 000 per laptop (cost price R10 500, selling price R16 500). The salespersons are allowed to offer a maximum trade discount of R500 per laptop to help them secure a sale if necessary.

At the end of the one-month trial period, you are provided with the figures on the next page.

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REQUIRED:

- Explain ONE problem relating to each salesperson. Provide figures to support your explanations. (6)
- What advice would you offer the directors in respect of the plan to employ these salespersons? (3)

INFORMATION:

Name of salesperson:	GUGU	MANNY	JIM
Number of laptops drawn from stock at the beginning of the month	20	20	20
Number of laptops sold for cash	9	16	11
Number of laptops returned to stock at the end of the month	11	4	8
Discounts allowed to customers	R0	R8 000	R5 000
Cash from sales deposited by each salesperson into the bank account	R148 500	R207 000	R193 000
Gross profit earned before discounts and other expenses	R54 000	R90 000	R72 000
Basic salary	R7 000	R7 000	R7 000
Commission paid to each salesperson	R14 850	R25 200	R17 850
Travel allowance claimed (R2,00 per km)	R3 000	R1 000	R1 000

60

GRAND TOTAL: 300

1.2.4

Regarding the incident concerning the office manager, Alex Fynn:
 Will this be a concern to you? Give a reason for your answer:
 Explain what action you would take as internal auditor. State THREE points.

40

8

1.2.1

Calculate the break-even point for the year.
 Comment on the level of production for the year.

7

1.2.2

Despite the fact that the factory workers were given a 10% wage increase, the direct material cost per unit has dropped by 50 cents per unit.
 What could have caused the difference?
 What comment would you make to Mark about the control of this item?

3

1.2.3

The fixed costs per unit dropped from R1,90 in 2012 to R1,80 in 2013.
 Should Mark be satisfied with this? YES/NO
 What comment would you make to Mark about the control of this item? Provide figures to support your answer.

4

QUESTION 2

2.1 Make a list of the changes to Aqua Wholesalers' account in the Creditors' Ledger, which the bookkeeper should process to correct the errors or omissions. Give a brief description in the Details column and show the changes to the balances in the Amount column.

Details	Amount
Pre-adjustment balance in Creditors' Ledger	
Correct balance	

12

2.2 Creditor's Reconciliation Statement of Aqua Wholesalers on 31 July 2013

Details	Amount
Balance per statement received from Aqua Wholesalers	
Correct balance	

10

2.3 The owner of Organic Traders is unhappy with the errors which occurred and resulted in inaccurate records in their books. Briefly explain TWO measures that Organic Traders can implement in order to maintain good control over their creditors and to avoid this from happening in future.

4

2.4 Organic Traders is experiencing cash problems and is currently in a position where they are not able to pay their creditors on time. Aqua Wholesalers has granted them a credit limit of R40 000. All their current creditors require them to pay within 30 days and they allow their customers credit terms of 60 days. Suggest TWO ways in which the liquidity position can be improved.

4

30

QUESTION 3

3.1 Explain to the shareholders what the main difference is between a projected income statement and a Cash Budget.

2

3.2 Name TWO items that could be included in 'other operating expenses'.

2

3.3 Debtors' Collection Schedule for July and August 2013

	Credit sales	July collections	August collections
May	R660 000		
June	R680 000		
July	R800 000		
August	R800 000		
TOTAL			

8

3.4.1 Calculate the % increase in sales in September 2013.

3

3.4.2 Calculate the rent income amount for September 2013. Note that the company is budgeting for a 12% increase in rent starting 1 September 2013.

2

3.4.3 Calculate the total sales for August 2013.

4

3.4.4 Calculate the amount that will be paid to creditors during September.

4

3.4.5 Calculate the amount that will be paid for interim dividends in September 2013.

4

3.4.6 Calculate what the buy-back of shares will cost the company in September 2013.

3

3.4.7 Calculate the interest that will be received for September 2013.

4

QUESTION 5

5.1.1	
5.1.2	
5.1.3	
5.1.4	
5.1.5	

5

5.1

**5.2 BELLCO LIMITED
CASH FLOW STATEMENT FOR THE YEAR ENDED 31 AUGUST 2013**

Cash effects of operating activities	1 293 000
Cash generated from operations	4 062 000
Interest paid	(462 000)
Cash effects of investing activities	
Cash effects of financing activities	
Net change in cash & cash equivalents	
Cash & cash equivalents at beginning of year	
Cash & cash equivalents at end of year	540 000

22

5.2

4.4 In your opinion, are the complaints by the Gaptu family about the dividends valid, or not? Explain.

4

4.4

4.5 Have the Gaptu family been offered a fair value for their shares? Explain.

3

4.5

4.6 In your opinion, will the repurchase of the shares from the Gaptu family benefit the remaining shareholders, or not? Explain.

