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# ACCOUNTING FUNDAMENTALS

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ASSESSMENT A 1



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***Income statement for 31. December 2021 for Wales plc***

| <b><i>Particulars</i></b>                      | <b><i>Amount (£)</i></b> |
|------------------------------------------------|--------------------------|
| <i>Revenue</i>                                 | <i>800 980</i>           |
| <i>Less: Cost of goods sold</i>                | <i>(578 650)</i>         |
| <b><i>Gross Profit</i></b>                     | <b><i>222 330</i></b>    |
| <i>Other income</i>                            | <i>0</i>                 |
| <b><i>Total other income</i></b>               | <b><i>0</i></b>          |
| <i>Administrative expenses</i>                 | <i>(30 000)</i>          |
| <i>Director's remuneration</i>                 | <i>(5 000)</i>           |
| <i>Distribution cost</i>                       | <i>(28 000)</i>          |
| <i>Dividend Paid (preference and ordinary)</i> | <i>(50 000)</i>          |
| <i>sales commission</i>                        | <i>(3 000)</i>           |
| <b><i>Operating cost</i></b>                   | <b><i>106 330</i></b>    |
| <i>Interest paid</i>                           | <i>(2 000)</i>           |
| <i>Profit before tax</i>                       | <b><i>104 330</i></b>    |
| <i>corporate taxation</i>                      | <i>(100 000)</i>         |
| <b><i>Profit for the year</i></b>              | <b><i>4 330</i></b>      |

## Statement of financial position for 31st Dec 2021 for Wales plc

| <i>Particulars</i>                  | <i>Amount (£)</i> |
|-------------------------------------|-------------------|
| <b>Assets</b>                       |                   |
| <b>Non-Current Assets</b>           |                   |
| Plant and Equipment                 | 632 730           |
| Stock                               | 330600            |
| <b>Total Non-Current Assets</b>     | <b>963 330</b>    |
| <b>Current Assets:</b>              |                   |
| Cash and bank                       | 76 250            |
| Closing Inventory                   |                   |
| Trade Receivables                   | 171 105           |
| <b>Total Current Assets</b>         | <b>247 355</b>    |
| <b>Total Assets</b>                 | <b>1 210 685</b>  |
| <b>Liabilities</b>                  |                   |
| <b>Current Liabilities:</b>         |                   |
| Trade payables                      | 171355            |
| Accrual Commission                  | 3000              |
| Accrual Corporate tax               | 100000            |
| Long term liability:                |                   |
| <b>Total Current Liabilities</b>    | <b>274 355</b>    |
|                                     |                   |
| <b>Non-Current Liabilities</b>      |                   |
| <b>Total Liabilities</b>            | <b>274355</b>     |
| <b>Net Assets</b>                   |                   |
| Shareholders' Equity:               |                   |
| £1 ordinary shares                  | 400 000           |
| 10% £1 preference shares            | 300 000           |
| Retained Profit                     | 136 330           |
| 4% Debentures                       | 100 000           |
| <b>Total Share capital</b>          | <b>936 330</b>    |
| <b>Total Liabilities and Equity</b> | <b>1 210 685</b>  |

b)

The balance sheet is a snapshot of the company's activities, its financial and financial condition. It is a business card of the company's management showing the results of the management decisions taken and implemented by it for the past, which has already passed a period. The balance sheet has a tabular form and consists of two interrelated parts: assets and liabilities. (Horner, 2013)

It is accepted in the asset of the balance sheet to describe the assets, i.e. the resources, the funds that the enterprise has and uses in carrying out the activity. In fact, the asset contains information characterizing the economic content of the entire set of assets that the enterprise uses and expects to benefit.

The liabilities of the balance sheet describe the capital of the enterprise, ie it contains information about the origin of the available used assets, what are the sources of formation of these assets. This information essentially shows the relationship of ownership of the enterprise to the owners of capital and in particular to the sources of equity, on the one hand, and, on the other hand, to the owners of foreign, borrowed capital, i.e. liabilities, liabilities of the enterprise. The total assets and liabilities of the balance sheet must be equal. This equality is determined by the fact that the assets and liabilities of the balance sheet reflect the same mass of assets, expressed in value, but from two different in their economic content groups: once - in composition and embodiment and the second time - in origin and affiliation. (Horner, 2013)

In fact, the balance sheet reflects not only the total amount of assets and capital of the enterprise at a given time. The data in the balance sheet practically reveals the structure of the assets and their sources of formation, acquisition, by types and groups, the relative share of each group, as well as the relationship and interdependence between them. In practice, the data in the balance sheet are used to calculate a number of indicators that characterize the activities carried out during the day, such as profitability.

The grouping of the assets and capital of the enterprise in the balance sheet is performed in sections, groups and balance sheet items.

The sections of the balance sheet contain summary information on the state of assets and capital according to their economic classification.

The groups are part of the sections of the balance sheet and in this sense, they contain more detailed information about the individual groups of assets and capital.

Balance sheet items, also called balance sheet items, are the smallest structural unit of the balance sheet, which shows the state of individual assets and capital at the time of compiling the balance sheet.

