COMPANY FINANCIAL STATEMENTS 7 MARCH 2013

Lesson Description

In this lesson we

- Examine the changes made to the format of an Income Statement and Balance Sheet of a company.
- Recap on GAAP principles.
- Focus on year-end adjustments which affect the financial statements.

Key Concepts

Income Statement

Definition

- The Income Statement will show the trading result i.e. has the business made a net profit or a loss for a specific accounting period (which is normally 1 year)
- Includes all income and expense accounts for a specific period (1 year)

Format

SALES (subtract debtors allowance)		
COST OF SALES		
GROSS PROFIT		
OTHER OPERATING INCOME		
GROSS OPERATING INCOME		
OPERATING EXPENSES		
OPERATING PROFIT		
Interest income	1	
OPERATING PROFIT BEFORE INTEREST EXPENSE		
Interest expense	2	
PROFIT BEFORE TAXATION		
Income Tax		
NET PROFIT FOR THE YEAR	9	

Balance Sheet

Definition

- A statement of the financial position of the business on a specified date.
- i.e. **A = OE + L**

ASSETS		
Non-current assets		
Tangible assets	3	
Financial assets		
Current assets		
Inventory	4	
Trade and other receivables	5	
Cash and cash equivalent	6	
Total Assets		
EQUITY AND LIABILITIES		
Ordinary shareholders equity		
Ordinary share capital	7	
Share Premium	8	
Retained income	9	
Non-current liabilities		
Mortgage loan		
Current liabilities		
Trade and other payables	10	
Bank overdraft		
Short-term loan *		
Total equity and laibilities		

*may be added to trade and other payables

Changes to the Notes (to the Financial Statements)

(Changes are in red)

Trade and Other Receivables (Note 5)

Trade debtors	Xx
Provision for bad debts	(xx)
Net trade debtors	XX
Accrued income	Xx
Prepaid expense	Xx
SARS (income tax) (DR balance i.e. if the receiver is owing the business)	xx

Ordinary Share Capital (Note 7)

Authorised	
Xxx ordinary shares @ Rxx each	Xx
Issued	
Xxx shares at Rxx each issued at the beginning of the year	Xx
Xxx shares at Rxx each issued during the year	X
Xxx shares at Rxx each issued at the end of the year	Xxx

Share Premium (Note 8)

Balance at the beginning of the financial year	Xxx
Xx shares issued during the year @ a premium of xx each	Xx
Balance at the end of the financial year	XX

Retained Income (Note 9)

Retained income @ beginning of the year	Xx
Net profit after tax	Xx
Ordinary share dividend	(xx)
Paid	X
Recommended	X

Trade and Other Payables (Note 10)

Trade creditors	Xx
Accrued expense	Xx
Income received in advance	Xx
Sars (paye)	Xx
Sars Iincome tax)	Xx
Shareholders for dividends	xx
Pension fund	Xx
UIF	xx

Generally Accepted Accounting Practice (GAAP)

Most important principles are:

MATCHING (Income Statement)

All income and expenses must be matched to the same period in which they incurred. (regardless of whether the income has been received or not; or the expense has been paid or not paid)

PRUDENCE (Balance Sheet)

Financial results are reported in a conservative manner.

Historical Cost (Balance Sheet)

The general rule is that assets are valued at their historical cost. Land and Buildings and trading stock will be shown in the balance sheet at the original cost to the business. There are however exceptions, (trading stock that is de-valued)

Questions

Question 1

You are provided with an extract of the pre-adjustment trial balance, adjustments and additional information of RK Ltd, on 29 February 2008. The business buys and sells office equipment. Stock is sold at a mark-up of 60% on cost.

Instructions

a.) Prepare the following **notes** to the Balance Sheet:
- i. Inventory (5)
- ii. Retained Income (5)
- iii. Trade and other Payables (8)

b.) Prepare the **Income Statement** for the year ended 29 February 2008 (62)

Information

RK LTD EXTRACT OF PRE-ADJUSTMENT TRIAL BALANCE ON 29 FEBRUARY 2008

Ordinary share capital (par value R2 each)	850 000
Ordinary Share Premium	41 200
Retained Income	**52 500**
Loan: XYZ Bank	110 000
Vehicles	162 000
Equipment	43 000
Accumulated depreciation on vehicles	51 200
Accumulated depreciation on equipment	38 450
Trading Stock	81 300
Debtors control	78 100
Provision for bad debts	4 100
Sars (income tax) (provisional payments)	63 420
Bank (DR)	35 539
Creditors control	**6 350**
Pension Fund	**590**
SARS (PAYE)	**340**
Sales	**797 500**
Cost of sales	**335 900**
Debtors allowance	**8 000**
Salary and wages	**180 000**
Pension fund contribution	**13 700**
Medical aid contribution	**13 111**
Sundry expenses	**620**
Packing materials	**5 600**
Rent income	**22 000**
Audit fees	**8 000**
Directors fees	**52 000**
Ordinary share dividend	**12 000**
Insurance	**11 040**
Bad debts	**1 350**
Interest on current account	**400**
Stationery	**4 200**
Interest on loan	**10 350**

Adjustment and Additional Information:

1. Rent has been received for 11 months only.

2. Included in insurance is an amount of R2 400 paid for the period 1 January 2008 to 30 June 2008.

3. Packing materials **used** during the current financial year amounted to R4 000.

4. No entry has been made for stock returned by a debtor on 25 February 2008, selling price R1 400.

5. A fire in one of the stock rooms caused R2 000 worth of damage to stock during February 2008. The insurance company has agreed to pay 75% of the loss in March 2008. The bookkeeper did not know how to record this transaction therefore no entries have been made in the books of the business.

6. A physical stock count on 29 February 2008 revealed the following stock on hand:

Trading stock	R78 500
Stationery	R420

7. Stock costing R1 000 was donated to a children's home **AFTER** stock taking was completed.

8. The bookkeeper posted the salaries journal to the General ledger on the 29 February 2008. However, she forgot to take into account that a 10% increase had been granted to S.Sithole as from 1 February 2008. The following details are applicable:
   S.Sithole earned a gross monthly salary of R9 000 on 31 January 2008.
   - 8% of his gross monthly salary is deducted for the pension fund.
   - PAYE amounts to 20% of his gross salary.
   - His increase won't affect his medical aid contributions.
   - The business contributes R1,50 for every R1 contributed by its employees to the Pension Fund.

9. A debtor whose account was written off as irrecoverable during December 2007, paid his outstanding debt of R750. No entry has been made.

10. A debtor owing R500 was declared insolvent. The business received 25c in the rand, which was recorded. No entry however was made for the bad debt.

11. Provision for bad debts must be decreased by R200.

12. Depreciation for the year is calculated as
    - Equipment R4 549
    - Vehicles R21 200
    - Note: A vehicle with a cost price of R40 000 and accumulated depreciation on date of sale R16 000 was sold to one of the directors on 1 January 2008 for R22 000 cash. The accountant forgot to record profit/loss on sale of asset.

13. Income Tax for the year amounts to R69 608.

14. A final dividend of 8c per share was declared on 29 February 2008.