5

4.6

50

5.5 According to the Companies Act (Act 61 of 1973), the directors may repurchase shares only if the liquidity of the business is acceptable. Quote and explain THREE financial indicators that provide evidence that they have complied with the Act.

6

5.6 One of the directors has suggested that they finance the expansion by increasing loans instead of issuing new shares. Quote and explain TWO financial indicators to support his opinion.

10

Factor	Advice

5.3.1 Calculation of acid-test ratio

4

5.3.2 Calculation of % return on average shareholders' equity

4

5.3.3 Calculation of debt-equity ratio

3

5.3.4 Calculation of % return on average capital employed (use net income before tax)

4

5.4 The directors are pleased that the operating efficiency of the business has improved. Quote and explain TWO financial indicators to support their opinion.

4

5.7

Explain in your own words why it is necessary for the independent auditors to mention internal controls under the section on Directors' Responsibility.

Under the section on Independent Auditor's Responsibility, they mention something about 'ethical requirements'. Give a practical example of this.

Is their final opinion a good one or not? Explain.

Why is it necessary for the Independent Auditor to have the qualification CA (SA) behind him name? Explain.

70

8

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QUESTION 6

6.1.1 **Calculate the profit/loss on the disposal of the office computers sold on 31 March 2013.**

6

6.1.2 **Calculate the value of stock on hand of the:**
Hypa laptops, according to the specific identification method:

ABX Printers, according to the FIFO method:

Silvo printing paper, according to the weighted-average method:

13

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basic education
 Department:
 Basic Education
REPUBLIC OF SOUTH AFRICA



**NATIONAL
 SENIOR CERTIFICATE**

GRADE 12

**ACCOUNTING
 EXEMPLAR 2014
 MEMORANDUM**

MARKS: 300

- MARKING PRINCIPLES:**
- Penalties for foreign items are applied only if the candidate is not using marks elsewhere in the question for that item (no foreign item penalty for misapplied mark). No double penalty applied.
 - Full marks for correct answer. If the answer is incorrect, mark the workings provided.
 - If a pre-adjustment figure is shown as a final figure, allocate the part-mark for the working for that figure (not the method mark for the answer).
 - Unless otherwise indicated, the positive or negative effect of any figure must be considered to award the mark. If no + or - sign or bracket is provided, assume that the figure is positive.
 - Where indicated, part-marks may be awarded to differentiate between differing qualities of answers from candidates.
 - Where penalties are applied, the marks for that section of the question cannot be a final negative.
 - Where method marks are awarded for operation, the marker must inspect the reasonableness of the answer before awarding the mark.
 - In awarding method marks, ensure that candidates do not get full marks for any item that is incorrect at least in part.
 - Codes: F = foreign item; p = placement/presentation.

This memorandum consists of 13 pages.

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QUESTION 1

1.1.1 Indicate the cost accounts that would be affected by the following in a manufacturing business:

	Details:	Cost account affected:
(a)	Rent paid for factory buildings	Factory overhead
(b)	Overtime paid to factory workers	Direct labour
(c)	Commission paid to salespersons	Selling and distribution
(d)	Cost of raw materials used in the production	Direct/prime materials
(e)	Salary of internal auditor	Administration

5

1.1.2 **ACE CALCULATORS**
 Production Cost Statement for the year ended 28 February 2013

Direct material cost	✓ 1 161 000
Direct labour cost	✓✓ 636 000
Prime cost	✓ 1 797 000
Factory overhead cost	✓ 810 000
Total production costs	✓ 2 607 000
Work-in-process at beginning of year	✓ 102 000
	✓ 2 709 000
Work-in-process at end of year	Check operative
	✓ 249 000
Cost of production of finished goods	✓ 2 460 000

Foreign items -1 (max -2)

10

1.1.3 Calculate the cost of production per unit.

✓ R2 460 000 ÷ 30 000 units = R82.00 per unit ✓

3

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1.2.1

Calculate the break-even point for the year.

$$\begin{array}{r} \checkmark\checkmark \\ 572\,000 \\ 5,60 - 2,70 \\ \hline = 249\,230 \text{ or } 249\,231 \\ 3,80 \\ \checkmark\checkmark \end{array}$$

Comment on the level of production for the year.