## Question 2

1

| Ratio                             | Formula                                                   | 2021          | 2020         |
|-----------------------------------|-----------------------------------------------------------|---------------|--------------|
| <b>Return on capital employed</b> | <b><i>Profit before interest/Assets employed*100%</i></b> | <b>11,14%</b> | <b>9,93%</b> |
| <b>ROCE</b>                       | <i>Operating profit</i>                                   | 805           | 699          |
|                                   | <i>total assets less than total current liabilities</i>   | 7 225         | 7 041        |

A return on capital employed ratio (ROCE) can help to determine a company's profit margin and capital efficiency. In other words, this ratio can reveal how efficiently a company is using its capital to generate profit. (CFC, 2022)

2.

|                         |                                                                 |            |            |
|-------------------------|-----------------------------------------------------------------|------------|------------|
| <b>Return on equity</b> | <b><i>Earnings/Ordinary share capital and reserves*100%</i></b> | <b>14%</b> | <b>13%</b> |
| <b>ROE</b>              | <i>Net Profit</i>                                               | 431        | 366        |

|  |               |       |       |
|--|---------------|-------|-------|
|  | <i>Equity</i> | 3 088 | 2 912 |
|--|---------------|-------|-------|

Accordingly, the return on equity in 2021 was higher, indicating growth in the firm's net income and the efficacy of its investments. (CFC, 2022)

3.

| <b>Earning Per share</b> | <b><i>Income/ Outstanding shareholders</i></b>  | <b>0,72</b> | <b>0,61</b> |
|--------------------------|-------------------------------------------------|-------------|-------------|
|                          | <i>Net Profit ( earnings)</i>                   | 431         | 366         |
|                          | <i>Ordinary share capital ( 50p per shares)</i> | 600         | 600         |

Divided by the number of outstanding shares of a company's common stock, earnings per share (EPS) represents the company's profitability.

Consequently, Sweet Plc's earnings per share in 2020 were 0.61, which increased to 0.72 in 2021, which indicates that the people in this company have seen a greater return on their investment. (CFC, 2022)

4.

| <b>Net profit Margin</b> | <b><i>Net Income / Sales*100</i></b> | <b>6,40%</b> | <b>5,68%</b> |
|--------------------------|--------------------------------------|--------------|--------------|
|                          | <i>Net Income</i>                    | 431          | 366          |
|                          | <i>Sales</i>                         | 6 738        | 6 441        |

A company's net profit margin can show how much of every dollar it collected in revenue translates into profits. As a result, the company reduced its operating expenses in 2021 along with boosting sales revenues. This, in turn, improved the organization's profit margin. (CFI, 2022)

5.

| <b>Asset turnover</b> | <b><i>Turnover/ Assets employed*100</i></b> | <b>93%</b> | <b>91%</b> |
|-----------------------|---------------------------------------------|------------|------------|
|                       | <i>Revenue</i>                              | 6 738      | 6 441      |
|                       | <i>Total Assets</i>                         | 7 225      | 7 041      |

Asset turnover ratio is an indicator of how effectively a company makes use of resources to generate revenue. A higher asset turnover ratio indicates a company's efficiency in generating revenue.

6.

| <b>Stock holding days</b> | <b><i>Inventory / Cost of sales *365</i></b> | <b>80 d</b> | <b>78 d</b> |
|---------------------------|----------------------------------------------|-------------|-------------|
|                           | <i>Inventory</i>                             | 708         | 659         |
|                           | <i>Cost of Goods Sold</i>                    | 3 235       | 3 096       |

In order for managers to measure liquidity, they will look at the inventory holding period. It measures whether a business can manage its assets and how quickly they can convert them into cash or income. (CFI, 2022)

7.

| <b>Debtors collection period</b> | <b><i>Trade receivable / Sales *365</i></b> | <b>68 d</b> | <b>73 d</b> |
|----------------------------------|---------------------------------------------|-------------|-------------|
|                                  | <i>Trade receivable</i>                     | 1 249       | 1 287       |
|                                  | <i>Credit of Sales</i>                      | 6 738       | 6 441       |

A shorter period of time indicates that an organization is becoming more efficient at collecting trade debts. In other words, the term debtor collection period is used in accounting for the average time taken to collect trade debts. (KAGAN, 2022)

8.

| <b>Current ratio</b> | <b><i>Current assets/Current liabilities</i></b> | <b>0,92:1</b> | <b>0,77:1</b> |
|----------------------|--------------------------------------------------|---------------|---------------|
|                      | <i>Current Assets</i>                            | 2 303         | 2 355         |
|                      | <i>Current Liabilities</i>                       | 2 511         | 3 046         |

An investment or analyst can use the current ratio to determine how a company can best maximize its current assets to pay its current liabilities and other paya

bles by maximizing its current assets on its balance sheet. The current ratio measures a company's ability to pay short-term obligations or those due within a year.

9.

| <b>Gearing ratio</b> | <b><i>(Debt/Debt+ Equity)*100</i></b>       | <b>57%</b> | <b>59%</b> |
|----------------------|---------------------------------------------|------------|------------|
|                      | <i>Debt(non current liabilities)</i>        | 4 137      | 4 129      |
|                      | <i>Debt(non current liabilities)+equity</i> | 7 225      | 7 041      |

Gearing measures how much debt is owed by a company as compared to its equity. The ratios can indicate how much financial risk a company faces, since too much debt can cause difficulties.

10.

| <b>Interest cover</b> | <b><i>Profit befor interest/Interest charges</i></b> | <b>3,56</b> | <b>3,86</b> |
|-----------------------|------------------------------------------------------|-------------|-------------|
|                       | <i>Profit before interest</i>                        | 805         | 699         |
|                       | <i>Interest</i>                                      | 226         | 181         |

It helps determine whether a company is generating enough profit from its operations to meet its debt obligations. When it is less than 1, it is not generating enough profit to meet its obligations.

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