

A Level Accounting Summer Independent Learning Activity

Sources of Finance

Welcome to A Level Accounting! As part of your studies in this subject, you need to learn about **sources of finance**.

A 'source of finance' is a place from where a business obtains the money (also known as 'capital') to operate.

You are expected to know about the following sources of finance: owner's capital (owner's savings); partners' capital; bank overdraft; bank loan; mortgage; ordinary shares; debentures

For each source of finance above, you'll need to know a definition, the features of the source of finance, and the advantages and disadvantages each source of finance to the business.

Task 1

Open up a word document and create a table like the one below. Using the links over the page, complete the table for **each** source of finance. These should then be **printed and brought to your first class** when you begin college in **September**.

Type of finance: Owner's Capital		
Definition/ general description		
	Advantages	Disadvantages

A general introduction to sources of finance

<http://www.bbc.co.uk/education/guides/zmj7tfr/revision/1>

Owner's capital & partners' capital

<https://www.tutor2u.net/business/reference/finance-personal-sources-of-finance-for-a-startup>

<https://www.tutor2u.net/business/reference/organisation-partnerships>

Bank Overdraft & Bank Loan

<https://www.tutor2u.net/business/reference/sources-of-finance-bank-overdraft>

<https://www.tutor2u.net/business/reference/sources-of-finance-bank-loans>

Ordinary shares

<https://www.tutor2u.net/business/reference/finance-introduction-to-raising-equity-finance>

Debentures

<https://www.tutor2u.net/business/reference/debentures>

<https://www.tutor2u.net/business/blog/sources-of-finance-debentures-in-action>

Task 2

Once you've got the required knowledge of each source of finance, the key skill you need is the ability to compare and contrast different sources of finance, in order to decide whether that particular source will benefit the business or not. A popular comparison is between money from shares (share capital) and money that comes from loans or debentures (loan capital)

Using the information from task 1, Analyse (explain) the differences, and similarities between loan and share capital. Make a judgement as to which you think is best for a business. Bring this to your lesson in September.

Income Statements

Businesses have to complete an income statement. An income statement is a financial statement which must be produced every year, that shows the total sales and expenses a business has and whether it is making a profit or a loss.

Please follow the link to the attached Powerpoint presentation showing the purpose and layout of an income statement.

<https://ncpontefract.ac.uk/wp-content/uploads/2021/07/NCB-Y11-Y12-A-level-Accounting-SIL-ppt-2021-2.pptx>

If the link above does not work you will find the PPT slides on pages 6 -17 of this document for you to view.

Task 1

- Learn the layout of the income statement on slide 5 of the powerpoint presentation
- Learn the key terms (see slide 6)
- Learn the formulae (slide 8)
- Work through the Matthew Lloyd worked example on the powerpoint (slides 12, 13, 14)

Once you have completed task 1, you should now be in a position to complete the following tasks, 2, 3 and 4.

Task 2

You are to fill in the missing figures for the following businesses:

	Revenue	Opening Inventory	Purchases	Closing Inventory	Cost of Sales	Gross Profit	Expenses	Profit/ (Loss) for the year
	£	£	£	£	£	£	£	£
Business A	20 000	5 000	10 000	3 000			4 000	
Business B	35 000	8 000	15 000	5 000				10 000
Business C		6 500	18 750	7 250		18 500	11 750	
Business D	45 250	9 500		10 500		20 750		10 950
Business E	71 250		49 250	9 100		22 750	24 450	
Business F	25 650	4 950	13 750			11 550		(3 450)

Task 3

The following balances have been recorded by the bookkeeper of John Adams at 31st December 2017.

	£	£
Inventory at 1 st January 2017 (opening inventory)	14 350	
Purchases	114 472	
Revenue (Sales)		259 688
Office rent	13 718	
Heating and Lighting	12 540	
Wages and Salaries	42 614	
Vehicle Expenses	5 817	
Advertising	6 341	

Inventory at 31st December 2017 is valued at £16 280 (closing inventory)

You are to prepare the Income Statement of John Adams for the year ended 31st December 2017.

Task 4

The following balances have been recorded by the bookkeeper of Clare Lewis as at 31st December 2018.

	£	£
Revenue (Sales)		144 810
Purchases	96 318	
Inventory at 1 st January 2018 (Opening inventory)	16 010	
Salaries	18 465	
Heating and Lighting	1 820	

Rent and Business rates	5 647	
Sundry Expenses	845	
Vehicle Expenses	1 684	

Inventory at 31st December 2018 (Closing inventory) is valued at £13 735.

You are to prepare the Income Statement of Clare Lewis for the year ended 31st December 2018

Profitability Ratios

A business uses the income statement to analyse its progress by comparing its performance from one year to the last. It can then see whether it is improving, by making more profit, or deteriorating by making less profit. This analysis helps the business to make decisions.