Compare figures of BEP to production (one mark); Comment (one mark)

The level of production (540 000 bottles) greatly exceeds the break-even point (249 230) ✓. The owners should be satisfied as this means that the business will be earning a very good profit. ✓

7

1.2.2

Despite the fact that the factory workers were given a 10% wage increase, the direct material cost per unit has dropped by 50 cents per unit.

What could have caused the difference?

The workers are operating very efficiently, possibly because Mark has motivated them with an increase which exceeds the inflation rate/probably because he has trained them well ✓ One mark for *partial/complete answer*

What comment would you make to Mark about the control of this item?

This is very good. They should aim to maintain the control over this item by continued monitoring and training if necessary. ✓

3

1.2.3

The fixed costs per unit dropped from R1,90 in 2012 to R1,80 in 2013.

Should Mark be satisfied with this? NO ✓

What comment would you make to Mark about the control of this item? Provide figures to support your answer.

Total fixed costs have increased by R174 000.
In 2012 fixed costs were: 420 000 x R1,90 = R798 000 ✓
In 2013 fixed costs were: 540 000 x R1,80 = R972 000 ✓
He must investigate the reasons for the difference (R174 000). ✓

Four answer for 1 mark
He should be happy because fixed costs have declined by 10 cents per unit.

4

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Regarding the incident concerning the office manager, Alex Fynn:

Will this be a concern to you? Yes

Give a reason for your answer:

It appears that Alex Fynn might have taken a bribe from Apex Products, which is unethical. ✓✓

Explain what action you would take as internal auditor. State THREE points.

- Expected responses: ✓✓ ✓✓ Two marks per valid point
- Investigate whether Mr Fynn had the authority to sign the contract whether the contract went out to tender (whether the business' procurement policies were adhered to and what the prices of other bottle suppliers are).
 - Question Mr Fynn on the acceptance of the laptop and if a suitable explanation is not provided, report the facts to the owner of the business for possible disciplinary sanction of Mr Fynn.
 - If any internal control procedures are deficient, rectify these immediately and ensure that fair tenders are applied in future.

8

40

2.3

The owner of Organic Traders is unhappy with the errors which occurred and resulted in inaccurate records in their books. Briefly explain TWO measures that Organic Traders can implement in order to maintain good control over their creditors and to avoid this from happening in future.

Any TWO valid measures ✓✓ ✓✓ ✓✓

- Division of duties: The duty performed by one employee serves as a check on another employee, e.g. the person doing the payments is not the same person recording the entries or ordering the stock
- Accurate documentation: Ensure that all documents are correctly recorded and check recording against source document
- Continue doing regular reconciliations to creditors' statements. This process is intended as a control measure to pick up errors such as this.

4

2.4

Organic Traders is experiencing cash problems and is currently in a position where they are not able to pay their creditors on time. Aqua Wholesalers has granted them a credit limit of R40 000. All their current creditors require them to pay within 30 days and they allow their customers credit terms of 60 days. Suggest TWO ways in which the liquidity position can be improved.

TWO valid points ✓✓ ✓✓

- He needs to negotiate longer terms with his creditors.
- Find other suppliers who allow longer credit terms.
- Negotiate a higher credit limit with his suppliers.
- Encourage customers to pay sooner, e.g. discounts on prompt payments.

4

30

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QUESTION 2

2.1

Make a list of the changes to Aqua Wholesalers' account in the Creditors' Ledger, which the bookkeeper should process to correct the errors or omissions. Give a brief description in the Details column and show the changes to the balances in the Amount column.

Details	Amount
Pre-adjustment balance in Creditors' Ledger	✓ # 44 571
Discount cancelled	✓✓ 884
Correction of Debit note 89	✓✓ 54
Correction of Invoice 141	✓✓ (840)
Discount on 22 July	✓✓ (900)
Correction of subtraction error	✓✓ # 10 000
Correct balance	<input checked="" type="checkbox"/> 53 769

R10 000 could be added to the opening balance (i.e. R54 571 for 3 marks).

