The Institute of Chartered Accountants in England and Wales

Accounting

Supplement to Learning Materials

For exams up to 31 July 2016

Supplement

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Accounting
The Institute of Chartered Accountants in England and Wales

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The content of this publication is intended to prepare students for the ICAEW examinations, and should not be used as professional advice.

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Introduction

Why we have provided an Accounting supplement

ICAEW is committed to providing the highest standard of learning materials to enable you to prepare for your exams. This supplement has been produced to incorporate resources that we wish to make available to you.

This supplement, as well as sample papers, webinars and other resources, can be accessed on the Accounting exam resources page of the ICAEW website, accessible via www.icaew.com/dashboard.

What the Accounting supplement covers

After receiving feedback from your fellow students, tutors and employers, a glossary of terms has been produced to aid in your understanding of the subject, as well as an extra scenario-based question to prepare for your exam.

Within this supplement you will find:

- **Clarifications and notified errata**
  Notes on updates within the Accounting learning materials (as of August 2015) which should be taken into account when using the Accounting study manual and question bank.

  The errata sheet can also be found on the Accounting exam resource pages of the ICAEW website, accessible via www.icaew.com/dashboard.

- **Scenario-based question**
  Adding to the existing scenario-based questions already available within the question bank, this additional question gives another chance to prepare for this type of question which will feature within your Accounting assessment.

- **Glossary of terms**
  This explains and clarifies terms that you may not have come across before starting your studies with ICAEW.

- **Mock exam guidance notes**
  These notes give you the information you need to create your own mock exams using the Accounting question bank.

How the Accounting supplement should be used

The Accounting supplement should be used by students who are preparing for and sitting the ICAEW Accounting assessment from 1 January to 31 July 2016. It is designed to be used in conjunction with the Accounting study manual and question bank for exams up to 31 July 2016, and should not be used in isolation.

Clarifications

Study manual

Chapter 2	The accounting equation
Page 53	**Worked example: Preparing a statement of profit or loss** Instead of 'Profit for the year', line 14 should read 'Profit for the period'.

Chapter 9	Inventories
Page 244	**Interactive question 6** The final part of the question should read, "…and four members are known to be in arrears at 30 June 20X7." **The following line should be added to the requirement:** Note: The Drones Club decided that from 1 July 20X6 they would no longer accept any part payment of subscriptions. This did not affect the collection of arrears.

Chapter 11	The nature of a limited company

Dividends clarification

Section 3

Page 297

The following note is a clarification on the calculation of dividends which you may be asked to complete in your Accounting assessment.

Equity dividends:

The dividend to be paid to the shareholders is decided by the board of directors. The dividend rate can be expressed in a number of different ways.

E.g. 1

It can be quoted in terms of the pence amount each share receives, for example, the equity share information may appear in the trial balance as follows:

	£	£
Ordinary share capital (£1 per share)		400,000

The company paid an equity dividend of 5p per share .

This means that the dividend paid amounts to £20,000. This is calculated by multiplying 400,000 shares by 5p.

Nominal value of shares

The nominal value of a share is an arbitrary value given to that unit. It is a base value, which does not change and therefore it differs from the market value of the share. If the market value of a share is higher than its nominal value, the difference is accounted for in the share premium account.

It is very important, therefore, that you note the nominal value of the share, as this will affect the number of shares in issue, and therefore your calculation of dividends and bonus issues. £1 is the most common nominal value but it can be more or less than this.

- If the nominal value of shares is £1, and the value of the ordinary share capital account is £500,000, that means there are 500,000 ordinary shares in issue (£500,000 ÷ £1).
- If the nominal value of the shares was £2, and the value of the ordinary share capital account was £500,000, that means there are 250,000 ordinary shares in issue (£500,000 ÷ £2).

- If the nominal value of shares is 50p, and the value of the ordinary share capital account is £500,000, that means there are 1,000,000 ordinary shares in issue (£500,000 ÷ £0.50).

E.g. 2

If the nominal value of the share was 50p, and the value of the equity share capital remained at £400,000 (from e.g. 1), the trial balance would appear as follows:

	£	£
Ordinary share capital (50p per share)		400,000

The payment of an equity dividend of 5p per share dividend would now result in a total dividend of £40,000. This is because there are actually 800,000 50p shares in issue.