It does this by calculating some ratios. See slide 17

Task 5

Learn the profitability ratios

Task 6

Using the income statement created for Clare Lewis, calculate the following profitability ratios:

- I. Gross profit margin
- II. Gross profit mark up
- III. Expenses in relation to revenue
- IV. Profit in relation to revenue

Bring your work for tasks on sources of finance and income statements, tasks 2, 3, 4 and 6 to college on your first day

Good luck and see you soon

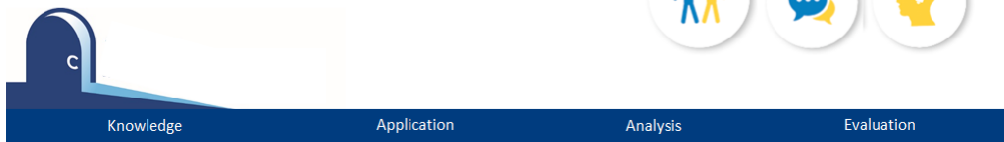
The Accounting Team at New College Learning Trust

Slide 2

By the end of these tasks...

- You will be able to define and explain the purpose of an income statement
- You will know the layout of an income statement and what to include within the statement.
- You will be able to make calculations to include in an income statement
- **Challenge**
- You will be able to calculate profitability ratios to analyse business performance

OPTIC



Slide 3

Introduction to Income Statements

- The main activity of a trading business is to buy goods at one price and sell the same goods at a higher price. The difference between the two prices represents a profit known as **gross profit**. The gross profit for each item is totalled to show one figure.
- At the end of the financial year, the business needs to produce an income statement, showing the trading of the business and showing the gross profit for the year.



Slide 4



- As a student, you need to know the layout of the income statement
- The layout of the income statement is as follows:

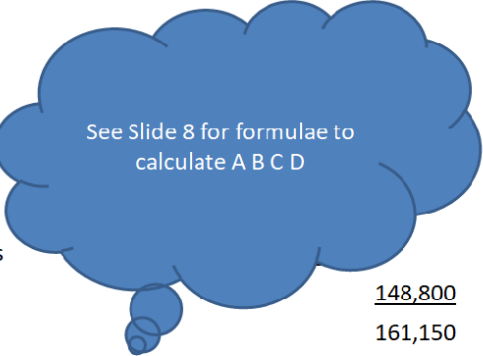


Slide 5



Income Statement for Wyvern Wholesalers
For the Year Ended 31 December 20-1

	£	£	£
Sales (Revenue)			250,000
Less Sales Returns			<u>5,400</u>
Net Revenue (A) NB1			244,600
Opening Inventory (1			
Purchases			
Carriage In			
Less Purchase Returns			
Net Purchases (B) NB2		<u>148,800</u>	
		161,150	
Less Closing Inventory (31 December 20-1		<u>16,300</u>	
Cost of Sales (C) NB3			<u>144,850</u>
Gross Profit (D) NB4			99,750



Slide 6

Key Terms

- **Revenue** – money coming into the business from sales
- **Purchases** – only include items that the business trades with; sells on.
- **Inventory** – these are the goods that the business has in stock
- **Cost of Sales** – cost to the business of the goods which have been sold in the financial year
- **Carriage in** – the expense to the business of having purchases delivered



Slide 7

- With viewing slide 5, certain calculations need to be carried out.
- To calculate A B C D see the next slide



Slide 8

Formulae

<p>Cost of Sales (C) Opening inventory + Purchases + Carriage in - Purchase Returns - Closing inventory = Cost of Sales</p>	<p>Gross Profit (D) Revenue - Sales Returns = Net Revenue - Cost of Sales = Gross Profit or Loss</p>
<p>Net Revenue or Turnover (A) Revenue (Sales) - Sales Returns = Net Revenue</p>	<p>Net Purchases (B) Purchases + Carriage In - Purchase Returns = Net Purchases</p>



Knowledge

Application

Analysis

Evaluation

Slide 9

Profit for the Year

- Obviously, businesses have many other costs other than buying goods to sell on. They need premises, electricity, salaries and insurance, etc.
- We now need to include these expenses on the income statement by subtracting them from the gross profit



Knowledge

Application

Analysis

Evaluation

Slide 10

Income Statement for Wyvern Wholesalers		£
For the year ended 31 December 20-1		
		99,750
		<u>2,500</u>
		102,250
Less Expenses		
Discount allowed	3,700	
Salaries	46,000	
Electricity and Gas	3,000	
Business Rates	2,000	
Subtotal	<u>4,700</u>	
		<u>59,400</u>
Profit for the year		<u>42,850</u>

Total Expenses = 3,700 + 46,000 + 3,000 + 2,000 + 4,700 = 59,400
 102,250 – total expenses 59,400 = profit for the year of 42,850

Slide 11



Example

The following 3 slides show you how to create an income statement




Slide 12

The following information has been extracted from the business accounts on Matthew Lloyd from his first year of trading which ended on 31st December 2018. (** there is no opening inventory! **)

	£	£
Purchases	94 350	
Revenue (Sales)		125 890
Inventory at 31 st December 2018 (Closing Inventory)	5 950	5 950
Office Rent	4 850	
Heating and Lighting	2 120	
Wages and Salaries	10 350	
Office Equipment	8 500	

You are to prepare the Income Statement of Matthew Lloyd for the year ended 31st December 2018.