12

2.2

Creditor's Reconciliation Statement of Aqua Wholesalers on 31 July 2013

Details	Amount
Balance per statement received from Aqua Wholesalers	✓ 19 479
Correction of CN1042	✓✓ 3 900
Correction of Invoice 2810	✓✓ (414)
Transfer of balance (JV450)	✓✓ (1 800)
Invoice 3056	✓✓ 32 604
Correct balance	<input checked="" type="checkbox"/> 53 769

10

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QUESTION 3

3.1 Explain to the shareholders what the main difference is between a projected income statement and a Cash Budget.

Explanation of projected income statement ✓

- The projected income statement projects the profits and losses.
- The projected income statement projects future expenses and income.

Explanation of Cash Budget ✓

- The Cash Budget projects future cash surplus or deficit.
- The Cash Budget projects future receipts and payments.

2

3.2 Name TWO items that could be included in 'other operating expenses'.

Any TWO valid items ✓ ✓

Possible answers:

- Packing material
- Stationery
- Printing
- Rates
- Electricity and water
- Telephone

2

3.3 Debtors' Collection Schedule for July and August 2013

	Credit sales	July collections	August collections
May	R660 000	✓ 132 000	
June	R680 000	✓ 238 000	✓ 136 000
July	R800 000	✓ 304 000	✓ 280 000
August	R800 000	£ same as above	£ 304 000
TOTAL	Operation both months	£ 674 000	720 000

8

3.4.1 Calculate the % increase in sales in September 2013.

$$\frac{240\,000}{1\,200\,000} \times 100 = 20\% \quad \text{Operation one part correct}$$

3

3.4.2 Calculate the net income amount for September 2013. Note that the company is budgeting for a 12% increase in rent starting 1 September 2013.

$$8\,500 + 12\% = R9\,520 \quad \checkmark \checkmark$$

2

3.4.3 Calculate the total sales for August 2013.

$$1\,200\,000 \checkmark + 60 \checkmark \times 100 \checkmark = R2\,000\,000 \quad \text{Operation one part correct}$$

4

3.4.4 Calculate the amount that will be paid to creditors during September.

$$2\,000\,000 \times 100 \times 80\% = R1\,600\,000 \quad \text{Operation one part correct}$$

4

3.4.5 Calculate the amount that will be paid for interim dividends in September 2013.

$$235\,000 \checkmark \times 40 \checkmark \text{ cents} = R94\,000 \quad \text{Operation one part correct}$$

4

3.4.6 Calculate what the buy-back of shares will cost the company in September 2013.

$$55\,000 \checkmark \times R15.50 \checkmark = R852\,500 \quad \text{Operation one part correct}$$

3

3.4.7 Calculate the interest that will be received for September 2013.

$$300\,000 \checkmark \times 0\% \checkmark = 12 \checkmark = R2\,000 \quad \text{Operation one part correct}$$

4

QUESTION 4

**4.1 PROSPECT LIMITED
EXTRACT FROM THE BALANCE SHEET ON 31 MARCH 2013**

	Note	See notes 7 & 8
Shareholders' equity ✓		R 3 816 000
Ordinary share capital ✓	7.	R 1 792 000
Retained income ✓	8.	R 1 824 000

6

3.5.1

What does this amount represent, since the financial year-end of this company is annually at the end of February?
A provisional tax payment. ✓✓

2

3.5.2

How will this amount be calculated?
It will be calculated on the profits projected in the projected income statement. ✓✓

2

4.2 NOTES TO THE FINANCIAL STATEMENTS

Note 7. ORDINARY SHARE CAPITAL ISSUED

✓ 400 000 ordinary shares in issue at beginning of year (1 250 000 ÷ 3,125)	✓ 2 300 000
✓ 100 000 ordinary shares issued during year at R9,00 each	✓ 900 000
✓ 220 000 shares repurchased (R6,40 ÷ average price)	R (1 408 000)
✓ 280 000 ordinary shares in issue at end of year	R 1 792 000

13

3.6.1

Explain why you believe the shareholders feel this way regarding the collection from debtors.
Explanation ✓✓
The credit terms of the company is 30 days, yet only 75% of all debtors are paying within this time.

2

3.6.2

Suggest TWO measures that can be introduced to improve the situation.
TWO measures ✓ ✓
• Change interest on overdue accounts
• Offer bigger discount for prompt payment
• Send regular reminders

2

Note 8. RETAINED INCOME

Balance at beginning of year	✓ 1 960 000
✓ Net profit after tax	✓ 1 600 000
✓ Repurchase of 220 000 shares (at R4,30 above average price)	R (946 000)
✓ Dividends for year	(790 000)
Interim (400 000 ÷ 3 × 70c ✓)	✓ 280 000
Final (500 000 ÷ 3 × 102c ✓)	✓ 510 000
Balance at end of year	Check operation R 1 824 000

15

3.7

Explain what you would say to the directors about each of the following items. Explain ONE point of advice in each case.