Preference dividends:

A company may also issue preference shares, which entitle the holders to a dividend out of profits

(preference dividend) before the equity (ordinary) shareholders are entitled to any equity dividend.

Difference between redeemable and irredeemable preference shares:

- Only preference shares which the company is not entitled to buy back or redeem at some stage in the future, known as irredeemable preference shares, are treated as share capital.
- Preference shares which the company is entitled to buy back from its shareholders or 'redeem' at some future time are called redeemable preference shares, and are treated as non-current liabilities (debt capital).

Unlike the equity shares (where there is no entitlement to a set amount of dividend), preference shares are often expressed as follows:

	£	£
7% £1 irredeemable preference shares		100,000

This means that the preference dividend to be paid will be £7,000. (£100,000 × 7%)

Calculating the dividends from retained earnings:

Retained earnings comprise the income (profits and gains less losses) that the company retains within the business, i.e. income that has not been paid out as dividends or transferred to any other reserve.

In some cases, you may be expected to calculate the dividends paid during the period without any information regarding the dividend rate to be paid. Instead, you need to understand the composition of the retained earnings account.

E.g. 3

Question:

The retained earnings of a company at 1 January 20X5 was £800,000. The retained earnings at 31 December 20X5 is £1,140,000. The profit for the year is £370,000. What was the total dividend paid during the year?

Answer:

The total dividend paid during the year is £30,000

Working:

RETAINED EARNINGS

	£		£
Dividends (bal. fig.)	**30,000**	B/fwd	800,000
C/fwd	1,140,000	Profit for the year	370,000
	1,170,000		1,170,000

Calculating the dividends from retained earnings where there has been a bonus issue during the year:

Note: In an exam, you should assume that a company uses the share premium account as fully as it can before using retained earnings, unless told otherwise.

Therefore, if there is no share premium account, or you are specifically told to use the retained earnings account for the issue of bonus shares, you should understand how this transaction will affect the calculation of dividends from the retained earnings account.

E.g. 4

Question: Using the information from e.g. 3, suppose that the company held £100,000 equity shares of £1 each. During the year the company decided to make a 1 for 10 bonus issue of shares from the retained earnings account. Calculate the dividends paid during the year.

Answer:

The total dividend paid during the year is £20,000

Working:

SHARE CAPITAL

	£		£
		B/fwd	100,000
C/fwd	110,000	Bonus issue	10,000
	110,000		110,000

RETAINED EARNINGS

	£		£
Bonus issue	10,000	B/fwd	800,000
Dividends (bal. fig.)	**20,000**	Profit for the year	370,000
C/fwd	1,140,000		
	1,170,000		1,170,000

Chapter 11	Limited company financial statements
General allowances	Some questions contain an adjustment for general allowances for receivables, e.g. adjustment number 4 in question 1 Hexham Ltd, to provide an allowance for doubtful debts of 5% of remaining receivables. The method used in the chapter on irrecoverable debts and allowances of the study manual (chapter 8) is to provide for specific allowances, i.e. provide an allowance for a doubtful debt of $1,500 owed by X Ltd. It is more likely that a specific allowance (second example) will be examined, however, students should be able to handle both methods in the exam.
Pro-forma (question)	The pro-formas as given in questions 1, 3, 4, 5, 6 and 7 are missing the following additional lines: **Missing line** — **Question** Provisions — 1, 4, 5, 6, 7. Dividends payable — 1, 7. Deferred income — 3
Pro-forma (solution)	You should report trade receivables and trade payables separately from prepayments and accruals in your exam. They have been incorrectly combined in the following questions: **Error** — **Question** Trade receivables combined with prepayments — 7 Trade payables combined with accruals — 5, 6, 7.
Question 4, Page 109	Preference dividends payable are included in 'Payables due within one year' on the TB and thus within trade payables in the Statement of Financial Position and do not need to be calculated for this question. Note 5 part (i) should read: Loan interest (12 months)
Question 6 page 113 **Question 7** **Page 115**	£1 per share is the nominal value of equity shares in questions 6 and 7.

