### ACCOUNTING

#### Syllabus overview

**6.1 The purpose of accounting**
- Understand and explain the difference between book-keeping and accounting
- State the purposes of measuring business profit and loss
- Explain the role of accounting in providing information for monitoring progress and decision-making

**6.2 Sources and recording of data**

**6.2.1 The double entry system of book-keeping**
- Explain the meaning of assets, liabilities and owner’s equity
- Explain and apply the accounting equation
- Outline the double entry system of book-keeping
- Process accounting data using the double entry system
- Recognise the division of the ledger into the sales ledger, the purchases ledger and the nominal (general ledger)

**6.2.2 Business documents**
- Recognise and understand the following business documents: invoice, credit note, debit note, statement of account
- Complete proforma business documents
- Understand the use of business documents as sources of information

Candidates do **not** need to know about document details

**6.2.3 Books of prime (original) entry**
- Explain the advantage of using various books of prime entry
- Explain the use of, and process, accounting data in the books of prime (original) entry – cash book, petty cash book, sales journal, purchases journal, sales returns journal, purchases returns journal and the general journal
- Post the ledger entries from the books of prime (original) entry
- Distinguish between and account for trade discount and cash discounts
- Explain the dual function of the cash book as a book of prime (original) entry and as a ledger account for bank and cash
- Explain and apply the imprest system of petty cash

**6.2.4 The ledger**
- Prepare ledger accounts
- Post transactions to the ledger accounts
- Balance ledger accounts as required and make transfers to final accounts
- Interpret ledger accounts and their balances

Candidates do **not** need to explain or use folio columns
### 6.3 Verification of accounting records

#### 6.3.1 The trial balance
- Understand that a trial balance is a statement of ledger balances on a particular date
- Outline the uses and limitations of a trial balance
- Prepare a trial balance from a given list of balances and amend a trial balance which contains errors
- Identify and explain those errors which do not affect the trial balance – commission, compensating, complete reversal, omission, original entry, principle

#### 6.3.2 Correction of errors
- Correct errors by means of journal entries
- Correct errors by means of suspense accounts
- Adjust the profit or loss for an accounting period after the correction of errors
- Understand the effect of correction of errors on a statement of financial position

#### 6.3.3 Bank reconciliation
- Understand the use and purpose of a bank statement
- Update the cash book for bank charges, bank interest paid and received, correction of errors, credit transfers, direct debits, dividends, and standing orders
- Understand the purpose of, and prepare, a bank reconciliation statement to include bank errors, uncredited deposits and unpresented cheques

#### 6.3.4 Control accounts
- Understand the purposes of purchases ledger and sales ledger control accounts
- Identify the books of prime (original) entry as sources of information for the control account entries
- Prepare purchases ledger and sales ledger control accounts to include credit purchases and sales, receipts and payments, cash discounts, returns, bad debts, dishonoured cheques, interest on overdue accounts, contra entries, refunds, opening and closing balances (debit and credit within each account)

### 6.4 Accounting procedures

#### 6.4.1 Capital and revenue expenditure and receipts
- Distinguish between and account for capital expenditure and revenue expenditure
- Distinguish between and account for capital receipts and revenue receipts
- Calculate and comment on the effect on profit of incorrect treatment
- Calculate and comment on the effect on asset valuations of incorrect treatment

#### 6.4.2 Accounting for depreciation and disposal of non-current assets
- Define depreciation
- Explain the reasons for accounting for depreciation
- Name and describe the straight line (equal instalment), reducing (diminishing) balance and revaluation methods of depreciation
- Prepare ledger accounts and journal entries for the provision of depreciation
- Prepare ledger accounts and journal entries to record the sale of non-current assets, including the use of disposal accounts

