IGCSE Accounting Sole Trader

1 Rani is a sole trader. On 31 December 2013 her statement of financial position was as follows.

Rani
Statement of Financial Position at 31 December 2013

	$	$
Non-current assets		
Fixtures and fittings (at book value)		12 000
Current assets		
Inventory		6 380
Trade receivables	1 200	
Provision for doubtful debts	(36)	
		1 164
Bank		110
		7 654
Total assets		19 654
Capital		18 454
Current liabilities		
Trade payables		910
Other payables		290
		1 200
Total liabilities		19 654

At the end of December 2014 the book-keeper ran away and it was found that no detailed records had been kept. The following information, however, was available for the year ended 31 December 2014.

1 Fixtures and fittings are depreciated at 20% per annum on the net book value. No fixtures or fittings had been bought during the year.

2 A delivery van costing $15 000 had been bought during the year. It was to be depreciated at the rate of 40% a year on the reducing (diminishing) balance basis. A full year's depreciation is to be provided in the year of purchase.

3 The provision for doubtful debts is to stay at the same percentage.

4 Other assets and liabilities at 31 December 2014 were as follows.

	$	
Inventory	8340	
Trade receivables (before provision)	1600	
Bank	90	debit
Trade payables	1100	
Accrued electricity	190	
Accrued wages	230	

5 Drawings amounted to $11 600.

REQUIRED

(a) Calculate the net assets of the business at 31 December 2014.

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Answer:

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Fixtures and fittings	12 000 – 2 400	*9 600*
Motor vehicle	*15 000 × 0.6*	*9 000*
Inventory		*8 340*
Trade receivables	*1 600 – 48*	*1 552*
Bank		*90*
Trade payables		*(1 100)*
Other payables	*190 + 230*	*(420)*
Net assets		*27 062*

(b) **(i)** Calculate the change in net assets between 31 December 2013 and 31 December 2014.

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Answer:

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Closing net assets	*27 062*
Opening net assets	*(18 454)*
Change	*8608*

(ii) State why the change in net assets was not equal to the profit for the year.

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Answer: *Drawings are included. Change in net assets is adjusted by the drawings to arrive at net profit.*

Rani wants to know more about the performance of her business.

REQUIRED

(c) State two ratios Rani could calculate from a detailed income statement to help her achieve this.

1 ....

2 ....

Answer: *Gross profit margin*
Net profit margin
Inventory turnover

Rani is concerned about the increase in the level of inventory and is considering a different basis of valuation.

REQUIRED

(d) Explain how the following accounting principles are applied to the valuation of inventory.

1 Prudence ....

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2 Realisation ....

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Answer: *Prudence – a business should not overstate profits/assets and so should value inventory at the lower of cost and net realisable value.*

Realisation – a business should not account for profit until it is realised and should use cost price rather than selling price for inventory valuation.

2 Nzita is a sole trader. His statement of financial position at 31 January 2014 included the following balances.

	$	
Trade receivables	700	
Trade payables	400	
Inventory	1 100	
Equipment at cost	15 700	
Provision for depreciation of equipment	4 100	
Prepaid rent	250	
Bank	2 100	debit

REQUIRED

(a) Calculate Nzita's capital at 31 January 2014.

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Answer:

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Trade receivables	*700*
Trade payables	*(400)*
Inventory	*1 100*
Equipment at cost	*15 700*
Provision for depreciation of equipment	*(4 100)*
Prepaid rent	*250*
Bank	*2 100*
Capital	*15 350*

A summary of Nzita's bank statements showed the following for the year ended 31 January 2015.

	$
Receipts from customers	28 900
Payments to suppliers	12 600
Wages	5 200
Rent	3 100
Purchase of new equipment	1 100
Sundry expenses	2 650
Drawings	6 600

Further information is as follows.

1 Nzita depreciates his non-current assets at the rate of 10% per annum on the straight line basis. A full year's depreciation is provided in the year of purchase.

2 No non-current assets were disposed of during the year.

3 Proper books of account were not kept during the year but Nzita provided the following information at 31 January 2015.

	$
Trade receivables	900
Trade payables	650
Inventory	1400
Prepaid rent	150

4 All sales and purchases were made on credit.

REQUIRED

(b) Prepare the following accounts for the year ended 31 January 2015 to determine the sales and purchases for the year.

Nzita
Total trade receivables account

Date	Details	$	Date	Details	$
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Nzita
Total trade payables account

Date	Details	$	Date	Details	$
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Answer:

Nzita
Total trade receivables account

2014		$	2015		$
Feb 1	*Balance b/d*	*700*	*Jan 31*	*Bank/Cash*	*28 900*
2015				*Balance c/d*	*900*
Jan 31	*Sales*	*29 100*			
		29 800			*29 800*
2015					
Feb 1	*Balance b/d*	*900*			

Nzita
Total trade payables account

2015		$	2014		$
Jan 31	*Bank/Cash*	*12 600*	*Feb 1*	*Balance b/d*	*400*
	Balance c/d	*650*	*2015*		
			Jan 31	*Purchases*	*12 850*
		13 250			*13 250*
			2015		
			Feb 1	*Balance b/d*	*650*

(c) Prepare Nzita's income statement for the year ended 31 January 2015.