Chapter 12	Statement of cash flows
Pro forma (questions)	The pro-formas as given in questions 1, 2, 4,and 5 are missing the following additional lines:

Missing line	**Question**
Impairment	1, 2, 4, 5.
Movement in accruals	2

Answer 5

Page 252

The following is a further breakdown of working 1, containing additional steps for clarification:

Working 1.1 LOAN (BORROWINGS)

Cash (bal. fig.)	516,000	B/fwd	472,000
C/fwd	556,000	PPE	600,000
	1,072,000		1,072,000

Working 1.2 REDEEMABLE PREFERENCE SHARES (BORROWINGS)

		B/fwd	0
C/fwd	150,000	Cash (bal. fig.)	150,000
	150,000		150,000

Working 1.3

Movement in borrowings:

Loan (from working 1.1)	516,000 (cash outflow)
Less: Preference shares (from working 1.2)	(150,000) (cash inflow)
Total cash outflow resulting from movement in borrowings	366,000

Notified Errata

Question bank

Chapter 11	Limited company financial statements
Answer 4, Page 220	Adjustment 10 from question 4 should result in an additional £9,000 cash and cash equivalents, and an additional £9,000 for trade payables. This affects the totals as shown below.

Cash and cash equivalents (15,477 + 9,000)	24,477
Total assets	168,806
Trade payables (49,809 + 9,000)	58,809
Total equity and liabilities	168,806

Answer 5 & 6

Page 223 &226

Please see revised marking schemes for Skylar Ltd and Corolla Ltd.

Skylar Ltd

Marking guide	Marks	
Revenue	1	
Cost of sales	2	
Distribution costs	1	
Administrative expenses	2½	
Finance costs	1	
Income tax	½	
Land and buildings	2	
Plant and equipment	2	
Inventories	1	
Prepayments	1	
Trade receivables	1½	
Cash and cash equivalents	1	
Share capital	½	
Retained earnings	1½	
Borrowings	1	
Trade payables	½	
Accruals	1	
Tax payable	½	
Warranty provision	1	
Total available	22½	
Maximum		16

Corolla Ltd

Marking guide	Marks
Revenue	½
Cost of sales	1½
Distribution costs	2
Administrative expenses	2½
Finance costs	1
Tax	½
PPE	2
Inventories	½
Receivables	1
Prepayments	1
Cash	½
Ordinary share capital	1
Retained earnings	1½
Loan	½

Payables	½	
Accruals	1	
Dividends	½	
Tax liabilities	½	
Total available	18½	
Maximum		16

Question 7

Page 115

The first line of adjustment 9 should read:

Ariel Ltd provides a warranty for certain lines of product. It is estimated that 1% of these warranties will be invoked at a cost of £25,000.

The pro-forma as given in question 7 shows land & buildings separate to plant & equipment. It should be combined to show a single line for property, plant & equipment.

Answer 7

Page 230

The c/fwd (balancing figure) in working 5 should be £4,779,000. The correct figure has been carried through to the answer.

Chapter 12 Statement of cash flows

Answer 1

Page 240

The final three lines of the solution should read:

Net increase/decrease in cash and cash equivalents	39,700
Cash and cash equivalents at beginning of period	(13,430)
Cash and cash equivalents at end of period	26,270

Answer 2

Page 242

The movement in accruals should read:

Movement in accruals (W12) (162,000)

Working 3 should read:

PROPERTY, PLANT AND EQUIPMENT – PROCEEDS FROM DISPOSALS

	£'000's		£'000's
PPE – Cost or valuation	1,201	PPE – acc dep (1,201 – 496)	705
Trade receivables	79	Statement of profit or loss	189
		Cash (bal. fig.)	221
		C/fwd	165
	1,280		1,280

Question 3

Page 135

The line for redeemable preference shares in the statement of financial position should read:

	20X2	20X1
Redeemable preference shares	200,000	

Note 5 should read:

Tam Ltd received £20,000 during the year from the sale of highly liquid investments, which are classed as cash equivalents.

Answer 3

Page 246

Working 1 should read:

SHARE CAPITAL

		B/fwd	1,000,000
		Share premium	50,000
C/fwd	1,100,000	Cash (bal. fig.)	50,000
	1,100,000		1,100,000

Question 5 **Page 139**	The line below trade receivables in the statement of financial position should read:

	20X5	20X4
Government bonds	105,000	100,000

The line below the loan in the statement of financial position should read:

	20X5	20X4
Preference Shares (redeemable)	150,000	0

The first line of note 4 should read:

An impairment review at 31 March 20X5 identified a fall in the recoverable amount of certain **non current** investments.