#### 6.4.3 Other payables and other receivables
- Recognise the importance of matching costs and revenues
- Prepare ledger accounts and journal entries to record accrued and prepaid expenses
- Prepare ledger accounts and journal entries to record accrued and prepaid incomes
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| 6.4.4 Bad debts and provision for doubtful debts | - Understand the meaning of bad debts and bad debts recovered  
- Prepare ledger accounts and journal entries to record bad debts written off  
- Prepare ledger accounts and journal entries to record bad debts recovered  
- Explain the reasons for maintaining a provision for doubtful debts  
- Prepare ledger accounts and journal entries to record the creation of, and adjustments to, a provision for doubtful debts |
| 6.4.5 Valuation of inventory | - Understand the basis of the valuation of inventory at the lower of cost and net realisable value  
- Prepare simple inventory valuation statements |
| 6.5 Principles of financial statements |  |
| 6.5.1 Income statements | - Calculate the gross profit and profit for the year based on accounting principles, for a specified period  
- Recognise that profit for the year is the increase in the net assets during that period |
| 6.5.2 Statements of financial position | - Recognise that they are statements of balances of assets and liabilities on a specified date  
- Recognise and define non-current assets (fixed assets), intangible assets, current assets, current liabilities, non-current liabilities, working capital, capital employed and capital owned  
- Comment on the inter-relationship of statements of financial position items |
| 6.6 Preparation of financial statements |  |
| 6.6.1 Sole traders | - Explain the difference between a trading business and a service business  
- Prepare income statements and statements of financial position for trading businesses  
- Prepare income statements and statements of financial position for service businesses  
- Make adjustments for provision for depreciation using the straight line (equal instalment), diminishing (reducing) balance and revaluation methods  
- Make adjustments for accrued and prepaid expenses and accrued and prepaid income  
- Make adjustments for bad debts and provisions for doubtful debts  
- Make adjustments for goods taken by the owner for own use |
| 6.6.2 Partnerships | - Explain the advantages and disadvantages of forming a partnership  
- Outline the importance and contents of a partnership agreement  
- Explain the purpose of an appropriation account  
- Prepare income statements, appropriation accounts and statements of financial position  
- Show the treatment of interest on partners’ loans, interest on capital, interest on drawings, partners’ salaries and the division of the balance of profit or loss  
- Make adjustments to financial statements as detailed in 6.6.1  
- Explain the uses of, and differences between, capital and current accounts  
- Draw up partners’ capital and current accounts in ledger account form and as part of a statement of financial position presentation |

There will be no questions on the admission of a new partner or on the dissolution of a partnership.
### 6.6.3 Limited liability companies
- Understand the meaning of the term limited liability
- Prepare simple appropriation accounts
- Understand and distinguish between called-up and paid-up share capital
- Understand and distinguish between share capital (preference shares and ordinary shares) and loan capital (debentures)
- Understand the capital structure of a limited company comprising preference share capital, ordinary share capital, general reserve and retained earnings
- Prepare statements of changes in equity
- Prepare statements of financial position

Candidates do **not** need to know about cumulative and non-cumulative preference shares, deferred and founders’ shares, participating shares, redeemable shares, rights issues, share premium or capital redemption reserve.

Candidates do **not** need to record the issue of shares, make entries for corporation tax, or know about the accounting requirements of the Companies Acts.

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### 6.4.4 Clubs and societies
- Distinguish between receipts and payments accounts and income and expenditure accounts
- Prepare receipts and payments accounts
- Prepare accounts for revenue-generating activities, e.g. refreshments, subscriptions
- Prepare income and expenditure accounts and statements of financial position
- Make adjustments as detailed in 6.6.1 as appropriate
- Calculate the accumulated fund

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### 6.6.5 Manufacturing accounts
- Distinguish between direct and indirect costs
- Distinguish between direct material, direct labour, prime cost and factory overheads
- Understand and make adjustments for work in progress
- Calculate factory cost of production
- Prepare manufacturing financial statements: income statements and statements of financial position
- Make adjustments to financial statements as detailed in 6.6.1

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### 6.6.6 Incomplete records
- Prepare opening and closing statements of affairs
- Calculate net profit or loss from changes in capital over time
- Calculate sales, purchases, gross profit, trade receivables and trade payables and other figures from incomplete information
- Prepare income statements and statements of financial position
- Make adjustments to financial statements as detailed in 6.6.1
- Apply the techniques of mark-up, margin and inventory turnover to arrive at missing figures