	COMMENT TO DIRECTORS ✓ ✓ ✓ ✓	ADVICE ✓ ✓ ✓ ✓
Advertising	The expense is much higher than the budgeted amount.	They should stick to the budgeted amount or consider different advertising techniques.
Training of employees	The budgeted amount has not been used.	Training is an important aspect of any company and should be used.
Rent Income	Significantly under budget (actual less than budget)/Budget was unrealistically high.	Investigate shortfall, e.g. poor collection, tenant has left, etc. to rectify this problem/attempt to sign debit orders/appoint a rent collector/charge interest on slow payers.

6

4.3

Net asset value per share on 31 March 2013 after the repurchase of shares

See 4.1	See 4.2	Operation, one part correct ✓
R 3 816 000	- 280 000 shares = 1291,4 cents or R12,91	

4

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5.3.1 Calculation of acid-test ratio

✓✓

$$\frac{1\ 745\ 000}{1\ 841\ 600} = 0,9 : 1$$
 ✓
 Operation, one part correct ✓

4

5.3.2 Calculation of % return on average shareholders' equity

✓

$$\frac{1\ 520\ 000}{\frac{1}{2}(11\ 011\ 400 + 8\ 595\ 000)} \times \frac{100}{1} = 18,6\%$$
 ✓✓
 Operation, one part correct ✓

4

5.3.3 Calculation of debt-equity ratio

✓

$$\frac{3\ 000\ 000}{11\ 011\ 400} = 0,3 : 1$$
 ✓
 Operation, one part correct ✓

3

5.3.4 Calculation of % return on average capital employed (use net income before tax)

✓

$$\frac{3\ 062\ 000}{\frac{1}{2}(14\ 011\ 400 + 13\ 985\ 000)} \times \frac{100}{1} = 21,9\%$$
 ✓✓
 Operation, one part correct ✓

4

5.4 The directors are pleased that the operating efficiency of the business has improved. Quote and explain TWO financial indicators to support their opinion.

Good answers = 2 marks each; partial = 1 mark; incorrect = 0.
 Operating expenses on sales have decreased from 44,5% to 37,9% which indicates better control of expenses. ✓✓
 Operating profit on sales has increased from 7,3% to 10,1% because, apart from the better control over expenses, there has been a slightly higher mark-up % applied as well. ✓✓

4

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5.5 According to the Companies Act (Act 61 of 1973), the directors may repurchase shares only if the liquidity of the business is acceptable. Quote and explain THREE financial indicators that provide evidence that they have complied with the Act.

Good answers = 2 marks each; partial = 1 mark; incorrect = 0.
 Current ratio improved from 0,4 : 1 to 1,9 : 1, which indicates that current liabilities are well covered by current assets. ✓✓
 Acid-test ratio improved from 0,4 : 1 to 0,9 : 1, which indicates that liquid assets (excluding stock) are almost equal to current liabilities. ✓✓
 The bank balance improved from an overdraft of R210 000 to a positive balance of R540 000. ✓✓

6

5.6 One of the directors has suggested that they finance the expansion by increasing loans instead of issuing new shares. Quote and explain TWO financial indicators to support his opinion.

Good answers = 2 marks each; partial = 1 mark; incorrect = 0.
 The debt-equity ratio has decreased from 0,6 : 1 to a very safe 0,3 : 1. If they increase the loans by R1,5m, the debt-equity ratio will still be much lower than it was in 2012 (i.e. 0,4 : 1). ✓✓
 The % return on total capital employed is 21,9% compared to the interest on loans of 11%. This indicates that profits can be geared up by using loans. ✓✓
 Explain TWO other factors, with advice, that the directors should consider before embarking on this expansion.
 Any TWO valid suggestions, e.g.

Factor	Advice
Demand for their products in the other areas ✓✓	Undertake market research, e.g. a survey ✓
The level of efficiency by employees at the new branch ✓✓	Ensure proper training is conducted ✓

10

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5.7

Explain in your own words why it is necessary for the independent auditors to mention internal controls under the section on Directors' Responsibility.

Good answers = 2 marks each; partial = 1 mark; incorrect = 0.