Answer 5

Page 252

Working 8 TRADE PAYABLES

Interest payable	5,000	B/fwd	289,600
		Investments	10,000
		Interest payable	10,000
C/fwd	348,500	Cash (bal.fig)	43,900
	353,500		353,500

Supplementary scenario-based question

Enercell Ltd

The trial balance for Enercell Ltd as at 31 October 20X7 is shown below.

	£'000	£'000
Share capital (£1 per share)		20,000
Share premium		2,500
Trade payables		5,022
Trade receivables	15,381	
Accruals		580
5% bank loan repayable in 10 years		30,000
Bank and cash	11,996	
Retained earnings		18,518
Interest	1,125	
Gross profit		39,539
Distribution costs	9,981	
Administrative expenses	5,478	
Dividends paid	1,950	
Closing inventories	18,000	
Property (freehold buildings) – cost	30,000	
Property (freehold buildings) – accumulated depreciation as at 1 November 20X6		3,750
Plant and equipment – cost	57,690	
Plant and equipment – accumulated depreciation as at 1 November 20X6		31,692
	151,601	151,601

Further information

1. There were no movements in non-current assets during the year. Plant and equipment is depreciated on a 10% straight line basis. Freehold buildings are depreciated over their useful life of 40 years. Depreciation is charged to administrative expenses.
2. The figure for closing inventories in the trial balance is the sales value (goods are sold at a mark-up of 25%). Inventory should be valued at cost of sales.
3. The company paid £72,000 insurance costs in June 20X7, which covered the period from 1 July 20X7 to 30 June 20X8. This was included in administrative expenses in the trial balance.
4. Interest on the bank loan for the last three months of the year has not been included in the trial balance.
5. The income tax charge for the year has been calculated as £1,881,000.
6. A customer was injured by a defective product during the year and has issued proceedings against the company. Enercell Ltd's legal team have advised that there is a 75% probability that this will result in an estimated payout of £750,000. Provisions are charged to administrative expenses.
7. Enercell Ltd hired additional warehouse space during the year for a period of 6 months, commencing on 1 August 20X7. The rent payable is £4,000 per month, no payments have been made to date. Rent is charged to distribution costs.
8. During the year, Enercell Ltd issued a 1 for 10 bonus share issue from share premium.
9. A cheque which was sent on 23 October 20X7 to a supplier for £32,000 was incorrectly recorded as £23,000.

Requirements

Prepare the income statement for Enercell Ltd for the year ended 31 October 20X7 and the statement of financial position at that date.

Income statement for the year ended 31 October 20X7

	£
Gross profit	
Distribution costs	
Administrative expenses	
Profit / (loss) from operations	
Finance costs	
Profit / (loss) before tax	
Income tax	
Profit / (loss) for year	

Statement of financial position at 31 October 20X7

	£
Non-current assets	
Property	
Plant and equipment	
Current assets	
Inventories	
Trade receivables	
Prepayments	
Bank and cash	
Total assets	
Equity	
Share capital	
Share premium	
Retained earnings	
Non-current liabilities	
Borrowings	
Current liabilities	
Trade payables	
Accruals	
Interest payable	
Tax payable	
Provision	
Total equity and liabilities	

Marking guide

		Marks
Gross profit	1	
Distribution costs	1	
Administrative expenses	2	
Finance costs	1	
Income tax	½	
Property	1½	
Plant & equipment	1½	
Inventories	1	
Trade receivables	½	
Prepayments	1	
Bank and cash	1	
Share capital	1	
Share premium	1	
Retained earnings	2	
Borrowings	½	
Trade payables	1	
Accruals	1	
Interest payable	½	
Tax payable	½	
Provision	½	
Total available	20	
Maximum		16

Enercell Ltd

Income statement for the year ended 31 October 20X7

	£'000
Gross profit (W1)	35,939
Distribution costs (W2)	(9,993)
Administrative expenses (W2)	(12,699)
Profit/(loss) from operations	13,247
Finance costs (5% x 30,000)	(1,500)
Profit/(loss) before tax	11,747
Income tax	(1,881)
Profit/(loss) for the period	9,866

Statement of financial position as at 31 October 20X7

	£'000
Assets	
Non-current assets	
Property (W3)	25,500
Plant and equipment (W3)	20,229
	45,729
Current assets	
Inventories (18,000 × 100/125)	14,400
Trade receivables	15,381
Prepayments (W2)	48
Bank and cash (11,996 – 9)	11,987
	41,816
Total assets	87,545