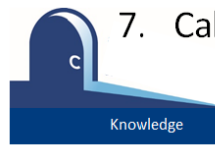


Knowledge
Application
Analysis
Evaluation

Slide 13

Steps to complete the Income Statement

1. Include the title showing the business name, statement name and date the financial statement ends (as slide 5)
2. Layout the income statement as shown on slides 5 and 10
3. Insert the figures (from slide 12)
4. Calculate cost of sales (from slide 8)
5. Calculate gross profit (from slide 8)
6. Add up total expenses (from slide 10)
7. Calculate profit for the year (from slide 10)



Knowledge
Application
Analysis
Evaluation

Slide 14

Answer - Checkpoint

MATTHEW LLOYD
INCOME STATEMENT FOR YEAR ENDED 31 DECEMBER 2018

	£	£
Revenue		125,890
Opening Inventory	-	
Purchases	94,350	
Less Closing Inventory	5,950	
Cost of Sales		88,400
Gross Profit		37,490
Less Expenses:		
Office Rent	4,850	
Heating and Lighting	2,120	
Wages and Salaries	10,350	
		17,320
Profit for the Year		20,170

Knowledge

Application

Analysis

Evaluation

Slide 15

Now go to the SIL document and complete tasks
2 3 and 4

Knowledge

Application


Analysis

Evaluation

Slide 16

Profitability Ratios

- A business uses the income statement to analyse its progress by comparing its performance from one year to the last. It can then see whether it is improving, by making more profit, or deteriorating by making less profit. This analysis helps the business to make decisions.



It does this by calculating some ratios

Knowledge

Application

Analysis

Evaluation

Slide 17

Using our Example – Matthew Lloyd

Gross Profit Margin

$$\frac{\text{Gross Profit}}{\text{Revenue}} \times 100 = \frac{37,490}{125,890} \times 100 = 29.78\%$$

This shows that for every £1 of revenue coming into the business, it make over 29p in gross profit. The higher the figure the better.



Knowledge Application Analysis Evaluation

Slide 18

Profitability Ratios

<p>Gross Profit Margin</p> <p>$\frac{\text{Gross Profit}}{\text{Revenue}} \times 100$</p> <p>The higher the percentage the better</p>	<p>Gross Profit Mark Up</p> <p>$\frac{\text{Gross Profit}}{\text{Cost of Sales}} \times 100$</p> <p>A margin of 25% means for every £100 of purchases made, the business makes £25 gross profit</p>
<p>Expenses in relation to Revenue</p> <p>$\frac{\text{Expenses}}{\text{Revenue}} \times 100$</p>	<p>Profit in relation to Revenue</p> <p>$\frac{\text{Profit for the Year}}{\text{Revenue}} \times 100$</p> <p>The higher the better</p>

Knowledge	Application	Analysis	Evaluation
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Slide 19



Gross Profit Mark Up

$$\frac{\text{Gross Profit}}{\text{Cost of Sales}} \times 100 = \frac{37,490}{88,400} \times 100 = 42\%$$

A margin of 42% means for every £100 of purchases made, the business makes £42 gross profit



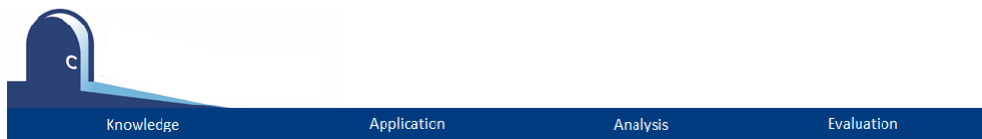
Knowledge	Application	Analysis	Evaluation
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Slide 20

Expenses in relation to Revenue

$$\frac{\text{Expenses}}{\text{Revenue}} \times 100 = \frac{17,320}{125,890} \times 100 = 14\%$$

For every £1 of revenue, the business spends
14p on expenses



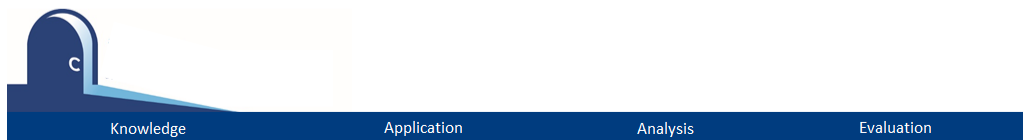
Slide 21

Profit in relation to Revenue

$$\frac{\text{Profit for the Year}}{\text{Revenue}} \times 100$$

$$\frac{20,170}{125,890} \times 100 = 16\%$$

Shows the percentage of profit made after all
expenses have been considered



- Now complete the last task on the SIL sheet
- Bring your work for tasks on sources of finance and income statements, tasks 2, 3, 4 and 6 to college on your first day



Good luck and see you soon

The Accounting Team at New College
Learning Trust



Knowledge

Application

Analysis

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