The internal control system must be properly in place in order to prevent errors and fraud and to ensure that the information that comes out of the bookkeeping system is reliable. Directors run the company so they are responsible for this. ✓✓

Under the section on Independent Auditor's Responsibility, they mention something about 'ethical requirements'. Give a practical example of this.

Any valid response, e.g. no conflict of interests (cannot be a shareholder and an auditor; cannot perform other services for the company); due diligence in carrying out the audit. ✓✓

Is their final opinion a good one or not? Explain.

Yes. This is an unqualified audit report. If there was a problem, it would have been mentioned. ✓✓

Why is it necessary for the Independent Auditor to have the qualification CA (SA) behind his name? Explain.

To assure readers that the auditor is well trained and educated, is well informed on the latest audit processes and the law, is bound by the SA/ICA code of conduct and could face disciplinary sanction if he is negligent. ✓✓

70

8

QUESTION 6

6.1.1 Calculate the profit/loss on the disposal of the office computers sold on 31 March 2013.

Depreciation for current year = $33\frac{1}{3}\% \times 18\ 000 \times 9/12 = R4\ 650$ ✓✓
 Accumulated depreciation = $R9\ 400 + R4\ 650 = R14\ 050$ ✓
 Cost price = $R18\ 000$ ✓
 Net book value at date of sale = $R4\ 550$ ✓
 Selling price = $R7\ 000$ ✓
 Profit = $R2\ 450$ ✓

6

6.1.2 Calculate the value of stock on hand of the:

Hypa laptops, according to the specific identification method:

✓ ✓
 $18 \times R10\ 500 = R189\ 000$

ABX Printers, according to the FIFO method:

✓ ✓ ✓ ✓
 $(34 \times R3\ 101) + (12 \times R750) = R36\ 540$
 $27\ 540$ ✓

Silvo printing paper, according to the weighted-average method:

✓ ✓ ✓ ✓
 $\frac{246\ 400}{5\ 800} \times \frac{600}{1} = R22\ 400$
 $5\ 800$ ✓✓

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6.1.3 KLOOF COMPUTERS (PTY) LTD
Income Statement for the year ended 30 June 2013

Sales		3 700 000
Cost of sales		(2 100 000)
Gross profit		1 600 000
Other income	✓ Check operation	£ 40 800
Commission income	(35 000 ✓ + 2 350 ✓)	✓ 38 350
Profit on disposal of asset		£ 2 450
	5	
		1 640 800
Operating expenses	✓ Check operation	£ (836 510)
Staff costs		180 000
Directors fees	(2 ✓ x (120 000 + 132 000) ✓)	✓ 504 000
Sundry expenses	(45 000 ✓ – 1 700 ✓)	✓ 43 300
Depreciation	(47 000 ✓ ✓ + 24 500 ✓ ✓ + 4 650)	66 150
Trading stock deficit	(281 000 ✓ – 21 000 ✓ – 247 940)	£ 12 060
Donations	(2 x 10 050)	✓ 21 000
	20	
Operating profit	✓ Check operation	£ 804 280
Interest on loan	(29 000 + 16 500) One part correct	£ 45 500
Net profit before tax		758 780
Income tax	(194 000 ✓ + 37 000 ✓)	✓ (231 000)
Net profit after tax	✓ Check operation	£ 527 880
	8	
		32

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6.2

Explain ONE problem relating to each salesperson. Provide figures to support your explanations.

	Explanation of problem (with figure(s))
GUGU	✓ Explanation of problem ✓ Figure(s) She has not sold many laptops (only 9). Her travelling is high (three times that of the others).
MANNY	✓ Explanation of problem ✓ Figure(s) He has offered a lot of discounts (R15 000). Cash missing = R21 500.
JIM	✓ Explanation of problem ✓ Figure(s) He has installed 2 laptops (cost price R10 500 x 2).

What advice would you offer the directors in respect of the plan to employ these salespersons?

Any valid conclusion ✓✓ One mark for points/impacts answer
Expected responses:

- Employ Gugu permanently because she made the biggest net profit after deducting all expenses (R35 150), but keep her travelling under control.
- Do not employ Manny or Jim as they each appear to have stolen cash and laptops worth more than R20 000 and are probably dishonest.
- Continue the plan to employ travelling salespersons on a commission basis as this will increase sales in future and will enable the business to enlarge its customer base.

60

GRAND TOTAL: 300

3



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