	£'000
Equity and liabilities	
Equity	
Share capital (W4)	22,000
Share premium (W4)	500
Retained earnings (W5)	26,434
Total equity	48,934
Non-current liabilities	
Borrowings (Bank loan)	30,000
Current liabilities	
Trade payables (5,022 – 9)	5,013
Accruals (580 + 12)	592
Interest payable ((30,000 × 5%) × 3/12)	375
Tax payable	1,881
Provision	750
	8,611
Total liabilities	38,611
Total equity and liabilities	87,545

Workings

1	Gross profit	39,539
	Change in inventory (18,000 – (18,000 × 100/125))	(3,600)
		35,939

2 **Administrative expenses**

	£'000
Administrative expenses	5,478
Freehold buildings depreciation charge (W3)	750
Plant and equipment depreciation charge (W3)	5,769
Prepayments - insurance (72 × 8/12)	(48)
Provision (see Note 6)	750
	12,699

Distribution costs

	£'000
Distribution costs	9,981
Rent accrual (4 × 3 months)	12
	9,993

3 **Property, plant and equipment**

	Freehold £'000	*Plant* £'000	*Total* £'000
Cost	30,000	57,690	
Acc dep''	(3,750)	(31,692)	
For year (30,000) ÷ 40) , (57,690 × 10%)	(750)	(5,769)	
Carrying amount	25,500	20,229	45,729

4 SHARE CAPITAL

	£'000		£'000
		B/d	20,000
C/d (bal fig.)	22,000	Bonus (share premium)	2,000
	22,000		22,000

SHARE PREMIUM

	£'000		£'000
Bonus issue	2,000	B/d	2,500
C/d (bal fig.)	500		
	2,500		2,500

5 RETAINED EARNINGS

	£'000		£'000
Dividends paid	1,950	B/d	18,518
C/d (bal fig.)	26,434	Profit for the year	9,866
	28,384		28,384

Glossary of terms

AVCO (average cost)	As purchase prices can change with each new consignment received, the average value of an item is constantly changing. Each item at any moment is assumed to have been purchased at the average price of all the items together, so inventory remaining is therefore valued at the most recent average price.
Accounting equation	ASSETS = CAPITAL + LIABILITIES.
Accruals (accrued expenses)	Expenses which are charged against the profit for a particular period, even though they have not yet been paid for.
Accruals basis of accounting	Items are recognised as assets, liabilities, equity, income and expenses (the elements of financial statements) when they satisfy the definitions and recognition criteria for those elements in the *Conceptual Framework*.
Accumulated depreciation	The total amount of the asset's depreciation that has been allocated to reporting periods to date.
Allowance for receivables	An amount in relation to specific debts that reduces the receivables asset to its prudent valuation in the statement of financial position. It is offset against trade receivables, which are shown at the net amount.
Appropriation of profit	Sharing out profits in accordance with the partnership agreement.
Asset	The *Conceptual Framework* states that an asset is a resource controlled by the entity as a result of past events from which future economic benefits are expected to flow to the entity.
Asset register	A listing of all non-current assets owned by the organisation, broken down by department, location or asset type, and containing non-financial information (such as chassis numbers and security codes) as well as financial information.
Bank reconciliation	A comparison of a bank statement (sent monthly, weekly or even daily by the bank) with the cash book. Differences between the balance on the bank statement and the balance in the cash book should be identified and satisfactorily reconciled.
Bank statement	A record of transactions on the business's bank account maintained by the bank in its own books.
Books of original entry	The records in which the business first records transactions.
Bonus issue (or capitalisation issue or scrip issue)	An issue of fully paid shares to existing shareholders, free of charge, in proportion to their existing shareholdings.
Business entity concept	The concept that financial accounting information relates to the activities of the business entity and not to the activities of its owner(s).
Capital	The *Conceptual Framework* states that capital is the residual interest in the assets of the entity after deducting all its liabilities.
Capital expenditure	Expenditure which results in the acquisition of long-term assets, or an improvement or enhancement of their earning capacity.
Capital income	Proceeds from the sale of non-current assets.
Carrying amount	Cost less accumulated depreciation.
Cash	Comprises cash on hand and demand deposits.