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6.7 Analysis and interpretation

6.7.1 Summary of commonly used ratios

1. Profitability ratios

(i) Percentage of gross profit to sales (gross profit margin) = \( \frac{\text{Gross Profit}}{\text{Revenue}} \times 100 \)

Mark up = \( \frac{\text{Gross Profit}}{\text{Cost of Sales}} \)

(ii) Percentage of profit to revenue (net profit margin) = \( \frac{\text{Profit for the Year}}{\text{Revenue}} \times 100 \)

(iii) Return on Capital Employed (ROCE) = \( \frac{\text{Profit for the Year}}{\text{Capital Employed}} \times 100 \)

[Capital Employed = Owner’s capital + long term liabilities]

2. Liquidity

(i) Current ratio = \( \frac{\text{Current Assets}}{\text{Current Liabilities}} \) (also known as working capital ratio)

(ii) Quick Ratio = \( \frac{\text{Current Assets} - \text{Inventory}}{\text{Current Liabilities}} \) (also known as ‘Acid Test’ or ‘Liquid ratio’)

(iii) Trade Receivables Collection Period = \( \frac{\text{Trade Receivable}}{\text{Credit Sales}} \times 365 \text{ days} \)

(iv) Trade Payables Payment Period = \( \frac{\text{Trade Payables}}{\text{Credit Purchases}} \times 365 \text{ days} \)

(v) Rate of Inventory Turnover = \( \frac{\text{Cost of Goods Sold}}{\text{Average Inventory}} \) (answer given in times)

Or Inventory Turnover = \( \frac{\text{Average Inventory}}{\text{Cost of Goods Sold}} \times 365 \text{ days} \)

6.7.2 Interpretation of accounting ratios

• Prepare and comment on simple statements showing comparison of results for different years
• Make recommendations and suggestions for improving profitability and working capital
• Understand the significance of the difference between the gross profit percentage and the percentage of profit to revenue as an indicator of a business’s efficiency

6.7.3 Inter-firm comparison

• Understand the problems of inter-firm comparison due to factors such as differing accounting policies
• Apply accounting ratios to inter-firm comparison

6.7.4 Interested parties

Discuss the uses of accounting by the following interested parties for decision-making:

• owners
• managers
• trade payables
• bank
• investors
• club members
• other interested parties such as governments, tax authorities, etc.
### 6.7.5 Limitations of accounting statements
Recognise the limitations of accounting statements due to such factors as:
- historic cost
- difficulties of definition
- non-financial aspects

### 6.8 Accounting principles and policies

#### 6.8.1 Accounting principles
Show understanding of the following accounting principles:
- **accruals (matching):** understand that costs must be matched against related income
- **business entity and ownership:** know that a distinction is made between the financial transactions of a business and those of its owner(s)
- **consistency:** understand that the same accounting treatment should be applied to similar items at all times
- **duality:** understand the two-fold aspect of every transaction
- **going concern:** understand that accounting assumes that a business will continue to operate indefinitely
- **money measurement:** know that transactions must be expressed in monetary terms
- **prudence:** know that profit should not be overstated by ignoring foreseeable losses or that revenue should not be recorded before it is earned
- **realisation:** know that revenue is recognised as being earned when legal liability to pay is incurred by the customer (i.e. when ownership of goods passes to the customer)

#### 6.8.2 Accounting policies
- Recognise the influence of international accounting standards and understand the following objectives in selecting accounting policies:
  - **comparability:** recognise that a financial report can only be compared with reports for other periods if similarities and differences can be identified
  - **relevance:** understand that financial information is relevant only if it affects the business decisions
  - **reliability:** understand that financial information is reliable only if it can be depended upon to represent actual events and is free from error and bias
  - **understandability:** recognise that a financial report must be capable of being understood by the users of that report

There will be no questions on specific international standards.