Nzita
Income Statement for the year ended 31 January 2015

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Answer:

Nzita
Income Statement for the year ended 31 January 2015

		$	$
Sales/Revenue			*29 100*
Inventory 1 Feb 2014		*1 100*	
Purchases		*12 850*	
		13 950	
Inventory 31 January 2015		*1 400*	
Cost of sales			*12 550*
Gross profit			*16 550*
Rent	*3100 + (250–150)*	*3 200*	
Wages		*5 200*	
Sundry expenses		*2 650*	
Depreciation of equipment		*1 680*	
			12 730
Profit for the year			*3 820*

(d) Prepare an extract from Nzita's statement of financial position at 31 January 2015 showing the capital section.

Nzita
Statement of Financial Position (extract) at 31 January 2015

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Answer:

Nzita
Statement of Financial Position (extract) at 31 January 2015

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Capital at 1 Feb 2014	*15 350*
Profit for the year	*3 820*
	19 170
Drawings	*6 600*
Capital at 31 January 2015	*12 570*

(e) Calculate, to two decimal places, Nzita's gross profit margin for the year.

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Answer: *16 550/29100 × 100 = 56.87%*

(f) Suggest two reasons why Nzita's gross profit margin was lower than in the previous year.

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Answer: *Lower selling prices*
Introduction of trade discount
Sales promotions
Higher purchases prices not passed on to customers
Change in mix of goods sold
Higher cost of sales

4 A trader provided the following information about a non-current asset.

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cost	12 000
accumulated depreciation at start of year	1 800
method of depreciation	reducing (diminishing) balance at 15% per annum

What was the accumulated depreciation at the end of the year?

A $1530

B $3330

C $3600

D $8670

Answer: *B. $3330*

5 The non-current assets of a sole trader increased.

What might have caused this to happen?

A a decrease in the bank overdraft

B an increase in trade receivables

C the charging of depreciation

D the introduction of capital by the owner

Answer: *D. the introduction of capital by the owner*

6 Siegfried is a sole trader who does not maintain a complete set of double entry records. He has provided the following information.

	1 January 2017	31 December 2017
	$	$
Equipment at cost	18 000	18 000
Inventory	2 415	2 934
Trade receivables	1 930	2 042
Trade payables	1 210	1 455
Bank	–	209
Bank overdraft	835	–
Accrued expenses	–	98
Prepaid rent	–	120
Capital	20 300	?

On 31 December 2017, Siegfried brought his own motor vehicle into the business, valued at $5500. He decided to write off trade receivables, $100, and to start depreciating equipment by 20% per annum.

REQUIRED

(a) Calculate Siegfried's capital at 31 December 2017 after making the necessary adjustments.

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Answer:

Assets	*$*	*$*
Equipment	*(18 000 – 3 600)*	*14 400*
Motor vehicle		*5 500*
Inventory		*2 934*
Other receivables		*120*
Trade receivables	*(2 042 – 100)*	*1 942*
Bank		*209*
		25 105
Liabilities		
Trade payables	*1 495*	
Other payables	*98*	*1 553*
Capital at 31 December 2017		*23 552*

During the year ended 31 December 2017, Siegfried's cash drawings were $2700.

REQUIRED

(b) Calculate the profit made by Siegfried for the year ended 31 December 2017.

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Answer:

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Opening capital	*20 300*
Add: Capital introduced	*5 500*
	25 800
Less: Drawings	*(2 700)*
	23 100
Less: closing capital	*(23 552)*
Profit for the year	*452*

Alternative presentation

Date	Details	$	Date	Details	$
2017			*2017*		
Dec 31	*Drawings*	*2 700*	*Jan 1*	*Balance b/d*	*20 300*
	Balance c/d	*23 552*	*Dec 31*	*Motor vehicle*	*5 500*
				Profit of the year	*452*
		26 252			*26 252*

(c) State what is measured by the return on capital employed (ROCE).

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(d) State the formula for the calculation of the ROCE.

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(e) Calculate Siegfried's return on capital employed for the year ended 31 December 2017. Use the opening capital in your calculation which should be correct to two decimal places.

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Answer: *(c)* *It shows the profit earned for each $100 used in the business*
Or
It shows how efficiently the capital is being employed
Profit received as a % of capital employed

(d) $\frac{\textit{Profit (for the year)}}{\textit{Capital employed}} \times \frac{100}{1}$

(e) $\frac{452\ \textbf{OF}}{20\,300} \times \frac{100}{1} = 2.23\%$

Siegfried knows that he sold the same number of units and had applied the same mark-up in the year ended 31 December 2017 as he did in the previous year, but made a lower profit for the year.

REQUIRED

(f) Suggest one reason why Siegfried made a lower profit for the year for the year ended 31 December 2017 than the previous year.

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(g) State three benefits to Siegfried of maintaining a full set of double entry records.

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Answer: *(f)* *Siegfried started charging depreciation on non-current assets*
Siegfried wrote off more bad debts this year
Increase in other expenses
Decrease in other income

(g) *Easier/quicker/used to prepare financial statements/calculate profit*
Helps to check accuracy/arithmetic errors or detect/locate errors
Helps to prevent fraud
Easy reference
Balances are more easily available
More detail available in income statement
Easier to calculate accounting ratios/measure performance
Cheaper accountancy fees
Maintains the principle of duality