Cash book	The book of original entry for receipts and payments in the business's bank account.
Cash discount	A reduction in the amount payable in return for immediate payment in cash, or for payment within an agreed period. There are separate ledger accounts for cash discounts: one for discount allowed to customers, and one for discount received from suppliers.
Cash equivalents	Short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value (maturity of three months or less from the date of acquisition).
Cash flows	These are inflows and outflows of cash and cash equivalents.
Comparability	Accounting policies used should be disclosed, to make it possible for users to compare the company's results with its own prior years and with the results of other companies.
Contra	When a person or business is both a customer and a supplier, amounts owed by and owed to the person may be 'netted off' by means of a contra entry.
Control account	Nominal ledger account in which a record is kept of the total value of a number of similar individual items. Control accounts are used chiefly for trade receivables and payables.
Conversion costs	Any costs involved in converting raw materials into final product, including labour, expenses directly related to the product and an appropriate share of production overheads (but not sales, administrative or general overheads).
Cost of sales	Opening inventory + purchases + carriage inwards – closing inventory = cost of sales. This amount is then deducted from revenue to arise at the business's gross profit.
Credit note	A document issued to a customer relating to returned goods, or refunds when a customer has been overcharged for whatever reason. It can be regarded as a negative invoice. It is a source document for credit transactions.
Creditor	Person to whom a business owes money.
Current account	A record of the profits retained in the business by the partner.
Current asset	An asset is current when it is expected to be realised in, or intended for sale or consumption in, the entity's normal operating cycle, or it is held for being traded, or it is expected to be realised within 12 months of the date of the statement of financial position, or it is cash or a cash equivalent.
Current liabilities	Debts of the business that must be paid within one year, or within the entity's normal operating cycle, or that are held to be traded.
Debtor	Person who owes money to the business.
Depreciation	The systematic allocation of the cost of an asset, less its residual value, over its useful life.
Discount	A reduction in the price of goods below the amount at which those goods would normally be sold to other customers.
Discounts allowed	Prompt payment discounts allowed to customers who pay within a certain period of time from the invoice date.
Discounts received	Prompt payment discounts received from suppliers for payment made within a certain time period from the invoice date.
Double entry bookkeeping	Each transaction has an equal but opposite effect. Every accounting event must be entered in ledger accounts both as a debit and a credit.
Drawings	Money and goods taken out of a business by its owner.

Economic value	(EV), or value in use: what the existing asset will be worth to the company over the rest of its useful life.
Equity	The amount invested in a business by the owners (IAS 1 refers to 'owners' rather than 'equity holders' or 'shareholders').
Error of omission	Failing to record a transaction at all, or making a debit or credit entry, but not the corresponding double entry.
Error of principle	Making a double entry in the belief that the transaction is being entered in the correct accounts, but subsequently finding out that the accounting entry breaks the 'rules' of an accounting principle or concept. A typical example of such an error is to treat revenue expenditure incorrectly as capital expenditure.
Expenses	Decreases in economic benefits over a period in the form of outflows or depletion of assets, or increases in liabilities, resulting in decreases in equity/capital (*Conceptual Framework*). Expense is a key element of financial statements.
FIFO (first in, first out)	Items are used in the order in which they are received from suppliers, so oldest items are issued first. Inventory remaining is therefore the newer items.
Fair presentation	The faithful representation of the effects of transactions, other events and conditions in accordance with the *Conceptual Framework*.
Faithful representation	Information that is complete, neutral and free from errors, so that users can understand the nature and significance of what is presented.
Financial accounting	A method of reporting the results and financial position of a business.
General ledger	Ledger in which all asset, liability, capital, income and expense ledger accounts are kept. Also known as the nominal ledger.
Going concern concept	The assumption that the business will continue in operation for the foreseeable future. It is assumed that the entity has neither the intention nor the necessity of liquidation or of curtailing materially the scale of its operations.
Goodwill, purchased	The excess of the purchase consideration paid for a business over the fair value of the individual assets and liabilities acquired.
Gross profit	The profit from the trading activities of the business. Calculated as Sales less Cost of Sales.
Historical cost	Transactions are recorded at their cost when they occurred.
Income	Increases in economic benefits over a period in the form of inflows or increases of assets, or decreases of liabilities, resulting in increases in equity/capital (*Conceptual Framework*). It can include both revenue and gains. Income is a key element of financial statements.
Inventories	Assets: • Held for sale in the ordinary course of business • In the process of production for such sale; or • In the form of materials or supplies to be consumed in the production process or in the rendering of services.
Inventories, cost of	All costs of purchase, of conversion (eg labour) and of other costs incurred in bringing the items to their present location and condition.
Inventories, cost of purchase	The purchase price, import duties and other non-recoverable taxes, transport, handling and other costs directly attributable to the acquisition of finished goods and materials.
Irrecoverable debt	A debt which is not expected to be paid.

LIFO (last in, first out)	Items issued originally formed part of the most recent delivery, while oldest consignments remain in stores. This is disallowed under IAS 2 *Inventories*.
Liability	The *Conceptual Framework* states that a liability is a present obligation arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits. Liabilities are key elements of financial statements.
Loss	The excess of expenses over income.
Management accounting	Sometimes known as cost accounting, is a management information system which analyses data to provide information as a basis for managerial action.
Material	Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or the nature of an item, or a combination of both, could be the determining factor.
Net assets	Assets less liabilities.
Net realisable value	The expected price less any costs still to be incurred in getting the item ready for sale and then selling it.
Nominal ledger	Ledger in which all asset, liability, capital, income and expense ledger accounts are kept. Also known as the general ledger.
Non-current assets	Assets acquired for continuing use within the business, with a view to earning income or making profits from their use, either directly or indirectly, over more than one reporting period.
Non-current liability	A debt which is not payable within one year. Any liability which is not current must be non-current.
Partnership	The relationship which exists between persons carrying on a business in common with a view of profit.
Payables ledger	The memorandum ledger for suppliers' personal accounts. It is not part of the nominal ledger nor part of the double entry system, but double entry rules apply to the payables ledger accounts.
Payroll	The book of original entry for recording staff costs.
Petty cash book	The book of original entry for small payments and receipts of cash.
Prepayments (prepaid expenses)	Expenses which have been paid in one reporting period, but are not charged against profit until a later period, because they relate to that later period.
Profit	The excess of income over expenses.
Provision	A liability of uncertain timing or amount.
Purchase day book	The book of original entry in respect of credit purchases.
Purchase returns day book	A listing of all credit notes received from credit suppliers. Sometimes known as the purchases returns journal.
Receivables ledger	The memorandum ledger for customers' personal accounts. It is not part of the nominal ledger nor the double entry system, but double entry rules apply to the receivables ledger accounts.
Reducing balance depreciation	The annual depreciation charge is a fixed percentage of the brought forward carrying amount of the asset.
Relevant financial information	Information which is capable of making a difference in the decisions made by users.

Replacement cost	The cost of an inventory unit is assumed to be the amount it would cost now to replace it. This is often (but not necessarily) the unit cost of inventories purchased in the next consignment *following* the date of the statement of financial position.
Residual value	The estimated amount that the entity would currently obtain from disposing of an asset, after deducting estimated disposal costs.
Retained earnings	A reserve used to accumulate the company's retained earnings.
Revenue	The gross inflow of economic benefits during the period arising in the course of the ordinary activities of an entity when those flows result in increases in equity, other than increases relating to contributions from equity participants.
Revenue expenditure	Expenditure which is incurred either: • For trade purposes. This includes purchases of raw materials or items for resale, expenditure on wages and salaries, selling and distribution expenses, administrative expenses and finance costs, or • To maintain the existing earning capacity of long-term assets.
Revenue income:	Income derived from • The sale of trading assets, such as goods held in inventory • The provision of services • Interest and dividends received from business investments
Rights issue	New shares are offered to existing owners in proportion to their existing shareholding, usually at a discount to the current market price.
Sales day book	The book of original entry in respect of credit sales.
Sales returns day book	A listing of all credit notes sent out to credit customers. Sometimes known as the sales returns journal.
Standard cost	All inventory items are valued at a pre-determined cost. If this standard cost differs from prices actually paid during the period the difference is written off as a 'variance' in the statement of profit or loss.
Statement of changes in equity	Financial statement that shows the changes in owners' equity (capital) invested in a business during the period.
Statement of financial position:	A *list* of all the *assets controlled* and all the *liabilities owed* by a business as at a particular date: it is a snapshot of the financial position of the business at a particular moment. Monetary amounts are attributed to assets and liabilities. It also quantifies the amount of the owners' interest in the company: **equity**.
Statement of profit or loss	A statement displaying items of income and expense in a reporting period as components of profit or loss for the period. The statement shows whether the business has had more income than expense (a profit for the period) or *vice versa* (a loss for the period).
Statutory accounts	Financial statements which limited companies are obliged by law to publish in a particular form.
Straight line depreciation	The depreciable amount (cost less residual value) is charged in **equal instalments** to each reporting period over the expected useful life of the asset. (In this way, the carrying amount of the non-current asset declines at a steady rate, or in a 'straight line' over time.)
Suspense account	An account showing a balance equal to the difference in a trial balance.
Timeliness	Financial information should be available in time to be capable of influencing users' decisions.

Trade discount	A reduction in the cost of goods, owing to the nature of the trading transaction. It usually results from buying goods in bulk. It is deducted from the list price of goods sold, to arrive at a final sales figure. There is no separate ledger account for trade discount.
Trade payables	The amounts due to credit suppliers. Also known as trade accounts payable or simply payables.
Trade receivables	The amounts owed by credit customers. Also known as trade accounts receivables or simply receivables.
Transposition errors	When two digits in an amount are accidentally recorded the wrong way round.
Trial balance	A list of nominal ledger balances shown in debit and credit columns, as a method of testing the accuracy of double entry bookkeeping. The trial balance is not part of the double entry system.
UK GAAP	The rules, from whatever source, that govern accounting and financial reporting in the UK.
Understandability	Financial information needs to be capable of being understood by users 'having a reasonable knowledge of business and economic activities and accounting'.
Useful life	The estimated economic life (rather than the potential physical life) of the non-current asset.
Verifiability	Information is verifiable if different observers can broadly agree that a particular way of presenting an item is a faithful representation.
Writing off (debt)	Charging the cost of the debt against the profit for the period.

Mock exam guidance notes

Suggested structure for Accounting mock exam

Exam standard

The mock exam should be set at the same level represented as the 2016 sample papers on the ICAEW website.

Exam format

The mock exam should consist of one scenario-based question worth 40% of the total marks, and 24 objective test questions worth 2.5 marks each.

Style of exam questions

1. The scenario-based questions will involve either:
   (a) Preparing a statement of profit or loss and statement of financial position from a trial balance and additional information, or
   (b) Producing a statement of cash flows from a statement of profit or loss, statements of financial position and additional information.
2. Each objective test question should conform to the style used in the sample paper i.e.:
   - Multiple choice questions (1 from 4), or
   - Multiple response (more than 1 from 4 or more)
   - Plcs use IFRS terminology
   - Ltds and unincorporated businesses use UK GAAP terminology
   - No negative questions
3. There should be 2-4 non-numerical, 'knowledge' type questions.

Exam coverage and balance

A mock exam should have roughly the syllabus coverage and balance set out in the table below.

The objective test questions should be chosen after the scenario-based question to ensure an appropriate balance of topics.

Syllabus area	Weighting (%)	No. of Questions
1 Maintaining financial records	30	9-11
2 Adjustments to accounting records and financial statements	35	8-11
3 Preparing financial statements	35	4-6
Total	**100**	**25**

A good mock might contain the following balance of questions (this example is for an exam where the scenario-based question involves preparing an income statement and statement of financial position from a trial balance and additional information).

Note the question topics listed here are only examples of the nature of questions which may be included – the actual exam questions may be on different topics.

Q number	Syllabus ref	Example
1	1a	Conceptual Framework
2	1a	IAS 1 (revised)
3	1b	Day books/source documents
4	1c	Inventory valuation (FIFO or AVCO; cost v. NRV)
5	1c	VAT/payroll
6	1c	Calculation of balances/Double entry (eg for disposal of NCA)
7	1c	Calculation of balances/Double entry (eg for accruals/prepayments)
8	1d	Double entry (eg share issue)
9	1d	Unincorporated business capital account
10	1e	Trial balance/suspense account
11	2a	Identify error/omission in double entry
12	2b	Correction of error using suspense account
13	2b	Bank reconciliation
14	2b	Payables control reconciliation
15	2b	Receivables control reconciliation
16	2c	ETB adjustments
17	2d	Nominal ledger entry journal
18	2d	Error correction journal
19	2d	Error correction journal
20	2d	Error correction journal
21	3a	Accounting for partnerships
22	3b	Accruals v. cash accounting
23	3b	Accounting concepts/principles including going concern
24	3c	Reconciliation of profit from operations to cash flow from operations

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